Team No. R11

Docket No. 19-305

IN THE

Supreme Court of the United States

ROBERT "BOBBY" MAXELROD, *et al.*,

Petitioner,

v.

AVA CATO

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fourteenth Circuit

BRIEF FOR RESPONDENT

QUESTIONS PRESENTED

I. Whether the determination that a transaction is domestic is sufficient for the extraterritorial application of Section 10(b).

II. Whether an employee who, at the insistence of a superior, inserts a false or misleading statement into investor materials, is subject to primary liability under Rule 10b-5(a) or (c), even if that individual is not the maker of the statement for purposes of Rule 10b-5(b).

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases **Page(s)**

Statutes

Regulations

Other Authorities

STATUTORY AND REGULATORY PROVISIONS INVOLVED

At issue is the interpretation of 15 U.S.C. § 78j(b), 15 U.S.C. § 78t(e), 17 C.F.R. § 240.10b-5, and 17 C.F.R. § 240.12g3-2(b). The relevant text is reproduced in the appendix.

STATEMENT OF FACTS

Alcollezione is an Italian wine and liqueur corporation founded in 2009 by CEO Gianni Marconi and CFO Benny Factor; Marconi and Factor are U.S. citizens who reside in Italy. R. at 2. The two founders hired General Counsel Ava Cato, an Italian citizen and recent graduate of an Italian university. *Id.* The company was established, headquartered, and continues to operate in Milan, Italy. *Id.*

Although Alcollezione started as a private company, understanding the need to raise capital to compete with more established rivals, Marconi and Factor eventually moved to take the company public. *Id.* at 3. In preparation for the initial public offering ("IPO"), Alcollezione created an "Investor Relations" section on its website, posting financial statements, corporate disclosures, and other investor materials. *Id.* Like most serious businesses, Alcollezione had its website and materials in English in addition to Italian. *Id.* Alcollezione's 2011 IPO closed with 20,000,000 shares of common stock that were then listed exclusively on the Borsa Italiana – the Italian stock exchange. *Id.*

Celebrating a successful IPO, Marconi and Factor then traveled to New York to visit family; Cato accompanied the two, visiting New York for the first time. *Id.* While there, the three met Doris Schutt, a friend of Factor and an investment banker who urged the Alcollezione executives to establish a subsidiary in the U.S. or at least sponsor American Depository Receipts ("ADRs") representing Alcollezione shares; in particular, she noted that sponsoring ADRs would allow Alcollezione to access U.S. capital. *Id.* However, weary of contacts he would have to maintain in the U.S. for a subsidiary or for sponsoring ADRs and noting that "he no longer had the temperament for American business," Marconi declined. *Id.*

In 2016, Schutt called Marconi in Milan to notify him that she was considering using her position at a New York depository to set up unsponsored ADRs ("uADRs") representing Alcollezione shares so her friends at U.S.-based hedge funds could purchase them; the hedge funds could not purchase Alcollezione shares directly due to portfolio restrictions against trading on foreign exchanges. *Id.* at 4. Schutt explained that since Factor was her friend, she wanted to let Alcollezione know before setting up the uADRs. *Id.* Marconi merely told her that a friend of Factor's was a friend of his. *Id.*

The ADRs Schutt referred to are certificates that evidence American Depositary Shares ("ADSs"). Additional Form F-6 Eligibility Requirement Related to the Listed Status of Deposited Securities Underlying American Depositary Receipts, Proposed Rule, 68 Fed. Reg. 54,644, 54,644 n. 4 (Sept. 17, 2003) (hereinafter "Additional Form F-6 Eligibility Requirement"). ADSs are securities created by depository institutions and represent ownership interest in foreign securities held by the depository. *Id.* The terms "ADR" and "ADS" are used interchangeably. *Id.*

ADRs can be sponsored or unsponsored. *Id.* To create a sponsored ADR, a foreign company whose security is being represented must enter into an agreement with a depository; the ADR holders in turn are third-party beneficiaries. *Id.* at 54,645. Meanwhile, to create unsponsored ADRs depositories only need to file a Form F-6 with the SEC. *Id.* Thus, the SEC describes uADRs as "essentially a two-party contract between depositories and the ADR holders." *Id.* at 54,644-45. The foreign company whose security is being represented has no filing obligations with the SEC. Exemption from Registration Under Section 12(G) of the Securities Exchange Act of 1934 for Foreign Private Issuers; Final Rule, 73 Fed. Reg. 52,755 (Sept. 10, 2008) (hereinafter "Exemption from Registration Under Section 12(G)").

In 2017, Alcollezione began preparations for its annual shareholders meeting (the "Annual Meeting") and the launch of Frizzantissimo, its new alcoholic sparkling beverage, at that meeting. R. at 5. Marconi asked Cato to conduct research to ensure Frizzantissimo's compliance with Italian beverage regulations. *Id.* With her biannual review looming, Cato conducted a thorough research of the Italian regulatory landscape. Cato described that compliance "would be an uphill climb" and "seemed unlikely in the short-term." *Id.*

However, wanting to put Frizzantissimo front and center at the Annual Meeting, Marconi ordered Cato to draft assurances that Frizzantissimo was compliant with the appropriate regulations. *Id.* He told Cato that the regulatory issues "always find a way of getting resolved." He assured her "[i]t is better to ask for forgiveness than permission—and trust me, I can handle the PR stuff if there is blowback." *Id.* Noticing Cato's visible discomfort, Marconi pressed her further by stating that "this sort of thing was perfectly common in business." Marconi then threatened, "listen, this is happening with or without you." *Id.*

