No. 09-525

IN THE

Supreme Court of the United States

JANUS CAPITAL GROUP, INC, AND
JANUS CAPITAL MANAGEMENT, LLC,

Petitioners,

v.

FIRST DERIVATIVE TRADERS,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF *AMICUS CURIAE*[1]

The Chamber of Commerce of the United States of America ("Chamber") is the world's largest business federation. The Chamber represents 300,000 direct members and indirectly represents the interests of more than three million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae* briefs in cases that raise issues of concern to the nation's business community, such as cases involving the federal securities laws, including *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008), *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308 (2007), and *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005).

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[1] Pursuant to this Court's Rule 37.6, *amicus curiae* affirms that no counsel for any party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae*, its members or its counsel made a monetary contribution to its preparation or submission.

Pursuant to Rule 37.3, *amicus curiae* states that petitioner and respondent have consented to the filing of this brief, and copies of their letters of consent are on file with the Clerk's Office.

The Fourth Circuit, in its decision below, held that a service provider who participates in drafting or supervising an allegedly misleading statement could be liable under §10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), and SEC Rule 10b-5(b), 17 C.F.R. § 240.10b-5, if investors "would attribute to the [service provider] *a substantial role in preparing or approving the allegedly misleading statement*" — a determination that would have to made on "*a case-by-case basis*." Pet. App. at 24a (emphasis added). The Fourth Circuit also held that a service provider could be deemed to have "made" a false statement based on its "participat[ion] in the writing and dissemination" of the statement, even though the statement was not publicly attributed to the service provider. *Id.* at 18a.

The Fourth Circuit's decision blurs the distinction between secondary actors who participate behind the scenes in preparing or approving statements and primary actors — typically issuers and certain of their corporate officers — to whom such statements are publicly attributed. This decision contradicts the holding of *Stoneridge* because it would significantly extend the implied private right of action under §10(b) and Rule 10b-5(b) to reach whole categories of defendants — lawyers, accountants, investment bankers, and other service providers — who have traditionally been deemed to be at most aiders and abettors, not primary violators.

Moreover, extending primary liability under §10(b) would put U.S. businesses at a significant

competitive disadvantage as issuers would have to indemnify these new classes of defendants against class action litigation costs. It would thereby increase the cost of raising capital on U.S. exchanges, thus discouraging businesses from raising capital in the U.S. This would diminish capital raising when our economy is most in need of that. And it would impede efforts to maintain the U.S. as the leading global financial center in increasingly competitive markets.

INTRODUCTION AND SUMMARY OF ARGUMENT

In *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994), and again in *Stoneridge*, the Court limited the scope of implied private action liability under §10(b). Both times, the Court declined to extend the implied right of action and subject secondary actors to amorphous and ill-defined theories of §10(b) liability. In contravention of *Central Bank* and *Stoneridge*, the Fourth Circuit's decision does exactly that. The Fourth Circuit's test extends §10(b) liability to anyone who "substantially" participates in drafting, preparing, or approving a misstatement even if the misstatement is publicly attributed to someone else. This expands the §10(b) implied private right of action to secondary actors in a way that this Court has repeatedly declined to do. By requiring lower courts to conduct a fact-intensive, "case-by-case" determination as to whether a given secondary actor's participation is "substantial" enough to warrant a

finding of primary liability, the Fourth Circuit's test would guarantee inconsistency in its application and outcome and foster uncertainty and unpredictability that would injure our financial markets.

The Court should reject this expansion in favor of a bright line rule, such as that adopted by the majority of federal appellate courts, which makes clear to all market participants that "those who sign or otherwise allow a statement to be attributed to them expose themselves to liability," while those who do not sign "are beyond the reach of Rule 10b-5's private right of action." *Pac. Inv. Mgmt. Co. v. Mayer Brown LLP*, 603 F.3d 144, 155 (2d Cir. 2010). A bright line rule is easier for district courts to apply, avoids protracted litigation, and avoids "discovery aimed at learning the identity of each person or entity that had some connection, however tenuous, to the creation of an allegedly false statement." *Id.* at 157.

1. The Court should reject the test adopted by the Fourth Circuit and decline to expand the implied right of action under §10(b) for numerous reasons.

First, *Stoneridge* held that the implied right of action should not be extended by the Court beyond "its present boundaries" as of 1995 when the Private Securities Litigation Reform Act of 1995 (the "PSLRA") was enacted. *Stoneridge*, 552 U.S. at 165. Those boundaries did not include implied private liability for those who participated in drafting false and misleading statements. The implied right of

action under §10(b) should not be extended when Congress declined to do so in 1995 and again in 2010. *Second*, extending the §10(b) implied right of action to cover those who merely participate in drafting or approving a misstatement is incompatible with the element of defendant-by-defendant reliance required by *Central Bank* and *Stoneridge*. *Third*, such an extension of implied private §10(b) liability is also incompatible with the defendant-by-defendant loss causation expressly required by the PSLRA. *Fourth*, the expansion proposed by the Fourth Circuit would inject considerable uncertainty into an area of the law where predictability and certainty are needed. And *fifth*, the Fourth Circuit's expansion, by extending class action liability to categories of financial market participants, such as accountants, lawyers, and investment bankers, who have traditionally been treated as at most aiders and abettors, would raise the cost of raising capital on domestic exchanges and deter issuers from listing their securities in the United States.

2. Independently, the Court should also reject the Fourth Circuit's holding that one who participates in drafting or disseminating a false statement can be deemed to have "made" the statement for numerous reasons.

