Docket No. 19-508

IN THE

Supreme Court of the United States

THE FORDHAM PUBLIC EMPLOYEES INVESTMENT FUND,

Petitioner,

v.

GORDON

Respondent.

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

BRIEF FOR PETITIONERS

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1. Is an officer of a company primarily liable under §10b of the Securities Exchange Act of 1934 when she organizes all information included in a memorandum and directs an employee to distribute that memorandum to investors?
2. Is a plaintiff entitled to a presumption of reliance under *Affiliated Ute* in a mixed case that alleges both omissions and affirmative misstatements?

STATEMENT OF THE CASE

1. Statement of the Facts

In 2017, Ms. Underwood and Ms. Scott acquired a business for $75 million and renamed it Gemstar. R. at 1-3. The company's most popular product was the SwiftMax, a machine tool that produced fasteners for cargo jet aircrafts. *Id.*

Ms. Underwood and Ms. Scott began to pursue a private placement as an exit strategy in 2021. *Id.* at 4. Katie Gordon, Gemstar's Vice President of Investor Relations, helped spearhead the private placement. *Id.* She alone was entrusted with coordinating the work of "Gemstar's experts," a hodgepodge of attorneys, financial advisors, auditors, engineering firms, and others. *Id.* Under her organization, they compiled what would become known as "the Memo"—the principal marketing agent that was to inform potential investors in the private placement. *Id.*

In May 2021, Gordon was alerted to a serious problem. The report on the structural integrity of Gemstar's products, submitted by the principal engineering firm, contained a "Trade Letter," with academic support, suggesting that the SwiftMax could develop microscopic cracks over time. *Id.* Moreover, the Trade Letter warned that these cracks could develop during extreme conditions, such as aircraft takeoffs. *Id.* at 6.

Ms. Gordon never delivered this information to Gemstar's experts. *Id.* Instead, she met with Ms. Underwood and Ms. Scott to discuss the potential problem. *Id.* The ultimate decision was to ignore the Trade Letter entirely, and Ms. Gordon decided "she could live with it." *Id.*

Come August 2021, the Memo was ready, *sans* Trade Letter. *Id.* In fact, the Memo, serving as the principal marketing document, made no mention of the risk of microscopic cracks *at all*. *Id.* Instead, the Memo contained three boilerplate statements about Gemstar's assets, indicating that Gemstar's assets are in "reasonable condition," its products are not "materially defective," and that "[t]here are no material undisclosed contingent liabilities relating to Gemstar's products." *Id.*

Ms. Gordon then directed her associate to distribute the Memo to potential investors. *Id.* One of those investors, the Fordham Public Employees Investment Fund ("the Fund"), then purchased 3,000,000 shares at $27 per share. *Id* at 7. Although the Memo did not mention Ms. Gordon's title, the Fund was aware of her role in creating the Memo. *Id.*

At the end of 2021, there was an explosion on a cargo jet upon takeoff. *Id.* The FAA identified the source of the issue as two fasteners, each manufactured using the SwiftMax. *Id.* Investigations revealed that the fasteners had developed microscopic cracks, thus substantiating the findings included in the Trade Letter. *Id.* One month after the FAA released their preliminary findings, the Fund sold its position at just $4 per share. *Id.* The Fund suffered a staggering $68 million in losses. *Id.*

2. Procedural History

In March 2022, the Fund commenced a private action in the United States District Court for the District of Fordham. R. at 8. The action was brought under Section 10(b) of the Securities Exchange Act of 1934 and Rule

10b–5, the Exchange Act's implementing regulation. *Id.* Gemstar and three of its executives, including Ms. Underwood, Ms. Scott, and Ms. Gordon, were named as defendants. *Id.* The Fund alleged that the company, along with its executives, engaged in a deceptive scheme to conceal material contingent liabilities relating to the defective composite. *Id.*

In September 2022, each executive filed a separate motion to dismiss under Rule 12(b)(6) for failure to state a claim upon which relief can be granted. *Id.* In her motion, Ms. Gordon asserted that she is not primarily liable because she did not make or disseminate the Memo's statements. *Id.* She further argued that the Fund failed to allege that it or its advisors relied on the Memo. *Id.* at 9.