While it was unclear whether Frizzantissimo would actually violate any beverage regulations, Cato drafted assurances that the product was to be approved and ready for the market in the second quarter of 2018. *Id.* at 6. She then condensed these assurances into a disclosure which were eventually inserted into Marconi's presentation slide deck for the Annual Meeting and footnoted in Alcollezione's pro forma financial statements. *Id.* The slide deck and financial statements materials were later uploaded to Alcollezione's website. *Id.* When Frizzantissimo was launched at the Annual Meeting, Alcollezione's share value increased and continued to do so. *Id.* Schutt later sent Factor a friendly email congratulating him on yet another success. *Id.*

On March 14, 2018, Alcollezione's share value decreased when Alcollezione halted production of Frizzantissimo upon discovering compliance issues. *Id.* After speaking with shareholders, Marconi, Factor, and Cato all resigned. *Id.*

STANDARD OF REVIEW

A court reviews *de novo* a dismissal under Rule 12(b)(6) of the Federal Rules of Civil Procedure. *Lormand v. US Unwired, Inc.*, 565 F.3d 228, 232 (5th Cir. 2009). The plaintiff must state a claim that is plausible on its face, which allows for a "reasonable inference that the defendant is liable for the misconduct alleged." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). When "it is clear from the face of the complaint, and matters of which the court may take judicial notice, that the plaintiff's claims are barred as a matter of law," dismissal is proper. *Conopco, Inc. v. Roll Int'l*, 231 F.3d 82, 86 (2d Cir. 2000).

SUMMARY OF ARGUMENT

The Fourteenth Circuit's decision should be affirmed. In restricting the application of Section 10(b) to domestic transactions and transactions of securities listed on U.S. exchanges, the Court in *Morrison* reaffirmed Section 10(b)'s presumption against extraterritoriality and made clearer when Section 10(b) should be applied. Staying true to *Morrison*, the Fourteenth Circuit adopted the Second Circuit's approach in *Parkcentral*, which held that a domestic transaction is only necessary to apply Section 10(b). This approach accords with the *Morrison* Court's repeated references to a transaction's other aspects to be considered when determining Section 10(b)'s applicability. Moreover, this approach upholds *Morrison*'s commitment to Section 10(b)'s presumption against extraterritoriality given the chaos between U.S. and foreign securities laws that would ensue if Section 10(b) were applicable to any domestic transaction. Accordingly, Section 10(b) should not apply to the predominantly foreign transaction at issue here because Alcollezione is an Italian company with shares listed exclusively on the Borsa Italiana and the alleged misrepresentations were made to Italian investors to raise Italian capital.

Even if Section 10(b) is applicable, Petitioners have failed to adequately plead primary liability for a deceptive scheme under Rule 10(b)-5(a) and (c).

Disseminators of misstatements should not be subject to primary liability in the private context. Expanding the private cause of action is outside the Supreme Court's authority and contradicts the distinction drawn between primary and secondary liability in prior holdings. Expanding the private cause of action is also detrimental to judicial economy. Furthermore, even if disseminators were subject to primary liability in the private context, Cato escapes liability because she does not meet the definition of a disseminator.

ARGUMENT

I. THE FOURTEENTH CIRCUIT'S RULING SHOULD BE AFFIRMED BECAUSE (1) A DOMESTIC TRANSACTION IS ONLY NECESSARY TO APPLY SECTION 10(B) AND (2) THE TRANSACTION HERE IS PREDOMINANTLY FOREIGN

It is a "longstanding principle of American law" that U.S. laws have a strong presumption against extraterritorial application. *E.E.O.C. v. Arabian Am. Oil Co.*, 499 U.S. 244, 248 (1991) ("*Aramco*"); *Morrison v. National Australia Bank Ltd.*, 561 U.S. 247, 255 (2010). Thus, unless Congress shows affirmative intent for a law to apply extraterritorially, the law does not. *Aramco*, 499 U.S. at 248; *Morrison*, 561 U.S. at 255. Since Congress does not show such an intent for Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), Section 10(b) does not apply extraterritorially. *Morrison*, 561 U.S. at 265. *See* 51 U.S.C. § 78j.

In fact, Section 10(b) applies only when the transaction at issue either (1) involves a security listed on a U.S. securities exchange or (2) occurs in the U.S. *Morrison*, 561 U.S. at 267. A transaction occurs in the U.S. and is considered "domestic when the parties [to the transaction] incur irrevocable liability to carry out the transaction within the United States or when title is passed within the United States." *Absolute Activist Value Master Fund Ltd. v. Ficeto*, 677 F.3d 60, 69 (2d Cir. 2012); *Stoyas v. Toshiba Corp.*, 896 F.3d 933, 949 (9th Cir. 2018); *United States v. Georgiou*, 777 F.3d 125, 136 (3d Cir. 2015); *U.S. S.E.C. v. Benger*, 2013 WL 593952, at *9 (N.D. Ill. Feb. 15, 2013).

From here, the Second and Ninths Circuits disagree on whether Section 10(b) applies to a transaction simply because the transaction occurred in the U.S. The Second Circuit and at least one district court in the Fifth Circuit have held that a domestic transaction is merely necessary for Section 10(b) to apply. *Parkcentral Glob. Hub Ltd. v. Porsche Auto. Holdings SE*, 763 F.3d 198, 215 (2d Cir. 2014). *See Lykuong Eng v. Akra Agric. Partners, Inc.*, 2017 WL 5473481, at *3 (W.D. Tex. Aug. 9, 2017). The Ninth Circuit has held that a domestic transaction is sufficient for Section 10(b) to apply. *Stoyas*, 896 F.3d at 950.

For the reasons below, the Ninth Circuit is wrong.