First, the Fourth Circuit's holding cannot be squared with the text of Rule 10(b)-5(b), which limits liability to those who "make" a false or misleading statement or omission. *Second*, the Fourth Circuit's

decision includes within the "maker" category those who merely "participate" in drafting or disseminating another's false statement, thereby extending the private right of action to aiders and abettors in contravention of *Central Bank*. *Third*, the Fourth Circuit's decision contravenes settled law that one who does not speak cannot be liable under §10(b) absent a duty to speak. And *fourth*, the Fourth Circuit's decision would impose liability not just on those who "make," but on those who "cause to be made" false or misleading statements. Congress knew how to reach this broader group of defendants when it wished to do so. This is evidenced by §18(a) of the 1934 Act, which provides an express cause of action if, but only if, a plaintiff actually relies on a defendant who "shall make or cause to be made" a false or misleading statement in any report or document filed pursuant to the 1934 Act. 15 U.S.C. §78r. The SEC did not include "cause to be made" language in Rule 10b-5(b), and the courts should not rewrite the Rule to add it.

ARGUMENT

I. PRIMARY LIABILITY UNDER §10(b) SHOULD NOT BE EXPANDED TO SECONDARY ACTORS TO WHOM NO FALSE OR MISLEADING STATEMENTS ARE PUBLICLY ATTRIBUTED.

A. The Court Should Defer To Congress' Decision Not To Expand Primary Liability To Secondary Actors To Whom No False Or Misleading Statements Are Publicly Attributed.

The private right of action under §10(b) and Rule 10b-5 is a "judicial construct that Congress did not enact in the text of the relevant statutes." *Stoneridge*, 552 U.S. at 164 (citation omitted); *see also Lampf, Pleva, Lipkin, Prupis & Pettigrow v. Gilbertson*, 501 U.S. 350, 359 (1991) ("[W]e have made no pretense that it was Congress' design to provide the remedy afforded."). As this Court held in *Stoneridge*, "[t]he decision to extend the implied cause of action is for Congress," not for the courts. 552 U.S. at 165*; see also Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1102 (1991) ("[T]he breadth of the [implied private] right once *recognized should not, as a general matter, grow beyond the scope congressionally intended.*") (emphasis added).[2]

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[2] *Cf.* 501 U.S. at 1110 (Scalia, J., concurring) ("[When] the federal cause of action at issue here was never enacted by

Accordingly, *Stoneridge* held that the implied private right of action under §10(b) should not be extended by the courts beyond the "boundaries" in place when the PSLRA was enacted in 1995. 552 U.S. at 165-66. "The decision to extend the cause of action is for Congress, not for us. . . . It is appropriate for us to assume that when [the PSLRA] was enacted, Congress accepted the §10(b) private cause of action as then defined but chose to extend it no further."[3] *Id.*

Stoneridge illustrates the Court's general approach not to extend implied private rights of action. The Court has consistently declined to extend existing implied rights of action. *See, e.g.*, *Wilkie v. Robbins*, 551 U.S. 537, 562 (2007) (no private *Bivens* action against Bureau of Land Management

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Congress . . . the more narrow we make it (within the bounds of rationality) the more faithful we are to our task.") (citation omitted).

[3] The *stare decisis* effect of *Stoneridge* extends to its rationale, and not merely to its narrow result. *See Carey v. Musladin*, 549 U.S. 70, 79 (2006) (*stare decisis* includes "explanatory language" for the Court's ruling even if "such guidance . . . may not have been strictly necessary as an explanation of the Court's specific holding"); *Seminole Tribe of Florida v. Florida,* 517 U.S. 44, 67 (1996) ("When an opinion issues for the Court, it is not only the result but also the portions of the opinion necessary to that result by which we are bound."); *County of Allegheney v. ACLU Greater Pittsburgh Chapter*, 492 U.S. 573, 668 (1989) (Kennedy, J., concurring and dissenting) ("As a general rule, the principle of *stare decisis* directs us to adhere not only to the holdings of our prior cases, but also to their explications of the governing rules of law.").

employees alleged to have used harassment and intimidation in attempt to force owner to grant easement); *Gonzaga Univ. v. Doe*, 536 U.S. 273, 287-91 (2002) (no private right of action created by nondisclosure provisions in Family Educational Rights and Privacy Act); *Alexander v. Sandoval*, 532 U.S. 275, 293 (2001) (no private right of action to enforce disparate-impact regulations promulgated under Title VI of Civil Rights Act of 1964).

When the PSLRA was enacted, the §10(b) implied private right of action had not been extended to those who merely participate in drafting an alleged misstatement. *See Central Bank*, 511 U.S. at 177 ("[T]he statute prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act."); *Shapiro v. Cantor*, 123 F.3d 717, 720 (2d Cir. 1997) ("Allegations of 'assisting,' 'participating in,' 'complicity in' and similar synonyms . . . all fall within the prohibitive bar of *Central Bank*."). Under *Stoneridge*, that should be the end of the matter.