In October 2022, the District Court for the District of Fordham denied Ms. Gordon's motion to dismiss. *Id.* The court found that although Ms. Gordon was not a "maker" of misleading statements or material omissions, she is still primarily liable as a "disseminator." *Id.* Moreover, the court found that the Fund did not need to allege reliance because the Fund is entitled to a presumption of reliance under *Affiliated Ute*. *Id.*

On appeal, the Fourteenth Circuit affirmed the District Court's holding that Ms. Gordon can be held primarily liable under Rule 10b-5. *Id.* at 23. However, the Circuit Court reversed the District Court's holding that the Fund is entitled to a rebuttable presumption of reliance under *Affiliated Ute*. *Id.* Finding no allegations concerning proof of reliance, the Circuit Court granted

Ms. Gordon's motion to dismiss. *Id.* Petitioners sought certiorari in this Court. *Id.* at 30. Their petition was granted in January of 2023. *Id.*

SUMMARY OF ARGUMENT

I

Ms. Gordon is liable as a primary violator under §10b of the Securities Exchange Act of 1934. Under *Lorenzo*, although Ms. Gordon did not "make" misleading statements or omissions, she is still a "disseminator." Moreover, Ms. Gordon's conduct clearly falls within subsections (a) and (c) of Rule 10b–5, which are provisions that impose scheme liability. As Vice President of Investor Relations, Ms. Gordon was entrusted with compiling Gemstar's Memo that served as the chief marketing tool for potential investors. She organized the experts involved in its creation, knew that the owners chose to omit a material contingent liability, and directed the Memo's distribution to potential investors. Directing her associate to distribute the Memo does not shield Ms. Gordon from liability. Instead, this Court's precedent and the express language of Rule 10b–5 mandate that Ms. Gordon be found primarily liable.

II

The Fund is entitled to a rebuttable presumption of reliance under *Affiliated Ute*. Although this case involves both omissions and affirmative misrepresentations, this case is one that primarily alleges omissions. Moreover, recognizing a presumption of reliance in this case is consistent with the purpose underlying *Affiliated Ute*. Despite a duty to disclose, Ms. Gordon omitted information material to the private placement. Moreover, requiring the

Fund to prove reliance is an impossible and unreasonable burden. In light of both the language of *Affiliated Ute* and its purpose, the Fund is entitled to a presumption of reliance.

ARGUMENT

I. Ms. Gordon is primarily liable under Rule 10b–5 because her conduct falls within scheme liability as set out in *Lorenzo*.

Whether a defendant can be found primarily liable depends on the text and purpose underlying the Exchange Act and Rule 10b–5. In response to the Great Depression and markets ripe with fraudulent conduct, Congress enacted the Securities Exchange Act of 1934 "to substitute a philosophy of full disclosure for the philosophy of *caveat emptor*." *SEC v. Cap. Gains Rsch. Bureau, Inc.*, 375 U.S. 180, 186 (1963). See also U. Pa. J. Bus. L. 843, 851. The Act's anti-fraud provision, §10(b), makes it unlawful "[t]o use or employ, in connection with the purchase or sale of any security… any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe." 15 U.S.C. §78j. This provision's implementing regulation, Rule 10b–5, expands on the phrase "manipulative or deceptive devices" by specifically stating that it is unlawful:

> "(a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any unlawful statement of material fact…, or
>
> (c) To engage in any act, practice, or course of business which operates… as a fraud or deceit."

17 C.F.R. 240.10b–5. *See United States v. O'Hagan*, 521 U.S. 642, 651 (1997). Together, the Exchange Act and its accompanying regulation work to further the goal of protecting buyers and sellers, while ensuring business transparency.

Although there has been longstanding recognition of private actions under Rule 10b–5 despite no explicit directive from Congress, private actions differ from criminal actions brought by the SEC. To limit liability in private causes of action, courts distinguish between primary and secondary violators. A private of action is recognized only against the former, leaving secondary violators under the purview of the SEC alone. 15 U.S.C. § 78t(e). *See also Stoneridge*, 552 U.S. 148, 157. A primary violator is someone who directly contravenes one or more subsections of Rule 10b–5, which contrasts secondary violators, who are more akin to aiders and abettors of the principal actor. An example of a secondary violator is an accountant who prepares false financial statements for an executive, where the executive is the one who actually makes and disseminates the information to investors. The accountant, however, can be subject to liability in a private action if she, as a secondary actor, "commit[s] primary violations." *Id.* at 166.