A. A domestic transaction is only necessary to apply Section 10(b)

Prior to *Morrison*, courts had strayed from the text of Section 10(b), sidelining the importance of a transaction's location in favor of other aspects and thereby ignoring the presumption against extraterritoriality. *See*, *e.g.*, *Schoenbaum v. Firstbrook*, 405 F.2d 200, 212–13 (2d Cir. 1968) (analyzing an alleged fraud's effect on the U.S. securities market and investors); *Itoba Ltd. v. Lep Group PLC*, 54 F.3d 118, 123-24 (2d Cir. 1995) (analyzing preparations in the U.S. for the alleged fraud); *Leasco Data Processing Equip. Corp. v. Maxwell*, 468 F.2d 1326, 1334 (2d Cir. 1972) (analyzing where the alleged fraud occurred).

Thus, when the Court in *Morrison* held that Section 10(b) only applied to domestic transactions, it defined a clear limit beyond which Section 10(b) was inapplicable and reaffirmed Section 10(b)'s strong presumption against extraterritoriality. *See* 561 U.S. at 459. The Second Circuit upheld those aims in *Parkcentral* by refusing to apply Section 10(b) to a transaction simply because the transaction occurred in the U.S. 763 F.3d at 215 ("[A] rule making [Section 10(b)] applicable whenever the plaintiff's suit is predicated on a domestic transaction, regardless of the foreignness of the facts constituting the defendant's alleged violation would seriously undermine *Morrison*'s insistence that § 10(b) has no extraterritorial application.").

1. <u>The Second Circuit in *Parkcentral* stays true to *Morrison*'s clear language and reasoning</u>

Writing for the Court in *Morrison*, Justice Scalia implied that a transaction's domestic location is only a necessary condition. *See Morrison*, 561 U.S. at 267 ("<u>[O]nly</u> transactions in securities listed on domestic exchanges, and domestic transactions in other securities, to which § 10(b) applies.") (emphasis added), 273 ("Section 10(b) reaches the use of a manipulative or deceptive device or contrivance <u>only</u> in connection with the purchase or sale of a security listed on an American stock exchange, and the purchase or sale of any other security in the United States.") (emphasis added). The Court never held "that an application of § 10(b) <u>will</u> be deemed domestic whenever such a transaction is present." *Parkcentral*, 763 F.3d at 215 (emphasis in original).

Further, in using a transaction's location to draw a clear limit for Section 10(b), the Court never rejected from consideration a transaction's other aspects. It merely reaffirmed Section 10(b)'s presumption against extraterritoriality that had fallen into disuse. *Compare Morrison*, 561 U.S. at 257 ("[T]he Second Circuit had excised the presumption . . . from the jurisprudence of § 10(b).") *with id.* at 261 ("[W]e [re]apply the presumption in all cases, preserving a stable background.") (emphasis added). *See also supra* pp. 7-8. Conversely, the Court's point that *Morrison* "involve[d] no securities listed on a domestic exchange, and all aspects of the purchases complained of . . . occurred outside the United States" would have been unnecessary if a transaction's location exclusively determined the applicability of Section 10(b). *See id.* at 273 (emphasis added). *See also id.* at 273-74 (Breyer, J. concurring) (noting that "the relevant purchases of these unregistered securities took place entirely in Australia and involved only Australian investors") (emphasis added).

2. The Second Circuit in *Parkcentral* upholds *Morrison*'s focus on the presumption against extraterritoriality

Aware of the economic realities of the global securities market, the Court in *Morrison* recognized that even foreign transactions often have domestic aspects. *See id.* at 266 ("[I]t is a rare case of prohibited extraterritorial application that lacks all contact with the territory of the United States.") (emphasis removed). Thus, the Court warned against a broad application of Section 10(b), noting that "the presumption against extraterritoriality would be a craven watchdog indeed if it retreated to its kennel whenever some domestic activity is involved." *Id.* (emphasis removed).

In honoring that warning while remaining faithful to the text of Section 10(b), the Second Circuit in *Parkcentral* held that while application of Section 10(b) must be rooted in a domestic transaction, not every domestic transaction warrants application of Section 10(b). 763 F.3d at 215. Thus, the Second Circuit recognized, whereas the Ninth Circuit in *Stoyas* did not, that if a domestic transaction alone triggers the application of Section 10(b), the presumption against extraterritoriality is meaningless. *Id.* at 213. Particularly with domestic transactions of uADRs, unless the transaction's other relevant aspects are considered, the heralded presumption against extraterritoriality is a craven watchdog indeed. *See id.* at 216.

a. If Section 10(b) applies to every transaction that occurs in the U.S., its presumption against extraterritoriality is moot

Contrary to the cautiously defined limit of Section 10(b) as drawn by the Court in *Morrison*, Section 10(b) under the Ninth Circuit's approach in *Stoyas* is limitless. It can apply to "wholly foreign activity clearly subject to regulation by foreign authorities solely because a plaintiff in the United States made a domestic transaction." *Parkcentral*, U.S. 763 F.3d at 215. This approach is indeed "clear," but that clarity is gained by turning the presumption against extraterritoriality on its head.[1] *See Stoyas*, 896 F.3d at 950 ("[I]t may very well

[1] The breadth of Section 10(b)'s application as determined by this Court will have far-reaching consequences. For example, other U.S. regulatory laws such as the Commodities Exchange Act often take their cue from U.S. securities

be that the . . . test in some cases will result in the Exchange Act's application of claims of manipulation of share value from afar.").