Moreover, any extension of the implied private right of action to those who participate in drafting would interfere with the "deliberate congressional choice" — at least twice — to "impose some forms of secondary liability, but not others" under the federal securities laws. *Central Bank*, 511 U.S. at 184. In 1994, Congress was urged to overturn *Central Bank* and extend the §10(b) private right of action. *See, e.g.*, *Abandonment of the Private Right of Action for*

Aiding and Abetting Securities Fraud/Staff Report on Private Securities Litigation: Hearing before the Subcomm. on Secs. of the S. Comm. on Banking, Hous. & Urban Affairs, 103d Cong. 14 (1994) (statement of Arthur Levitt, Chairman, SEC) ("Legislation is also needed to restore aiding and abetting liability in private actions which are a necessary supplement to [the SEC's] overall enforcement program."). In particular, then-SEC Chairman Levitt urged Congress to extend §10(b) private damages liability to defendants who "act behind the scenes and do not themselves make statements." *Securities Litigation Reform: Hearings before the Subcomm. on Telecomms. & Fin. of H. Comm. on Energy and Commerce*, 103d Cong. 35 (1994) (testimony of Arthur Levitt, Chairman, SEC). However, Congress declined to extend the boundaries of the §10(b) action because doing so "would be contrary to [the PSLRA's] goal of reducing meritless securities litigation." S. Rep. No. 104-98, at 19 (1995), *reprinted in* 1995 U.S.C.C.A.N. 679, 698.

In *Stoneridge*, the Court deferred to Congress' determination, recognizing that, when the PSLRA was enacted, "Congress accepted the §10(b) private cause of action *as then defined but chose to extend it no further*." 522 U.S. at 166 (emphasis added). The Court held that, in light of concerns with the expansion of judge-made implied rights of action, "the §10(b) private right [of action] should not be extended beyond its present boundaries." *Id.* at 165. *Stoneridge* properly has been understood to stand for

the proposition that "§10(b) liability should remain narrow and limited to its current contours." *Malack v. BDO Seidman, LLP*, No. 09-4475, 2010 WL 3211088, at *9 (3d Cir. Aug. 16, 2010).

Stoneridge's rationale of not extending the §10(b) implied right of action is even sounder today. This is because recently, when Congress enacted the Dodd-Frank Act, it declined to overturn *Central Bank* and *Stoneridge* and provide an expanded private right of action. Congress was repeatedly urged to do so. *See, e.g., Evaluating S. 1551: The Liability for Aiding and Abetting Securities Violations Act of 2009: Hearings Before the Subcomm. on Crime & Drugs of the S. Comm. on the Judiciary,* 111th Cong. 2 (2009) (statement of John C. Coffee, Jr., Adolf A. Berle Professor of Law, Columbia Univ. School of Law) ("[T]he Federal Securities laws . . . since 1994, do not permit the victim [of securities fraud] to sue the aider and abetter [sic] even if there is conscious, knowing assistance given to the primary violation. Now, it is time to reevaluate that."). An early draft of the Senate bill contained a provision that would have extended §10(b) liability to those who "provide substantial assistance" to another person in violation of the Exchange Act. S. ___, 111th Cong. §984 (draft dated Nov. 19, 2009). That provision was not included in the bill presented to the full Senate on April 10, 2010. S.3217, 111th Cong. (draft dated Apr. 15, 2010). On May 3, 2010, during the Senate floor debate on the bill, Senator Arlen Specter submitted amendment SA 3776 which would have explicitly

overturned *Stoneridge and Central Bank.*[4] That amendment was withdrawn on May 20, 2010, (111 CONG. REC. 4077 (2010)), however, and was not included in the Senate's final version of the bill.

Following Senate passage of the bill, the House-Senate conference considered yet another proposed amendment that would have included a private right of action against those who substantially assist a §10(b) violation. Susan E. Hurd & Elizabeth P. Skola, *Still No Aiding and Abetting Liability Provision*, LAW360 (July 28, 2010), http://www.law360.com/print_article/181906. That amendment was rejected, however. *Id.* Instead, the 848-page final Act contains a provision that requires the Comptroller General to perform a study, to be

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[4] Specifically, the amendment would, in part, have included the following language in the financial reform bill:

> For purposes of any private civil action implied under this title, any person that knowingly provides substantial assistance to another person in violation of this title, or of any rule or regulation issued under this title, shall be deemed to be in violation of this title to the same extent as the person to whom such assistance is provided. For purposes of this paragraph, a person acts knowingly only if the person has actual knowledge of the conduct underlying the violation described in the preceding sentence.

111 CONG. REC. 3047-48 (2010).

submitted to Congress within one year of the enactment of the Act, on the costs and benefits of expanding the private right of action under §10(b). Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 at §929Z (2010).[5]

Congress is presumed to know the law when it legislates. *See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 379 (1982). Thus, when the Dodd-Frank Act was promulgated, Congress knew from *Stoneridge* that federal courts would not expand §10(b) liability beyond its boundaries at the time of the PSLRA. *See supra*, at 9-11. Congress' repeated decisions not to expand §10(b) private liability should be dispositive because "[i]t is the federal lawmaker's prerogative . . . to . . . shape the contours of . . . §10(b) private actions." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 310-11 (2007). Expanding §10(b) liability by judicial fiat to cover those who assist behind the scenes with preparing or approving another's false statement would do what Congress chose *not* to do — overrule *Stoneridge*. The Court should again decline to extend implied §10(b) private liability by judicial action where Congress has repeatedly declined to do so.

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[5] As explained *infra*, at 24-27, the Chamber believes that such an expansion's costs far exceed any benefits and would harm the competitiveness of U.S. markets.

B. Expanding Primary Liability To Secondary Actors To Whom No Misstatements Are Publicly Attributed Is Incompatible With The Defendant-by-Defendant Reliance Required By *Central Bank* and *Stoneridge*.

The §10(b) private right of action requires plaintiffs to establish reliance on a defendant-by-defendant basis. *See Stoneridge*, 552 U.S. at 159 ("Reliance by the plaintiff on the *defendant's* deceptive acts is an essential element of the §10(b) private cause of action.") (emphasis added); *Central Bank*, 511 U.S. at 180 ("A plaintiff must show reliance on the *defendant's* misstatement or omission to recover under 10b-5. Were we to allow the aiding and abetting action proposed in this case, the *defendant* could be liable without any showing that the plaintiff relied upon the *aider and abettor's* statements or actions.") (emphases added and internal citations omitted). Indeed, "[r]eliance provides the requisite causal connection between a *defendant's* misrepresentation and a plaintiff's injury." *Basic, Inc. v. Levinson*, 485 U.S. 224, 243 (1988) (emphasis added).