Ms. Gordon is primarily liable for fraudulent activity because she is a "disseminator." She organized the construction of the Memo and knew that it contained material misrepresentations and omissions. Although the Memo was indirectly distributed through her associate, Ms. Gordon exercised substantial control over the Memo, making her a "disseminator" under *Lorenzo*. However, it is important to remember that the label of "disseminator" is a proxy for determining whether someone is directly in contravention of one of Rule 10b–5's subsections, which is what primary liability really turns on. Because of her role, Ms. Gordon engaged in a fraudulent scheme and course of business, clearly placing her within the scope of subsections (a) and (c) of Rule 10b–5. Because she engaged in a primary violation of Rule 10b–5, she is liable as a primary violator, regardless of whether she is labeled as a "disseminator."

A. By directing its delivery to investors, Gordon "disseminated" the Memo with the intent to defraud, which exposes her to primary liability under *Lorenzo*.

To proactively protect investors, this Court has recognized the need to interpret Rule 10b-5 flexibly, most notably in *Lorenzo*. *See Lorenzo v. SEC*, 139 S. Ct. 1094 (2019). The defendant in *Lorenzo*, as Vice President at an investment banking company, sent "false statements directly to investors." *Id.* at 1101. Because he did not "make" the statements, the question posed was whether or not he was a primary violator. In answering this question, the Court sought to address indeterminacies arising from a previous case, *Janus*. *See Janus Cap. Grp., Inc. v. First Derivative Traders*, 564 U.S. 135, 142 (2011) (holding that "the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it").

Under *Janus*, only "makers" of false statements are primarily liable. *Id.* Although the defendant in *Lorenzo* would not be liable under this standard, the Court would not let the defendant off so easy. To avoid shielding an actor who blatantly engages in fraudulent activity, the majority in *Lorenzo* imposed liability under subsections (a) and (c) of Rule 10b–5, noting how inclusive the language is—the plain meanings of "scheme" or fraudulent "course of business" obviously encompasses Lorenzo's activities. *Id.* at 1101.

In its ruling, the *Lorenzo* court effectively cabined *Janus*, rejecting the notion that a primary violator could only be someone who "makes" the fraudulent statement. *Id* at 1103. The effect of *Lorenzo* is an additional, separate realm of malfeasance, denoted as "dissemination." *Id.* "Dissemination" requires control of fraudulent material that is spread, even if it is in service of a fraudulent scheme for which the disseminator is not the principal actor. *Id.* This means individuals can be found primarily liable, regardless of their position within a company, so long as they exercise significant control over fraudulent activity. The Court justified their expansive definition of fraudulent conduct by pointing to the Exchange Act's purpose, which is to stamp out fraud in the securities market. Notably, *Lorenzo* does not impose unlimited liability. The scope of liability is limited by the protection of aiders and abettors, which the Court upheld. *Id.*

Ms. Gordon's behavior is analogous to the defendant in *Lorenzo*. Their titles *and* roles are similar. Each title indicates the officers' significance and autonomy—both individuals faced little oversight from supervisors and both individuals contributed heavily to the decisions of their respective company. And as Vice President for Investor Relations, Ms. Gordon was the point person for fielding questions and concerns from institutions interested in investing in

Gemstar. Because both Ms. Gordon and the defendant in *Lorenzo* exercised significant control over statements directed toward potential investors, both are primarily liable despite not being the "makers" of such statements.

The fact that Ms. Gordon directed her associate to send the Memo is of no consequence. To illustrate this point, the *Lorenzo* court's hypothetical involving a mail room clerk is helpful. *Id*. at 1101. The *Lorenzo* court held that it would be inappropriate to hold a mailroom clerk liable for dissemination. *Id.* The Court reasoned that the clerk is tangentially involved in the underlying fraud, only performing ministerial duties. *Id*. In order to preserve the distinction between primary and secondary violators, the task of this Court is to distinguish between those who exercise significant control and those who simply aid and abet by carrying out ministerial duties. If the Court is willing to recognize the mail room clerk's role as so tangential as to warrant protection from liability, delegation to such individuals should not dilute the controlling role of superiors like Ms. Gordon. Ms. Gordon's use of an associate does not obviate her as the source of the dissemination. To hold otherwise would be to license fraud, so long as the fraudulent conduct is delegated to an inferior, regardless of how trivial that inferior's authority is.