As exemplified by uADRs, applying Section 10(b) to all domestic transactions effectively forces foreign companies to comply with U.S. securities laws. *But see Morrison*, 561 U.S. at 269 (noting the "interference with foreign securities regulation that application of § 10(b) abroad would produce"). Since uADRs can be established without any input from foreign companies, foreign companies cannot stop others from transacting in them. Additional Form F-6 Eligibility Requirement at 54,645 (establishing a uADR "does not involve the formal participation, or even require the acquiescence of, the foreign company whose securities will be represented by the ADRs"). *See supra*, p. 3. Thus, anyone who transacts in a uADR in the U.S. could unilaterally drag the respective foreign company into Section 10(b) litigation. Other aspects of the transaction, such as whether the foreign company even intended or acted to access the U.S. market are irrelevant. *See Stoyas*, 896 F.3d at 949 ("[I]t does not matter that a foreign entity was not engaged in the transaction" at issue.). As such, if a foreign company without any contacts to the U.S. market can be sued under Section 10(b), the only way a foreign company can truly protect itself is to actually comply with U.S. securities laws.[2]

---

laws. *See, e.g.*, *In re London Prime Int'l Trading, Ltd. v. BP P.L.C.*, 937 F.3d 94, 107 (2d Cir. 2019).

[2] Even if a foreign company precluded the creation of uADRs by sponsoring its own ADR, the company would then be forced under standard practices to "arrange for the exercise of voting rights, the distribution of proxy materials, and forwarding of shareholder communications" to the sponsored ADR holders – all at its own expense. Additional Form F-6 Eligibility Requirement at 54,645.

Conversely, limiting Section 10(b)'s application to transactions that both occur in the U.S. and are sufficiently domestic better respects *Morrison*'s aims. A plaintiff cannot unilaterally drag a foreign company into Section 10(b) litigation because a transaction's other relevant aspects like a foreign company's intent and conduct matter. *Cf. Giunta v. Dingman*, 893 F.3d 73, 82-83 (2d Cir. 2018) (holding a transaction sufficiently domestic because it occurred in the U.S. and the foreign issuer actively solicited funds from a U.S. citizen). As such, a foreign company can choose to avoid the U.S. market and its laws or access it and comply. Thus, the presumption against extraterritoriality is upheld and participants in the global securities market can look to the clearly defined limits of Section 10(b).

b. If Section 10(b) applies simply because a transaction occurred in the U.S., conflict between U.S. and foreign securities laws will be ubiquitous

Application of Section 10(b) should be limited to avoid interfering with foreign securities laws. *See Parkcentral*, 763 F.3d at 215 ("[I]f an application of the law would obviously be incompatible with foreign regulation, and Congress has not addressed that conflict, the application is one which Congress did not intend."). While this is not always possible, allowing any domestic transaction to bind a foreign company under Section 10(b) "would so obviously implicate the incompatibility of U.S. and foreign laws that Congress could not have

---

Moreover, depending on the type of sponsoring, the company may have to comply with U.S. securities laws. *Id.* Regardless, the foreign company is still deprived of choice because it is forced to sponsor ADRs.

intended it *sub silentio*." *Id.* at 216. "Such a rule would inevitably place § 10(b) in conflict with the regulatory laws of other nations." *Id.* at 215. *See Morrison*, 561 U.S. at 269 ("[T]he regulation of other countries often differs from ours as to what constitutes fraud, what disclosures must be made . . . and many others.").

As such, it is "'presum[ed] that United States law governs domestically but does not rule the world.'" *Kiobel v. Royal Dutch Petroleum Co.,* 569 U.S. 108, 115 (2013) (quoting *Microsoft v. AT&T Corp.,* 550 U.S. 437, 454 (2007)). Meanwhile, "[f]oreign conduct is [generally] the domain of foreign law. *Microsoft*, 550 U.S. at 455. With this understanding, U.S. and foreign securities laws are mutually respected, and comity is maintained. *See Predictability and Comity: Toward Common Principles of Extraterritorial Jurisdiction*, 98 HARV. L. REV. 1310, 1321 (1985) (hereinafter "*Predictability and Comity*") ("It is . . . important that other nations consider United States jurisdictional policy to be fair.").

Thus, under U.S. securities laws, to be represented by a uADR, a foreign security only has to be listed on a foreign exchange and accompanied by documents in English showing that the security's issuer is compliant with relevant foreign securities laws. 17 C.F.R. § 240.12g3-2(b)(1). The SEC intended this requirement "to help assure that <u>there is a non-U.S. jurisdiction that principally regulates and oversees</u> the trading of the issuer's securities and the issuer's disclosure obligations to investors." Exemption from Registration Under Section 12(G) at 52,755 (emphasis added). *See also id.* at 52,753.

Notably, the SEC does not require additional disclosures or requirements outside of those under the relevant foreign securities laws.

If Section 10(b) is applied at the pull of a hair trigger such as a domestic transaction, foreign companies are forced to comply with U.S. securities laws as noted previously, and comity is broken. *See supra*, p. 11; *Predictability and Comity* at 1321 ("If other nations believe that American policy unfairly disadvantages their citizens . . . , they are apt to resist enforcement efforts and perhaps to retaliate with countermeasures of their own."). Moreover, such an application might be seen as an aggressive expansion of U.S. laws, and foreign jurisdictions may not be so kind to U.S. companies in the near future. *See Kiobel*, 569 U.S. at 124 (warning that if the U.S. applies its laws extraterritorially, other nations "could hale our citizens into their courts").

Conversely, by considering a domestic transaction's other relevant aspects to determine the applicability of Section 10(b), the Court creates a rational record examining U.S. interests while respecting foreign jurisdictions. Indeed, under this approach, one relevant aspect might be whether a foreign regulator is already investigating the alleged fraud behind the transaction at issue. *See*, *e.g.*, *Parkcentral*, 763 F.3d at 216 (holding a transaction as predominantly foreign when it involved investigations by German authorities into allegedly fraudulent statements made in Germany regarding stock in a German company).