Less than a month after *Central Bank* was decided, then-SEC Chairman Arthur Levitt told Congress that *Central Bank* required defendant-by-defendant reliance under §10(b): "[a]s the Supreme Court emphasized in *Central Bank of Denver*, a private plaintiff under Rule 10b-5 must show, *defendant by defendant*, that the plaintiff reasonably

relied on the defendant's misstatement or omission." *Abandonment of the Private Right of Action for Aiding and Abetting Securities Fraud/Staff Report on Private Securities Litigation, Hearing before the Subcomm. on Secs. of the S. Comm. on Banking, Hous. & Urban Affairs,* 103d Cong. 51 (1994) (statement of Arthur Levitt, Chairman, SEC) (emphasis added). Congress left *Central Bank's* requirement of defendant-by-defendant reliance untouched in the PSLRA.

The reliance element under §10(b) may be satisfied by a rebuttable presumption of reliance in two different circumstances. First, reliance may be presumed where a defendant who owes a duty to disclose to the plaintiff omits to state a material fact. *See Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 153-54 (1972). This presumption is inapplicable here, where petitioner Janus Capital Management, LLC ("JCM"), an investment adviser, was found by the district court below not to have owed a duty to disclose to respondents, the shareholders of its parent company (a finding left undisturbed by the Fourth Circuit). Second, under the fraud-on-the-market doctrine, reliance may be presumed when a defendant's allegedly false statements become public and are reflected in the market price of the security. *See Basic*, 485 U.S. at 247; *Stoneridge*, 552 U.S. at 159. However, the fraud-on-the-market presumption of reliance must still satisfy the requirement of defendant-by-defendant reliance, in that a plaintiff must still allege and prove

"that the *defendant* made public misrepresentations." *Basic*, 485 U.S. at 248 n.27 (emphasis added).

Here, the fund prospectuses that contained the allegedly false statements were not attributed to JCM and, as the Fourth Circuit noted, "the clear essence of plaintiff's complaint is that . . . JCM *helped draft* the misleading prospectuses." Pet. App. at 17a (emphasis added). Under these circumstances, where no alleged false or misleading statements were publicly attributed to JCM, respondent cannot establish the defendant-by-defendant reliance that is required by *Central Bank* and *Stoneridge*. *See Stoneridge*, 552 U.S. at 159 (stating that because "[n]o member of the investing public had knowledge, either actual or presumed, of *respondents'* deceptive acts . . . [p]etitioner . . . cannot show reliance upon any of *respondents'* actions except in an indirect chain that we find too remote for liability") (emphasis added).

The majority rule, from which the Fourth Circuit departed in its decision below, recognizes the element of defendant-by-defendant reliance cannot be satisfied where a false or misleading statement is not directly and publicly attributed to the defendant:

> [t]he mere identification of a secondary actor as being involved in a transaction, or the public's understanding that a secondary actor is at work behind the scenes are alone insufficient. To be

> cognizable, a plaintiff's claim against a secondary actor must be based on *that actor's own articulated statement,* or on statements made by another that have been *explicitly adopted by the secondary actor.*

Pac. Inv. Mgmt., 603 F.3d at 155 (emphasis added) (internal citations and quotes omitted); *see also Wright v. Ernst & Young LLP*, 152 F.3d 169, 175 (2d Cir. 1998) ("[A] secondary actor cannot incur primary liability under the [Securities Exchange] Act for a statement not attributed to that actor at the time of its dissemination. . . . Thus, the misrepresentation must be attributed to that specific actor at the time of public dissemination, that is, in advance of the investment decision.").[6]

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[6] *See also Ziemba v. Cascade Int'l, Inc.*, 256 F.3d 1194, 1205 (11th Cir. 2001) ("[W]e conclude that, in light of *Central Bank*, in order for the defendant to be primarily liable under §10(b) and Rule 10b-5, the alleged misstatement or omission upon which a plaintiff relied must have been publicly attributable to the defendant at the time that the plaintiff's investment decision was made."); *Anixter v. Home-Stake Prod. Co.*, 77 F.3d 1215, 1226 (10th Cir. 1996) ("[W]e conclude that in order for accountants to 'use or employ' a 'deception' actionable under the antifraud law, they must themselves make a false or misleading statement (or omission) that they know or should know will reach potential investors."); *SEC v. Wolfson*, 539 F.3d 1249, 1259 (10th Cir. 2008) ("[T]he attribution requirement of the bright-line test stems directly from the need for *private* litigants to prove reliance on an alleged fraud to succeed on a *private* cause of action.").

In contrast, the Fourth Circuit's decision, by erasing the distinction between defendants to whom false or misleading statements are directly and publicly attributed and those who merely participate in drafting, preparing, or approving the statements, improperly substitutes reliance on the *statements* for reliance on the *defendant* as an element of a §10(b) cause of action. *See* Pet. App. at 19a ("While the prospectuses did not explicitly name [JCM] as the drafter[], plaintiffs nevertheless allege in their complaint that [JCM] may be held responsible for the statements in the prospectuses because as a practical matter JCM runs the Janus funds.") (internal quotation omitted). However, merely alleging reliance on another entity's false or misleading *statements* does not satisfy the element of defendant-by-defendant reliance required by *Central Bank* and *Stoneridge*. *See Pacific Investment Management Company*, 603 F.3d at 156 ("Without explicit attribution to the firm . . . reliance on that firm's participation can only be shown through 'an indirect chain . . . too remote for liability.'") (*citing Stoneridge*). *Stoneridge* forbids precisely this sort of expansion of the §10(b) implied right of action.