Respondents would have us believe that Ms. Gordon is herself the mail room clerk, carrying out the demands of other executives. But this is not so. The *Lorenzo* court's choice of a mail room clerk in their hypothetical suggests that the court was thinking of shielding only low-skilled, ministerial workers from liability—people who would likely not understand the intricacies of a fraudulent scheme. Ms. Gordon's responsibilities obviously extend beyond those of a mail room clerk, indicated by the fact that she has associates to help her distribute the Memo. Second, the mail room clerk does not play any role in the creation of the mail. Ms. Gordon, while not "making" the Memo under *Janus*, still played a pivotal role in its creation. "Her primary responsibility was to manage the flow of information." R. at 5. This is not typically within the scope of a mail room clerk's responsibility or even capability, which explains why Ms. Gordon's role, responsibilities, and control distinguish her from the mail room clerk and expose her to primary liability.

Ms. Gordon was the true source of dissemination. Although *Lorenzo* limited *Janus*, *Janus* is still instructive in determining whether someone's involvement in a scheme rises to the level of a primary violation. In its definition of "make," the *Janus* court emphasized the party to whom the work is attributed. This necessarily shields from liability someone like a speechwriter, who literally creates words, but does not bear the imprimatur of the speech when delivered. In other words, *Janus* indicates that courts should look toward the individual who exercises the most control over the dissemination process. In our case, that person is Ms. Gordon. She was entrusted with controlling the entire memo process and communicating her work product to potential investors. While the dissemination was not literally done by her hand, she was the putative face of the dissemination as Vice President of Investor Relations. Whether the paper bore her name or not, she was the person that a reasonable investor would rely on, and the Fund knew of her role in the construction of the Memo. R. at 7.

Additionally, policy considerations favor imposing primary liability on Ms. Gordon. Recognizing a more expansive conception of primary liability would deter officers from implementing the schemes of their superiors and would deter superiors from delegating fraudulent conduct to their inferiors. Without imposing primary liability in cases such as this, if executives who do not literally “make” statements can find a way to obscure their involvement, they would be free to disseminate false statements. Similarly, if this Court finds that Ms. Gordon can escape liability because she simply followed other executive’s orders, individuals will be encouraged to participate in the schemes constructed by their superiors. A broad definition of primary liability combats this by providing an internal check on the fraudulent activities within companies.

Finding Ms. Gordon primarily liable as a “disseminator” does not impose unlimited liability. The *Lorenzo* dissent argues that the language in subsections (a) and (c) is only meant to cover “planning, scheming, designing, or strategizing.” *Id.* at 1108. For the dissent, widening the reach of subsections (a) and (c) would lead to a runaway liability issue, where these provisions would encompass too much conduct. *Id.* But Ms. Gordon’s conduct would fall within these subsections regardless of how narrowly they are read. Compared to *Lorenzo* who only “cut and pasted” false statements, Ms. Gordon met with other executives to orchestrate the dissemination, creating a plan to omit material information from the Memo. *Id.* at 1106; R. at 6. With only three people in the room, it is difficult to imagine that Ms. Gordon was not intimately involved in the plan. So, even if subsections (a) and (c) are read even narrower than the *Lorenzo* court's reading, primary liability still attaches to Ms. Gordon as a "disseminator," thus preserving the narrow application of subsections (a) and (c) that the *Lorenzo* dissent sought jealously to protect.

B. **Even if Ms. Gordon is not a "disseminator," subsections (a) and (c) of Rule 10b–5 reach her conduct.**

To implement the will of Congress, this Court has read §10(b) "flexibly, not technically and restrictively." *Superintendent of Ins. of N.Y. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 12 (1971). The *Lorenzo* Court implies that, when fraud is "obvious" and falls within the "natural meaning" of the statutory language, courts should look to impose primary liability, subject to some limiting principle. *Lorenzo*, 139 S. Ct. 1094, 1101. So, when confronted with clearly fraudulent acts performed by a public-facing executive, this Court should presume that Congress intended to cover this conduct via the wide reach the Exchange Act and Rule 10b–5. If this Court were to conclude that Ms. Gordon is not a "disseminator" under *Lorenzo*, she is still primarily liable under scheme liability.