3. Section 10(b)'s "in connection with" requirement cannot reliably filter truly foreign from domestic transactions

Likely aware of the deluge of litigation to come under its application of Section 10(b), the Ninth Circuit in *Stoyas* notes that predominantly foreign claims will be filtered out because Section 10(b) requires the fraud at issue to be "in connection with" the transaction. *See* 896 F.3d at 951. However, this reliance on Section 10(b)'s "in connection with" requirement is a mistake because that requirement is easily met. *See SEC v. Rana Research, Inc.*, 8 F.3d 1358, 1362 (9th Cir. 1993) ("[I]f fraud alleged 'somehow touches upon' or has 'some nexus' with 'any securities transaction,'" the "in connection with" requirement is met.). *See also Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit,* 547 U.S. 71, 85 (2006); *SEC v. Zandford,* 535 U.S. 813, 825 (2002).

"Any statement that is reasonably calculated to affect the investment decision of a reasonable investor will satisfy the 'in connection with' requirement." Thomas Lee Hazen, *Treatise on the Law of Securities Regulation* § 12:20 (6th ed. 2009). Further, an alleged fraud does not even have to relate to the security issued. *See Rana Research Inc.,* 8 F.3d at 1362-63 (holding that a consultant's press releases were "[s]tatements 'calculated' to influence investors"). Moreover, whether the issuer is a party to the transaction at issue is immaterial. *See SEC v. Tex. Gulf Sulphur Co.*, 401 F.2d 833, 860 (2d Cir. 1968) (en banc) ("There is no indication that Congress intended that the corporations or persons responsible for the issuance of a misleading statement would not violate the section unless they engaged in related securities transactions.").

Thus, because the "in connection with" requirement focuses on how an investor is affected as opposed to a transaction's relevant aspects, it is an inappropriate tool for distinguishing between truly foreign and domestic transactions. Under an "in connection with" analysis, Alcollezione as an Italian company with shares exclusively listed on the Borsa Italiana is no different from a U.S.-based company with shares listed on the New York Stock Exchange. That Alcollezione's statements regarding Frizzantissimo were made to an Italian audience to raise capital from Italian investors has no bearing on whether Petitioners relied on the statements. That Petitioners relied on the statements in transacting the uADRs is enough to satisfy the "in connection with" requirement.

Moreover, since the "in connection with" requirement is examined only after Section 10(b)'s scope has been determined, it is not an appropriate substitute for determining whether Section 10(b) applies at all. *See Stoyas*, 896 F.3d at 950-51 ("*Morrison* delineates the transactions to which the Exchange Act can theoretically apply without being impermissibly extraterritorial, but while applicability is necessary, it is not sufficient to state an Exchange Act claim.").

B. Section 10(b) is inapplicable to the transaction here because the transaction here is predominantly foreign

Looking to the economic reality of the transaction in Alcollezione uADRs at issue, the transaction here is predominantly foreign even if it occurred in the U.S. *See Reves v. Ernst & Young*, 494 U.S. 56, 61 (1990) ("In discharging our duty, we are not bound by legal formalisms, but instead take account of the economics of the transaction under investigation.”).

First, the transaction here is predominantly foreign because the uADR here represented shares in Alcollezione, an Italian company operating in Italy, that were only available on the Borsa Italiana. *See Parkcentral* at 216 (holding a transaction as predominantly foreign because it was connected to shares in a German company operating in Germany that were only available on European stock exchanges); *In re Societe Generale Sec. Litig.*, 2010 WL 3910286, at *5 (S.D.N.Y. Sept. 29, 2010) (“Where, as here, domestic plaintiffs purchased shares of a foreign bank traded on a foreign exchange, the Exchange Act is inapplicable.”).

Second, the transaction here is predominantly foreign because Alcollezione’s statement about Frizzantissimo was made in Italy by agents of Alcollezione, an Italian entity, to Italian investors. *See cf. Giunta*, 893 F.3d at 82-83 (holding a transaction as sufficiently domestic because a U.S. citizen’s statement about his holding company was made in the U.S. to another U.S. citizen). That Alcollezione’s investor materials were put on its website and translated into English is immaterial given the ubiquitous use of English in business. *See*, *e.g.*, 17 C.F.R. § 240.12g3-2(b)(1)(iii) (requiring basic company information in English to qualify for exemption from U.S. securities laws).

Third, the transaction here is predominantly foreign because Alcollezione intentionally avoided entering the U.S. securities market. *See cf. Giunta*, 893 F.3d at 82-83 (holding a transaction as sufficiently domestic because after establishing a direct agreement with a U.S. investor, a defendant issuer later contacted that investor in the U.S. to solicit further capital). Here, Alcollezione declined Petitioner's suggestion to set up a U.S. subsidiary and then declined to sponsor ADRs representing its shares. In doing so, Alcollezione never solicited capital from the U.S. market and intentionally avoided being bound by U.S. securities laws.

In transacting in the uADRs at issue here without obtaining proper approval from Alcollezione,[3] Petitioners are responsible for dragging Alcollezione into this mess. *See In re Societe Generale Sec. Litig.*, 2010 WL 3910286 at *6 (holding a transaction predominantly foreign because the ADR at issue "[was] not traded on an official American securities exchange" and instead "traded in a less formal market with lower exposure to U.S.-resident buyers"). Unsurprisingly, with the exception of *Stoyas*, Section 10(b) has never been applied to uADRs – only sponsored ADRs. *See*, *e.g.*, *Reese v. Malone*, 747 F.3d 557 (9th Cir. 2014); *Freidus v. Barclays Bank PLC*, 734 F.3d 132 (2d Cir. 2013).