C. Expanding Primary Liability To Secondary Actors To Whom No False or Misleading Statements Are Directly And Publicly Attributed Is Incompatible With The PSLRA's Defendant-By-Defendant Loss Causation Requirement.

Extending §10(b) liability to secondary actors to whom no false or misleading statement or conduct is directly and publicly attributed is also incompatible with the PSLRA's defendant-by-defendant loss causation requirement. The PSLRA requires that the plaintiff allege and prove that "the act or omission of *the defendant* alleged to violate this chapter caused the loss." 15 U.S.C. §78u-4(b)(4) (emphasis added). This express statutory requirement is satisfied only by showing that the price of securities purchased or sold by the plaintiff declined because of the particular defendant's deceptive act or omission. *See Dura Pharms., Inc. v. Broudo*, 544 U.S. 336, 344 (2005); *see also Lattanzio v. Deloitte & Touche LLP,* 476 F.3d 147, 158 (2d Cir. 2007) ("Plaintiffs have not alleged facts to show that *Deloitte's misstatements*, among others (made by Warnaco) that were much more consequential and numerous, were the proximate cause of plaintiffs' loss.") (emphasis added).

The Fourth Circuit's decision to expand primary liability under §10(b) to a defendant where there is no public attribution of any false or misleading statement to "the defendant" contradicts

the PSLRA's express requirement of defendant-by-defendant loss causation. All that the Fourth Circuit would require would be an allegation that the defendant substantially participated in some other defendant's statement or omission. Pet. App. at 24a. However, such an allegation, without more, would not satisfy the PSLRA's requirement that "the act or omission *of the defendant*" be the cause of the loss. Thus, the Fourth Circuit's expansion of the §10(b) implied right of action is incompatible with the PSLRA's express language.

D. The Expansion Adopted By The Fourth Circuit Is Uncertain And Unworkable.

As *Central Bank* held, liability under §10(b) is "'an area that demands certainty and predictability.'" 511 U.S. at 188 (quoting *Pinter v. Dahl*, 486 U.S. 622, 652 (1988).). The test adopted by the Fourth Circuit, which extends §10(b) liability to secondary actors if a court finds that "interested investors" would "attribute to the defendant a substantial role in preparing or approving" an alleged false statement, clouds with uncertainty the question of who can be primarily liable under §10(b) and burdens district courts with a liability test that is unworkable in application. Pet. App. at 24a.

The SEC has also advocated for a similar test, which it calls the "creator" test, pursuant to which a defendant would be liable under §10(b) for "creating"

a false or misleading statement on which investors relied, even if the defendant did not make the statement and the statement was not publicly attributed to him. *See* Brief for S.E.C. as Amicus Curiae Supporting Plaintiffs-Appellants at 7, *Pac. Inv. Mgmt. Co. v. Mayer Brown LLP*, 603 F.3d 144 (2d Cir. 2010) (No. 09-1619-cv). The SEC's proposed test suffers from all the same defects as the Fourth Circuit's, including unpredictability and uncertainty.

In *Pacific Investment Management Co. v. Mayer Brown LLP*, the Second Circuit properly rejected the SEC's "creator" test. It concluded that "[a] creator standard would inevitably lead to uncertainty regarding the scope of Rule 10b-5 liability and potentially deter beneficial conduct" in that it "establishes no clear boundary between primary violators and aiders and abettors, and it is uncertain what level of involvement might expose an individual to liability." 603 F.3d at 157.

The same is true for the Fourth Circuit's test. By requiring a fact-intensive, case-by-case assessment in order to determine whether a defendant's participation in a false or misleading statement warranted attributing "a substantial role" to the defendant, the Fourth Circuit's test is certain to breed inconsistency in its application and outcome. And by blurring the clear line between defendants to whom false statements are directly and publicly attributed and everyone else who is involved in the preparation of a public statement, the Fourth

Circuit's decision fosters *ad hoc* judicial rule making that guarantees unpredictability and uncertainty for financial industry participants. *See Central Bank*, 511 U.S. at 188 (uncertainty in the scope of §10(b) and Rule 10b-5 liability results in "decisions made on an ad hoc basis, offering little predictive value to those who provide services to participants in the securities business") (internal quotation omitted).

Under the Fourth Circuit's test, financial industry participants who are named as defendants in securities litigation would face a highly unpredictable outcome with enormous financial stakes. Thus, they would have every incentive to "as a business judgment . . . abandon substantial defenses and . . . pay settlements in order to avoid the expense and risk of going to trial." *Id.* at 189. The Fourth Circuit's test will also raise costs for issuers, particularly new and less established businesses seeking to raise capital in the financial markets. Indeed, "newer and smaller companies may find it difficult to obtain advice from professionals. A professional may fear that a newer or smaller company may not survive and that business failure would generate securities litigation against the professional, among others." *Id.*