The *Lorenzo* court properly recognized expanded scheme liability imposed by subsections (a) and (c) to include individuals acting as disseminators. *Lorenzo*, 139 S. Ct. 1094, 1099. Still, the Court did not expand primary liability so far as to reach the outer bounds of Congress' intent. In *Rio Tinto*, the Second

Circuit told us that in recognizing the liability of "disseminators," the Court was providing us with only "one example of something extra that makes a violation a scheme." *SEC v. Rio Tinto PLC*, 41 F.4th 47, 50 (2d Cir. 2022). So even if Ms. Gordon is found not to be a "disseminator," the wide reach of subsections (a) and (c) indicate that this Court can still recognize Ms. Gordon's conduct as "something extra" that triggers primary liability. Ms. Gordon's conduct constitutes a primary violation within the scope of Rule 10b-5 regardless of which label attaches to her.

Interpreting subsections (a) and (c) as encompassing Ms. Gordon's conduct would best honor Congress' intent to stamp out fraudulent conduct. Such an approach would be an appropriate judicial response to individuals who engage in fraudulent schemes but seek to obscure their involvement by delegating some portion of the fraudulent conduct.

A broad interpretation of these provisions still fits within the confines of Rule 10b–5. The fact that the regulation includes three separate categories demonstrates that the regulation is meant to encompass a wide range of fraudulent activity. While some contend that a broad reading of subsections (a) and (c) would render subsection (b) superfluous, statutes and regulations are often promulgated with provisions that have overlapping applications, especially when Congress or an agency seeks to impose a directive with wide-reaching application. A strict application of the presumption against superfluity would require construing Rule 10b–5 in such a way that a "scheme" in subsection (a) could never also be covered by a fraudulent "course of business" in subsection (c). Such a strained and narrow reading would be unnecessary and undesirable.

Circuit courts have disagreed about the proper scope of subsections (a) and (c). The inconsistency among circuit courts should be resolved in a way that furthers Congress' goal of stamping out fraud and allowing the securities market to function efficiently. In *Simpson*, the Ninth Circuit held that an actor may be primarily liable if she acted with "the principal purpose and effect of creating a false appearance in deceptive transactions as part of a scheme to defraud." *Simpson v. AOL Time Warner, Inc.*, 452 F.3d 1040, 1052 (9th Circ. 2006). Courts in the Fifth and Eighth Circuit interpret Rule 10b–5 narrowly, requiring fraudulent misstatements or omissions for primary liability to attach. *See Regents of the Univ. of Cal. v. Credit Suisse First Boston*, 482 F.3d 372 (5th Cir. 2007); *see also Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 443 F.3d 987, 992 (8th Cir. 2006) (concluding that a defendant cannot be held primarily liable if he "does not make or affirmatively cause to be made a fraudulent misstatement or omission").

The Fifth and Eighth Circuit's reading of Rule 10b–5 renders only subsection (b), the provision covering misstatements and omissions, operable. In contrast, the Ninth Circuit's expansive interpretation of scheme liability gives force to all subsections under the rule. Since Congress sought to replace a doctrine of *caveat emptor* in favor of punishing fraudulent activity, the Ninth Circuit's interpretation of Rule 10b–5 is broad enough to reach a wide range of fraudulent activities, and, therefore, this interpretation best serves Congress' intent. Notably, Ms. Gordon's conduct would easily fall within the Ninth Circuit's broad interpretation of Rule 10b–5.

Respondents contend that such a broad interpretation would destroy the distinction between primary and secondary liability. The mandate against imposing primary liability on aiders and abettors in private causes of action is strong. See *Stoneridge*, 552 U.S. 148, 162 (rejecting interpretations that "make[] any aider and abettor liable under §10(b) if he or she committed a deceptive act in the process of providing assistance"). Imposing primary liability on Ms. Gordon still respects the protection of aiders and abettors. Rather than simply providing assistance, Ms. Gordon unilaterally controlled the flow of information to investors and was entrusted with creatin the primary marketing material for potential investors. She thus acted much more independently and with much more control than the defendants in *Stoneridge*. R. at 5.