[3] Marconi's well-wishing in response to Schutt's abrupt call discussing the formation of uADRs representing Alcollezione shares is hardly considered consent in standard business practices. Exemption from Registration Under Section 12(G) at 52,762.

II. AN EMPLOYEE WHO AT THE INSISTENCE OF A SUPERIOR, INSERTS A FALSE OR MISLEADING STATEMENT INTO INVESTOR MATERIALS, IS NOT SUBJECT TO PRIMARY LIABILITY UNDER RULE 10(B)-5(A) OR (C)

Section 10(b) of the Exchange Act prohibits the use of any "manipulative or deceptive device" in connection with the purchase and sale of securities. 15 U.S.C. § 78j. Rule 10(b)-5, promulgated thereunder, makes it unlawful for any person to "(a) employ any device, scheme, or artifice to defraud, (b) 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 the light of the circumstances under which they were made, not misleading, or (c) engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security." 17 C.F.R. § 240.10b-5.

A. Disseminators of information are not subject to primary liability under Rule 10(b)-5(a) or (c) in private actions

In *Lorenzo v. SEC*, 139 S. Ct. 1094 (2019), the Supreme Court determined that disseminators of misstatements may be liable under Rule 10(b)-5 subsections (a) and (c) in SEC actions, even if they do not "make" those statements for purposes of subsection (b). 139 S. Ct. at 1100. This is not an SEC action and *Lorenzo* should not apply.

1. <u>Expanding the private cause of action is contrary to Congress' intent</u>

Section 10(b) does not expressly create a private cause of action. *See, e.g., Halliburton Co. v. Erica P. John Fund, Inc.*, 573 U.S. 258, 267 (2014). Although the Supreme Court has recognized an implied private right of action, the right remains a "judicial construct that Congress did not enact in the text of the relevant statutes." *Stoneridge Inv. Partners, LLC v. Sci.-Atlanta*, 552 U.S. 148, 164 (2008).

The decision to expand the private cause of action is for Congress, not for the courts. *Stoneridge*, 552 U.S. at 165. *See also*, *Halliburton*, 573 U.S. at 284-85 (Thomas, J., concurring) ("The authority to fashion private remedies to enforce federal law belongs to Congress alone."). Absent Congressional intent, the judiciary's recognition of an implied right of action conflicts with the authority of Congress under Art. III to set the limits of federal jurisdiction. *Stoneridge*, 552 U.S. at 165-66.

Congress has not demonstrated an intent that the private cause of action reach disseminators, and in fact has expressed that it should not. The decision in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994) led to calls for Congress to create an express cause of action for aiding and abetting Section 10(b) violations. *Stoneridge*, 552 U.S. at 158. In 1994, then–SEC Chairman Arthur Levitt testified before the Senate Securities Subcommittee and recommended that aiding and abetting liability in private claims be established. S. Hearing No. 103–759, pp. 13–14 (1994). Congress did not follow this course and instead limited coverage of aiders and abettors by passing the Private Securities Litigation Reform Act of 1995 ("PSLRA"). *Stoneridge*, 552 U.S. at 162. In Section 104 of the PSLRA, Congress directed that aiders and abettors be prosecuted exclusively by the SEC. *Id.* at 158.

Dissemination of false information is conduct Congress intended to be enforceable only by the SEC. Disseminating, but not "making," misstatements constitutes aiding and abetting a Rule 10(b)-5(b) violation. *Lorenzo*, 139 S. Ct. at 1104. Such conduct cannot simultaneously constitute a primary violation of subsections (a) and (c) reachable by private plaintiffs, since Congress intended for aiding and abetting to be enforceable only by the SEC. Therefore, expanding the private cause of action to disseminators is outside the judiciary's authority.

2. <u>Subjecting disseminators to a private cause of action is inconsistent with the sharp distinction drawn between primary and secondary liability in prior Supreme Court holdings</u>

By recognizing that Congress intended that the private right of action remain narrow, the Supreme Court repeatedly refused to expand the right in *Central Bank*, *Stoneridge*, and *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011). *Central Bank* drew a clear line between primary and secondary liability in Section 10(b) violations; primarily liability is enforceable by private plaintiffs while secondary liability is only enforceable by the SEC. 511 U.S. at 191. Subjecting disseminators of false information to primary scheme liability would convert secondary violators into primary violators in breach of *Central Bank*'s clear line.

Stoneridge held that private plaintiffs cannot bring Section 10(b) suits for undisclosed deceptions upon which the plaintiffs could not have relied. *Id.* at 165. In that case, suppliers and customers of a cable-box company were not subject to scheme liability when they entered into business agreements that allowed the company to produce inflated financial statements. 552 U.S. at 155.

Entering into contracts that were never disclosed to the public was "too remote to satisfy the requirement of reliance." *Id.* Collapsing secondary misstatement liability into primary scheme liability is inconsistent with *Stoneridge*'s rule of excluding those who play a disconnected role in the release of information from private action.

In addition, only "makers" of misstatements can be primarily liable for the misstatements. *Janus*, 564 U.S. at 142. "Makers" of statements are those with ultimate authority over the statement, including its content and method of communication. *Id.* The term was defined narrowly to accord with the narrow scope of the private right of action. *Id.* Those who do not "make" misstatements can at most be liable as aiders and abettors. *Id.* In *Janus*, an investment advisor was not liable for false information contained in mutual fund prospectuses because only its parent company had authority over the prospectuses. *Id.* Subjecting disseminators to primary scheme liability contradicts *Janus*' view that private plaintiffs cannot bring suit for misstatements against those who do not "make" the misstatements.