The necessary certainty and stability can be provided only by the bright-line rule adopted by a majority of federal appellate courts, requiring that misstatements be directly and publicly attributed to a defendant to establish liability under §10(b). *See Pac. Inv. Mgmt.*, 603 F.3d at 155 ("[S]econdary actors can

be liable in a private action under Rule 10b-5 for only those statements that are explicitly attributed to them."); *Ziemba v. Cascade Int'l, Inc.*, 256 F.3d 1194, 1205 (11th Cir. 2001) ("[T]he alleged misstatement or omission upon which a plaintiff relied must have been publicly attributable to the defendant at the time that the plaintiff's investment decision was made."); *Anixter v. Home-Stake Prod. Co.*, 77 F.3d 1215, 1226 (10th Cir. 1996) ("[F]or an accountant's misrepresentation to be actionable as a primary violation, there must be a showing that he knew or should have known that his representation would be communicated to investors."). A bright line rule makes clear to all financial industry participants that "those who sign or otherwise allow a statement to be attributed to them expose themselves to liability," while those who do not sign "are beyond the reach of Rule 10b-5's private right of action." *Pac. Inv. Mgmt.*, 603 F.3d at 157. A bright line rule is easier for district courts to apply, avoids protracted litigation, and discourages "discovery aimed at learning the identity of each person or entity that had some connection, however tenuous, to the creation of an allegedly false statement." *Id.*

E. The Expansion Adopted By The Fourth Circuit Would Discourage Issuers From Listing On U.S. Exchanges.

As the Court noted in *Stoneridge*, expanding the §10(b) implied right of action would "raise the

cost of being a publicly traded company under our law and shift securities offerings away from domestic capital markets." 552 U.S. at 164. United States capital markets have become less competitive with their counterparts around the world, in large part because of fears of costly U.S. securities litigation. *See* U.S. Chamber of Commerce, *Commission on the Regulation of U.S. Capital Markets in the 21st Century: Report and Recommendations* (2007);[7] Michael R. Bloomberg and Charles E. Schumer, *Sustaining New York's and US' Global Financial*

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[7] Available at http://www.uschamber.com/sites/default/files/reports/0703capmarkets_full.pdf. *See also Howell E. Jackson, Summary of Research Findings on Extra-Territorial Application of Federal Securities Law,* in *Global Capital Markets & U.S. Securities Laws,* 1743 PLI/Corp. 1243, 1253 (2009) ("Many interviewees cite U.S. anti-fraud laws—specifically Rule 10b-5—as a 'top concern' because they are the 'most intrusive' and have the 'biggest' impact on extra-territorial transactions."); Jonathan Macey, *What Sarbox Wrought*, Wall St. J., Apr. 7, 2007, at A9 ("All of a sudden it is no longer fashionable to be a U.S. public company: It's for suckers who can't access the piles of sophisticated 'global' capital available elsewhere. . . . If the U.S. is to regain its former position in the world capital market, much more will have to be done. Massive litigation risk remains . . . ."); Ian Swanson, *Foreign Executives Press For Reform Of Litigation in United States*, The Hill, May 18, 2007, at 11 ("[L]itigation is a greater disincentive to doing business in the U.S. than fears that a protectionist Congress might impose new barriers to foreign trade and investment."); Alan Beattie, *London Named Top Financial Centre*, Fin. Times, June 12, 2007, at 6 (the United States has been disadvantaged because of its "litigious and apparently arbitrary culture of regulation and policy").

Services Leadership (Jan. 22, 2007);[8] Comm. on Capital Mkts., *Interim Report of the Committee on Capital Markets Regulation,* at 11 (Nov. 30, 2006).[9]

This was highlighted in a non-partisan report commissioned by New York City Mayor Michael Bloomberg and New York Senator Charles Schumer, entitled *Sustaining New York's and US' Global Financial Services Leadership* (the "Report"). The Report found that the threat of costly securities litigation was a significant deterrent to foreign companies wishing to do business in the United States. Report at 101. The Report also found that "a fair and predictable legal environment" was among the most important factors considered in the assessment of places to do business and that the United States was perceived to be at a significant disadvantage with regard to the fairness and predictability of its legal environment. *Id.* at 16.

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[8] Available at http://www.abanet.org/buslaw/committees/CL116000pub/materials/library/NY_Schumer-Bloomberg_REPORT_FINAL.pdf ("[T]he legal environments in other nations, including Great Britain, far more effectively discourage frivolous litigation" while "the prevalence of meritless securities lawsuits and settlements in the U.S. has driven up the apparent and actual cost of business -- and driven away potential investors.").

[9] Available at http://www.capmktsreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf ("Foreign companies commonly cite the U.S. class action enforcement system as the most important reason why they do not want to list in the U.S. market.").

The Fourth Circuit's test would add to the cost and unpredictability of securities litigation and drive away companies wishing to list their securities on U.S. exchanges. Under the Fourth Circuit's test, securities litigation will become more costly as the ranks of potential defendants expand to include lawyers, accountants, bankers, investor relations consultants, and other financial market professionals. The subjective and highly fact-intensive nature of the Fourth Circuit's test would add to the cost of securities lawsuits by prompting litigation in almost every case as to whether a service provider's participation in an issuer's alleged false statement was sufficiently "substantial" to support a claim for primary liability under §10(b). Inevitably, numerous issuers would list securities elsewhere — or forego capital raising — rather than indemnify all these service providers against §10(b) class action litigation costs.

The Fourth Circuit's test would also yield unpredictable results. Individual trial courts applying the test on a "case by case" (Pet. App. 24a) basis will have differing and inconsistent views as to whether a given service provider's level of participation is "substantial" enough to merit attributing an alleged false statement to that service provider, which will lead to *ad hoc* and inconsistent judicial rulemaking. Such a test will also add to the complexity of a jury's task at trial, as jurors grapple with assigning liability among various lawyers, accountants, bankers, and other market professionals based on whether they

"substantially" participated in an alleged false statement. All of this will only strengthen the prevailing view that §10(b) class action liability is too costly and unpredictable to do business here.