Imposing wide-reaching scheme liability would best serve Congress' interest in allowing victims of fraud to recover compensatory damages. The *Lorenzo* court expanded the range of individuals exposed to liability in private actions because they worried claims brought by the SEC would not be sufficient by themselves to punish all fraudulent activity. *Lorenzo*, 139 S. Ct. 1094, 1104. Thus, *Lorenzo* sought to empower private citizens to pursue causes of action that hold individuals responsible for fraudulent conduct, even if they are not a "maker" of statements under *Janus*. Broadening the scope of scheme liability and further empowering citizens to recover would help ensure that Rule 10b–5 is enforced to the extent that Congress intended.

In summary, Ms. Gordon is primarily liable under Rule 10b–5 because she is a "disseminator." Even if this Court finds that she is not, subsections (a) and (c) are wide-reaching. Under a broad interpretation of Rule 10b–5, Ms. Gordon is in direct contravention of both subsections and is thus primarily liable. Imposing primary liability in this case conforms with both the text of the Exchange Act and Rule 10b–5, while also best serving the purpose underlying the statute and regulation.

II. The Fund is entitled to a rebuttable presumption of reliance under *Affiliated Ute.*

In a typical private cause of action for securities fraud, the plaintiff bears the burden of proving that they relied upon a material misrepresentation or omission. Securities Exchange Act of 1934, § 10, 15 U.S.C.A. § 78j; *see also Sharpe v. Coopers & Lybrand*, 649 F.2d 175, 188 (3d Cir. 1981) (holding that "[a] steadfast rule requiring the defendant to refute a presumption of reliance would be neither equitable nor logical"). However, "to assist courts in managing circumstances in which direct proof . . . is rendered difficult," the Court has recognized rebuttable presumptions of reliance, effectively shifting the burden of proof to the defendant. *Basic Inc. v. Levinson*, 485 U.S. 224, 245 (1988) (establishing the fraud-on-the-market presumption); *see also Sharpe*, 649 F.2d at 188 (finding that "[t]he reason for shifting the burden on the reliance issue has been an assumption that the plaintiff is generally incapable of proving that he relied on a material omission"). More importantly for this case, in *Affiliated Ute*, the Court found that a presumption of reliance arises when a defendant omits the truth rather than affirmatively misrepresents it. *Affiliated Ute Citizens of Utah v. U.S.*, 406 U.S. 128, 153–54 (1972).

Mixed cases, which involve both omissions and affirmative misleading or false statements, have given rise to two competing strands of case law under *Affiliated Ute*. On one hand, some courts will apply a standard that looks to whether a mixed case primarily alleges omissions or misrepresentations. On the other hand, some courts will apply a flexible approach, recognizing a presumption of reliance only when there is a duty to disclose, materiality, and an unreasonable evidentiary burden. The courts that take the latter approach look to whether a presumption of reliance is consistent with the purpose of *Affiliated Ute*. The Fund is entitled to a presumption of reliance under either of these standards.

A. The Fund is entitled to a presumption of reliance because this is a case primarily about omissions.

Affiliated Ute holds that in cases that "involv[e] primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery." *Id.* But while this gives a clear directive in cases that purely allege only omissions, mixed cases that involve both omissions and affirmative misrepresentations present significant complications. *See Little v. First California Co.*, 532 F.2d 1302, 1304 n.4 (9th Cir. 1976) (finding that "[t]here is a true dilemma [when] there has been a general representation from which material facts are omitted and there is no independent alternative ground" to justify a presumption). The Court's lack of guidance in such instances has exacerbated this quandary.