3. <u>Blurring the distinction between primary and secondary liability in the private context will substantially increase the number of securities lawsuits.</u>

Creating a private cause of action for disseminating false information would drastically increase the number of defendants who would qualify as primary violators. The SEC retains the exclusive power to bring Section 10(b) aiding and abetting suits under 15 U.S.C. § 78t(e). Therefore, the SEC may prosecute the dissemination of misstatements regardless of whether it might also have a claim for a deceptive scheme. *See id.* Extending the same right to private plaintiffs, on the other hand, would create causes of action where there otherwise is none. Countless parties could simply repackage their misstatement claims under scheme liability theories, thereby drastically increasing the number of lawsuits. Even the Court in *Stoneridge* foresaw that subjecting remote participants to primary liability would allow the private cause of action to "reach the whole marketplace in which the issuing company does business." 552 U.S. at 160.

Judicial economy is especially important given a recent surge in securities lawsuits. In 2017, the courts saw 432 shareholder class action lawsuits accusing companies of making false or misleading statements, an increase of 44 percent from the previous year. Jonathan Stempel, "A Lawsuit a Day; U.S. Securities Class Actions Soar," REUTERS (Jan. 29, 2018), https://www.reuters.com/article/us-stocks-classaction/a-lawsuit-a-day-u-s-securities-class-actions-soar-idUSKBN1FI2FM. This was the highest since 1995 when Congress passed the PSLRA, which implemented procedural safeguards to Section 10(b) actions. *Id.* Much of that increase was attributable to a growing number of frivolous lawsuits which were either dismissed or settled for insignificant amounts. *Id.* A clear line between primary and secondary liability must be maintained in order deter frivolous lawsuits and reduce caseload.

B. Cato's conduct does not violate the text of Rule 10(b)-5(a) or (c)

1. Scheme liability requires conduct beyond mere misstatements and some degree of planning or intentional wrongdoing.

Statutory language must be interpreted to give effect to every clause and part of the statute. *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 566 U.S. 639, 645 (2012). When a statute or regulation contains both a general provision and a specific one, the "general/specific canon" is applied to resolve inconsistencies between them. *Id.* Under this canon, "the specific governs the general," meaning the specific enactment is operative while the general provision only governs activity not within the provisions of the particular. *Id.* at 646 (quoting *D. Ginsberg & Sons, Inc.*, 52 St. Ct. 322). This method of construction is necessary to avoid "the superfluity of a specific provision that is swallowed by the general one." *Id.* at 645.

Here, subsection (b) of Rule 10(b)-5 specifically addresses misstatements, while subsections (a) and (c) prohibit deceptive "schemes" and "practices" more generally. *See, Aaron v. SEC*, 446 U.S. 680, 696 (1980). In order to give effect to every aspect of Rule 10(b)-5 and to avoid the superfluity of the misstatement prohibition, subsection (b) must be operative while (a) and (c) must govern "additional kinds of illegalities." *Lorenzo*, 139 S. Ct. at 1110 (Thomas, J., dissenting).

Thus, fraudulent schemes must encompass conduct beyond mere misrepresentations or omissions. *Pub. Pension Fund Group v. KV Pharm. Co.*, 679 F.3d 972, 987 (8th Cir. 2012). *See also*, *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 177 (2d Cir. 2005). A complaint alleging facts identical to those in a misstatement or omission claim will not survive a motion to dismiss a deceptive scheme claim. *Id.* For example, in *WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc.*, 655 F.3d 1039, 1058 (9th Cir.2011), alleging that founders of a computer company conferred together to refrain from disclosing a secondary securities sale was not sufficient to plead scheme liability. The complaint only contained facts that were "fundamentally the same as an omission claim." *Id.* Conversely, in *SEC v. Seethruequity, LLC*, 2019 U.S. Dist. LEXIS 71997, at *13 (S.D.N.Y. Apr. 26, 2019), a complaint adequately alleged scheme liability because it claimed that defendants' "entire business model, beyond any misstatements or omissions" was deceptive.

In addition, the scheme liability provisions imply some form of planning or intentional wrongdoing. The Court in *Lorenzo* acknowledged that the dictionary definitions of the Rule 10(b)-5(a) terms "device", "scheme," and "artifice" encompass planning, designing, devising and strategizing. 139 S. Ct. at 1101 (quoting, *Aaron v. SEC*, 446 U.S. 680, 696, n. 13, (1980)). These definitions carry a connotation of "knowing or intentional practices" such as price rigging, short-selling and wash sales. *See id.* at 1107. For example, in *Swack v. Credit Suisse First Bos.*, 383 F. Supp. 2d 223, 239 (D. Mass. 2004) an investment bank was subject to scheme liability when it worked extensively with the CEO of a company to issue bullish research reports with the deliberate aim to boost the company's stock price. Administrative acts like disseminating information does not amount to the same level of calculated, intentional deception. *Lorenzo*, 139 S. Ct. at 1108 (Thomas, J., dissenting).

2. <u>Cato merely performed ministerial acts under pressure from a superior which does not constitute a deceptive scheme</u>

Cato performed ministerial acts which do not constitute conduct more than mere misstatements or omissions. Like in *WPP Luxembourg*, in which company founders conferring together to prevent disclosure of a securities sale was fundamentally the same as a material omission, here, drafting assurances and condensing them into a disclosure does not amount to conduct beyond a mere misstatement. In fact, if conferring together to deceive investors is not sufficient to plead a deceptive scheme, then surely individual ministerial acts like summarizing legal information at the direction of a superior is not either. Furthermore, unlike in *Seethruequity*, in which a complaint adequately alleged scheme liability by claiming an entire business model was deceptive, here, Cato is not subject to scheme liability because the alleged wrongdoings only pertain to the release of inaccurate assurances regarding the regulatory landscape. Inaccurate assurances by themselves do not evidence larger fraudulent business practices that go beyond misstatements.