II. INDEPENDENTLY, LIABILITY UNDER RULE 10(b)-5(b) DOES NOT EXTEND TO THOSE WHO DO NOT MAKE FALSE OR MISLEADING STATEMENTS ABSENT A DUTY TO SPEAK.

A. Extending Liability Under Rule 10b-5(b) To Those Who Do Not Themselves "Make" A Misstatement Contradicts The Text Of The Rule.

Independently, the Fourth Circuit's decision, which held that a defendant who *substantially participated* in drafting or disseminating a false statement could be deemed to have made the false statement for purposes of assessing liability under §10(b), contradicts the text of Rule 10b-5(b).[10] Rule 10b-5(b) renders it unlawful for any person "to *make* any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading." 17 CFR §240.10b-5(b) (2010) (emphasis added).

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[10] This brief addresses only Rule 10b-5(b) because there are no questions presented on appeal concerning sub-sections (a) or (c) of Rule 10b-5.

The alleged false statements that are at issue here were not publicly attributed to JCM, and JCM is nowhere identified as the "maker" of the false statements. Pet. App. at 17a. Nevertheless, the Fourth Circuit held that, for purposes of assessing liability under Rule 10b-5(b), JCM could be deemed to have made the false statements because it "*caus[ed*] mutual fund prospectuses" containing the statements "to be issued" and "ma[de] them available for the investing public" by filing them with the SEC and posting them on a website. Pet. App. at 17a-18a (quotation omitted) (emphasis added). The Fourth Circuit found that "[t]hese statements, taken together, allege that . . . JCM, by participating in the writing and dissemination of the prospectuses, *made* the misleading statements contained in the documents." Pet. App. at 18a (emphasis in original).

The Fourth Circuit's decision contradicts the text of Rule 10b-5(b). By focusing on those who "make" false or misleading statements, Rule 10b-5(b) is clearly intended to reach *speakers* — issuers and the corporate officers to whom an issuer's statements are directly and publicly attributed. Rule 10b-5(b) does not reach non-speakers who merely participate in or assist with the drafting and dissemination of public statements, but to whom no statements are directly and publicly attributed.

As an analogy, consider an unsigned and unattributed newspaper editorial. The editorial is the statement of an organization, not of unnamed

participants in creating the editorial. The newspaper is the speaker, not those who draft, review, edit, or approve the editorial. Those who do not sign the written statements of an organization, and who do not have such statements attributed to them, simply do not "make" the statements issued by the organization.

B. Extending Liability Under Rule 10b-5(b) To Those Who Participate In Drafting Or Disseminating A Misstatement Contravenes *Central Bank*.

The Fourth Circuit's decision, by conflating *participating* in drafting and disseminating a false statement with *making* a false statement, revives aiding and abetting liability in contravention of *Central Bank*. *See Central Bank*, 511 U.S. at 177 ("[T]he statute prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act."). Liability based on participation in another's false statement is aiding-and-abetting liability under a different label, as the Fourth Circuit's own language illustrates. *See* Pet. App. at 17a ("In this case . . . the clear essence of the plaintiffs' complaint is that . . . JCM *helped* draft the misleading prospectuses.") (emphasis added); *see also Shapiro*, 123 F.3d at 720 ("Allegations of 'assisting,' 'participating in,' 'complicity in' and similar synonyms . . . all fall within the prohibitive bar of *Central Bank*.").

Under §104 of the PSLRA, Congress entrusted the SEC — and only the SEC — with the power to bring a civil enforcement action against "any person that knowingly provides substantial assistance to another person in violation of" §10(b) and Rule 10b-5. 15 U.S.C. §78t(e). This was a considered policy choice by Congress. *See Stoneridge*, 552 U.S. at 166 (noting that "the enforcement power is not toothless"). Extending the §10(b) implied private right of action so that every class action lawyer in America could sue anyone who participated in another person's §10(b) violation would obliterate the line drawn by Congress.

Like §104 of the PSLRA, other provisions of the 1933 and 1934 Acts also allow only the SEC and the Justice Department, not private litigants, to sue secondary actors who participate in another's primary violation. Respondent's argument would undo Congress' policy decision to entrust government regulators and prosecutors, rather than private class actions lawyers, with policing these secondary actors. In §17(a) of the 1933 Act, for example, Congress expressly rendered it unlawful "to engage in any *transaction*, practice, or *course of business* which operates or would operate as a fraud or deceit upon the purchaser." 15 U.S.C. §77q(a)(3). Unlike §10(b), §17(a)(3) expressly covers defendants who engage in a "transaction" or "course of business," rather than those who "use" or "employ" a deceptive device itself. The SEC regularly invokes §17(a) in enforcement actions against secondary actors. *See, e.g., Weiss v. SEC*, 468 F.3d 849, 855-56 (D.C. Cir. 2006). However,

there is no private right of action under §17(a). *See, e.g., Finkel v. Stratton Corp.*, 962 F.2d 169, 175 (2d Cir. 1992).

Congress left to the SEC and the Justice Department the sole power to enforce the more sweeping prohibitions applicable to secondary actors under §17(a). In doing so, Congress chose not to leave enforcement against secondary actors in the hands of the class action bar, where prosecutorial decisions would be driven by purely private economic, rather than public, interests. *See also* §§15 U.S.C. 78o(b)(4)(E), 78u-3(a) (granting the SEC, not private class action plaintiffs lawyers, the power to sue registered broker-dealers and "associated persons" who "willfully aided, abetted, counseled, commanded, induced, or procured" violations of the securities laws). The Court should continue this policy choice by Congress and not undo it by expanding the §10(b) private right of action.