However, this dilemma has not stopped courts from ruling on mixed cases. Seizing on *Affiliated Ute*'s explicitly stated application to "cases involving *primarily* a failure to disclose," some courts have applied a "primarily alleges omissions" standard to cases involving a mix of omissions and misrepresentations. *Affiliated Ute*, 406 U.S. at 153–54 (emphasis added). These courts hold that "the presumption is only appropriate if the case can be characterized as 'primarily a nondisclosure case.'" *In re Volkswagen "Clean Diesel" Marketing, Sales Practices, and Products Liability Litigation*, 2 F.4th 1199, 1204 (quoting *Binder v. Gillespie*, 184 F.3d 1059, 1064 (9th Cir. 1999); *see also Desai v. Deutsche Bank Securities Ltd.*, 573 F.3d 931, 940 (9th Cir. 2009) (holding that "[t]he presumption . . . is limited to cases that 'can be characterized as ... primarily alleg[ing] omissions'"). Among the circuits that have addressed mixed cases, "the preferred approach is to . . . 'analytically characterize [the] action as either primarily a nondisclosure case (which would make the presumption applicable), or a positive misrepresentation case.'" *Binder*, 184 F.3d at 1064 (citing *Finkel v. Docutel/Olivetti Corp.*, 817 F.2d 356, 359 (5th Cir.1987) and *Austin v. Loftsgaarden*, 675 F.2d 168, 178 n.21 (8th Cir.1982)). To apply this standard, courts categorize cases on a fact-specific basis. Although simple in theory, applying this application has proven difficult without express guidance from the Court.

Under this standard, the present case is one that primarily alleges omissions. Naturally, courts look to the plaintiff's complaint to determine whether a case primarily *alleges* omissions. *See, e.g., Joseph v. Wiles*, 223 F.3d

1155, 1162 (10th Cir. 2000) (justifying its holding on "the nature of the allegations contained in the complaint"). According to the Record, the Fund alleges omissions twice. First, the Fund alleges that it relied on "material omissions." R. at 8. Second, the Fund alleges that Ms. Gordon "engag[ed] in a deceptive scheme to conceal material contingent liabilities relating to the defective composite." *Id.* This is not a case about the generic, boilerplate information that was contained in the Memo. Although this information certainly constitutes affirmative misrepresentations, these statements do not constitute the "deceptive scheme to conceal material contingent liabilities" that the Fund alleges. *Id.* Even Ms. Gordon saw these affirmative representations as "routine" and nothing more. *Id.* at 5. Rather, this case is primarily about information obtained and then subsequently withheld by Ms. Gordon, the high-ranking officer charged with "manag[ing] the flow of information" to potential investors. *Id.* Because the Fund primarily alleges Ms. Gordon's role in withholding information, this case falls within the category of cases that "primarily allege omissions," which entitles plaintiffs to the *Affiliated Ute* presumption.

Recognizing a presumption of reliance in our case would not mean that *Affiliated Ute*'s application is unlimited. In mixed cases, the presumption of reliance recognized by *Affiliated Ute* is cabined by some important limitations, one of which arises when an omission is simply the inverse of an affirmative misrepresentation. For example, in *In re Volkswagen*, a court declined to extend a presumption of reliance because "the omission is of the truth that certain affirmative statements allegedly misrepresent." *In re Volkswagen*, 2 F.4th at 975.

The Fund's alleged omissions are not the "inverse" of Ms. Gordon's affirmative misrepresentations. While it is true that the Memo contained generic statements referring to Gemstar's products, omitting highly-technical information about a defective composite is not the inverse of including boilerplate information about Gemstar's products that Ms. Gordon considered "routine." R. at 5. If the court were to find otherwise, individuals marketing investments could make broad, generic statements such as "there are no material deficiencies in the health of the company." The inverse of such a statement would be the omission of any risks or deficiencies that are material to the company's health, ensuring that virtually any omission is the inverse of the generic statement. By simply making generic statements, defendants could ensure that plaintiffs never benefit from a presumption of reliance. Because holding the omission in this case to be the inverse of the generic statements included in the Memo would lead to similarly absurd results, the omission of information about the defective composite is not the inverse of the boilerplate statements about Gemstar's assets and products. Rather, the omission of information regarding the product defect entitles the Fund to a presumption of reliance.

B. Recognizing a presumption of reliance is consistent with the purpose underlying *Affiliated Ute*.

Although many courts attempt to categorize cases as either primarily about omissions or primarily about misrepresentations, some courts find that a more holistic approach makes sense. Rather than seizing on the *Affiliated Ute* court's language about "cases involving primarily a failure to disclose," some courts look to whether a presumption of reliance is consistent with the purpose of *Affiliated Ute*. *Affiliated Ute*, 406 U.S. at 154. Courts typically recognize a presumption of reliance as consistent with *Affiliated Ute*'s purpose when three factors are met: there is a duty to disclose, the undisclosed fact is material, and it is impossible for a plaintiff to bear the burden of proving reliance. Such a standard is much more practicable than a "primarily alleges omissions" standard and better conforms with the language of *Affiliated Ute*. Under this standard, the Fund is entitled to a rebuttable presumption of reliance.