In addition, Cato performed the ministerial tasks at the insistence of a superior, which does not reflect any sort of planning or intentional wrongdoing. Marconi pressured Cato through statements like "listen, this is happening with or without you" and "it is better to ask for forgiveness than permission." Marconi also convinced Cato that releasing assurances without compliance was commonplace when stating, "these things always find a way of getting resolved" and "this sort of thing is perfectly common in business." An inexperienced lawyer adhering to a CEO's commands does not reflect strategizing or intent to defraud. Unlike in *Swack* in which the investment bank worked extensively with a company to issue inflated research reports with a deliberate aim to boost stock prices, here, Cato did not strategize extensively with other Alcollezione executives. She simply obeyed orders, which is far from a calculated, intentional scheme like price rigging, short-selling or cross sales.

C. Even if disseminators of false information are subject to primary liability under Rule 10(b)-5(a) and (c) in private actions, Cato escapes liability because she is not a disseminator

The Supreme Court acknowledged in *Lorenzo* that subjecting disseminators of false information to scheme liability “may present difficult problems of scope in borderline cases. 139 S. Ct. at 1101. “Purpose, precedent, and circumstance could lead to narrowing their reach in other contexts.” *Id.* Cato’s conduct is precisely that which “dissemination” should not encompass.

Disseminating false information in violation of the scheme provisions involves direct interaction and communication with investors. *See id.* In *Lorenzo*, the director of investment banking Lorenzo at a registered broker-dealer disseminated information by sending two emails to investors overstating the value of the total assets held by an energy company. *Id* at 1099. At the direction of his boss, the disseminator signed the emails with his own name, identified himself as “Vice-President—Investment Banking,” and invited the recipients to “call with any questions.” *Id.*

Disseminating information in violation of the scheme provisions also requires certainty that the statements are false. In *Lorenzo*, the investment banking director was subject to scheme liability because he sent “emails he understood to contain material untruths." *Id.* at 1101. The director knew that the energy company owned less than $400,000 in assets and that its intellectual property was worthless. *Id.* Yet, he forwarded and signed emails stating the company had "10 million dollars in confirmed assets." *Id.*

Cato did not disseminate false information because she did not demonstrate a sufficient level of interaction and communication with investors. Unlike in *Lorenzo* in which the director of investment banking disseminated information by sending two emails directly to potential debenture purchasers, here, Cato did not disseminate information because she drafted assurances regarding the Italian regulatory landscape and condensed them into disclosures. These disclosures were later inserted into slide decks and footnoted in pro forma financial statements. Investors did not receive the assurances until Marconi presented the slide decks and pro forma financial statements at the Annual Meeting. Therefore, Cato only participated remotely in the eventual release of regulatory assurances. "Purpose, precedent and circumstance" should dictate that a line be drawn at those who play a direct role in communicating information. The securities laws did not envision holding disconnected participants primarily liable.

Additionally, Cato did not disseminate misstatements because she was not certain that the information contained in the disclosures was false. Unlike in *Lorenzo*, in which investor emails clearly mischaracterized the value of company assets, here, the assurances regarding the regulatory landscape were not totally inaccurate. Cato's research indicated that regulatory approval of

Frizzantissimo would be an “uphill climb” and at worst “unlikely in the short-term.” Therefore, assurances that the product would be approved and ready for the market in the second quarter of 2018 had some possibility of being true. Furthermore, Cato’s drafts were based on her own assessment of the legal landscape. Such analysis is always subject to some doubt, especially when conducted by a recent graduate. Cato could not have disseminated misstatements if she had some confidence that the statements would turn out to be true.

CONCLUSION

For the reasons stated herein, Respondent respectfully requests this Court to affirm the decision of the United States Court of Appeals for the Fourteenth Circuit.

Dated: March 2, 2020

Respectfully submitted,

/s/ Team R11

Team R11
Counsel of Record for Respondent

APPENDIX

APPENDIX 1

15 U.S.C. § 78j(b):

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange – (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78t(e):

(e) Prosecution of persons who aid and abet violations

For purposes of any action brought by the Commission under paragraph (1) or (3) of section 78u(d) of this title, any person that knowingly or recklessly provides substantial assistance to another person in violation of a provision of this chapter, or of any rule or regulation issued under this chapter, shall be deemed to be in violation of such provision to the same extent as the person to whom such assistance is provided.

17 C.F.R. § 240.10b-5:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) 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 the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

APPENDIX 2

17 C.F.R. § 240.12g3-2(b):

(1) A foreign private issuer shall be exempt from the requirement to register a class of equity securities under section 12(g) of the Act (15 U.S.C. 78*l*(g)) if:

(i) The issuer is not required to file or furnish reports under section 13(a) of the Act (15 U.S.C. 78m(a)) or section 15(d) of the Act (15 U.S.C. 78o(d));

(ii) The issuer currently maintains a listing of the subject class of securities on one or more exchanges in a foreign jurisdiction that, either singly or together with the trading of the same class of the issuer's securities in another foreign jurisdiction, constitutes the primary trading market for those securities; and

(iii) The issuer has published in English, on its Internet Web site or through an electronic information delivery system generally available to the public in its primary trading market, information that, since the first day of its most recently completed fiscal year, it:

(A) Has made public or been required to make public pursuant to the laws of the country of its incorporation, organization or domicile;

(B) Has filed or been required to file with the principal stock exchange in its primary trading market on which its securities are traded and which has been made public by that exchange; and

(C) Has distributed or been required to distribute to its security holders.