C. Extending Liability Under Rule 10b-5(b) To Defendants Who Participate In Drafting Or Disseminating A Misstatement Would Contravene Settled Law That Those Who Are Silent Are Not Liable Absent A Duty To Speak.

When an issuer, or any company, makes a statement, the speaker is the company itself and those of its officers who have signed the statement, spoken the words, or personally have a duty to disclose. To hold otherwise would be to vastly expand the categories of individuals and entities that can be sued in §10b cases.

By definition, those who "participate" in an issuer's public statements do not themselves speak. They are silent. Silence is not actionable under §10(b) "absent a duty to speak." *Chiarella v. United States*, 445 U.S. 222, 235 (1980). Thus, while those who sign or otherwise allow a statement to be attributed to them expose themselves to liability, those who do not are beyond the reach of §10(b) and Rule 10b-5(b), absent a duty to investors to speak.

And not just any duty suffices — the defendant must have a "duty to disclose arising from a relationship of trust and confidence *between parties to a transaction*." *Id.* at 230 (emphasis added). And to have an implied §10(b) private right of action, a plaintiff must show not merely a violation of law, but

a breach of a legal duty owed to *that specific plaintiff*. *See, e.g., Stoneridge*, 552 U.S. at 159 (explaining that "if there is an omission of a material fact *by one with a duty to disclose*, the investor *to whom the duty was owed*" will be presumed to have relied on the omission) (emphasis added); *Bangor Punta Operations v. Bangor & Aroostook R.R.*, 417 U.S. 703, 716 n.13 (1974) ("[T]he recovery provided is intended to compensate, not the public generally, but those who have been injured by a breach of duty owed to them."); *Foss v. Bear, Stearns & Co.*, 394 F.3d 540, 541 (7th Cir. 2005) (Easterbrook, J.) (§10(b) private civil claim requires deceit against the plaintiff); *Moss v. Morgan Stanley Inc.*, 719 F.2d 5, 13, 16 (2d Cir. 1983) (explaining that, although investment bank employee was convicted of criminal §10(b) violation for insider trading, shareholders in target company had no §10(b) claim because "[t]here is no 'duty in the air' to which any plaintiff can attach his claim") (citation omitted); *see also Cipollone v. Liggett Grp., Inc.*, 505 U.S. 504, 522 (1992) (plurality opinion) (citing Black's Law Dictionary 1489 (6th ed. 1990) as "defining 'tort' as 'always [involving] a violation of some duty *owing to plaintiff*'") (emphasis added; brackets in original). No such duty can be alleged here between JCM, an investment adviser, and respondents, the shareholders of a different company — the investment adviser's parent. *See* Pet. Br. at 42.

D. Extending §10(b) Liability To Those Who Cause A Misstatement To Be Made Would Nullify Statutory Limitations On The Express Private Right of Action Under §18(a) Of The 1934 Act.

The Fourth Circuit's test would extend Rule 10b-5(b) liability to those who "caused" a false statement to be made. Pet. App. 17a-18a. Rule 10b-5(b) applies only to defendants that "make" a statement. In contrast, the limited but express right of action that Congress provided in §18(a) of the 1934 Act imposes liability on a defendant who "shall make *or cause to be made*" a statement that is "false or misleading with respect to any material fact" in "any application, report or document filed" pursuant to the Exchange Act. 15 U.S.C. §78r(a). Surely, when the SEC promulgated 10b-5(b) in 1942, it understood that "make or cause to be made" is broader than "make." Ignoring that the SEC chose the narrower term "make," the Fourth Circuit's test improperly extends Rule 10b-5(b) to defendants that only "caused" statements to be made.

Moreover, although express §18(a) private liability reaches a broader array of defendants than §10(b), Congress imposed in §18(a) a critical limitation to preclude excessive damages liability: the plaintiff must have actually read and relied upon the alleged false statement. Section 18(a) limits potential plaintiffs to "any person . . . who, *in reliance upon*

such statement, shall have purchased or sold a security at a price which was affected by such statement, for *damages caused by such reliance*." *Id.* (emphasis added). Because §18(a) expressly refers to the plaintiff's reliance on the specific statement, it can be satisfied only by proof of individual reliance, rather than by the fraud-on-the-market presumption. *See, e.g., In re Suprema Specialties, Inc. Secs. Litig.*, 438 F.3d 256, 283-84 (3d Cir. 2006); *Heit v. Weitzen*, 402 F.2d 909, 916 (2d Cir. 1968).

By contrast, in private §10(b) actions, the reliance requirement is not a statutory creation but rather was judicially implied to delimit the implied cause of action. *See Basic Inc. v. Levinson*, 485 U.S. 224, 243 (1988). Allowing the fraud-on-the-market presumption to satisfy reliance in a §10(b) action does not render §18(a) a nullity only so long as the class of defendants that can be sued in a §10(b) implied private civil action is narrower than in the express §18(a) action. The Fourth Circuit's test erases that line by extending liability under §10(b) to those who cause a false statement to be made. Such expansive implied civil liability under §10(b) would nullify the statutory limitations on private civil liability that are contained in §18(a). Section 10(b) should not be interpreted to erase the limits set forth by Congress in an express cause of action in the 1934 Act. *See Central Bank*, 511 U.S. at 184 ("The fact that Congress chose to impose some forms of secondary liability, but not others, indicates a deliberate

congressional choice with which the courts should not interfere.").

CONCLUSION

The decision of the court of appeals should be reversed.

Respectfully submitted,

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