A "primarily alleges omissions" standard creates more problems than it addresses. The classification of a case as primarily alleging omissions collapses in on itself when one realizes that "[t]he categories of 'omission' and 'misrepresentation' are not mutually exclusive. All misrepresentations are also nondisclosures, at least to the extent that there is a failure to disclose" the truth. *Little v. First California Co.*, 532 F.2d at 1304 n.4; *see also Grae v. Corrections Corporation of America*, 329 F.R.D. 570, 583 (M.D.T. 2019) (finding that omissions and misleading statements "are little more than the same lie seen from different angles"). Because every misrepresentation, by definition, omits the truth, "every plaintiff can style his or her complaint as a material misrepresentations or omissions case." *Simpson v. Specialty Retail Concepts*, 823 F.Supp. 353, 356 n.7 (M.D.N.C. 1993). It is unlikely that the *Affiliated Ute* court intended the presumption of reliance to turn on this sort of gamesmanship.

Courts that construe *Affiliated Ute* as requiring a rigid categorization of cases are thus engaged in an artificial exercise to determine whether a case is primarily about statements or omissions, even if a case might wholly be about both. "The only way out of this seeming conundrum, as far as the court can tell, is to construe the scope of Affiliated Ute narrowly, or, at least, narrowly enough to avoid creating an exception that swallows the rule." *Grae*, 329 F.R.D. at 583; *see, e.g.*, *Joseph*, 223 F.3d at 1163 (holding that it "cannot allow the mere fact of this concealment to transform the alleged malfeasance into an omission rather than an affirmative act. To do otherwise would permit the *Affiliated Ute* presumption to swallow the reliance requirement almost completely"); *Johnson v. HBO Film Management, Inc.*, 265 F.3d 178, 193 (3d Cir. 2001).

In light of the impracticability of a "primarily alleges omissions" standard, many courts simply ask whether recognizing a presumption of reliance would be consistent with the purpose of *Affiliated Ute. E.g. In re Volkswagen*, 2 F.4th at 974 (citing *Waggoner v. Barclays PLC*, 875 F.3d 79 (2d Cir. 2017) (finding that a "focus on the purpose behind Affiliated Ute was a helpful touchstone"). This standard offers a more flexible, holistic approach for determining whether a presumption of reliance applies. *See Sharpe*, 649 F.2d at 189 (finding that "a flexible approach avoids the potential problems of a broad judicial pronouncement of a precept governing reliance”). These courts will focus on whether there is a duty to disclose, whether the undisclosed fact is material, and whether it is impossible for the plaintiff to bear the burden of proof.

An approach that focuses on the underlying purpose of *Affiliated Ute* is supported by both the language of *Affiliated Ute* and policy considerations. In *Affiliated Ute*, the Court explicitly stated that the “obligation to disclose and [the] withholding of a material fact establish the requisite element of causation in fact.” *Affiliated Ute*, 406 U.S. at 154 (citing *Chasins v. Smith, Barney & Co.*, 438 F.2d 1167 (2d 1970)). Thus, *Affiliated Ute* suggests that when both a duty to disclose and the materiality of a fact are established, courts are more willing to recognize reliance and shift the burden of proof to the defendant. The Ninth Circuit also pointed out that failing to recognize a presumption when a plaintiff faces a an unreasonable evidentiary burden would “threaten[] to defeat valid claims implicit in *Affiliated Ute*” and would “lead[] to underinclusive recoveries and thereby threaten[] the enforcement of the securities laws.” *Blackie v. Barrack*, 524 F.2d 891, 908 (9th Cir. 1975). Because both *Affiliated Ute* and the circuit courts who have interpreted the case look toward a duty to disclose, the materiality of the omitted fact, and the reasonableness of the evidentiary burden, applying a standard that incorporates these three factors makes sense.

Entitling the Fund to a presumption of reliance would be consistent with the purpose underlying *Affiliated Ute*. First and foremost, as a threshold question, a court will look to whether there is a duty to disclose. Without such a duty, nondisclosure cannot lead to a presumption of reliance, or even a successful action against securities fraud. *Chiarella v. U.S.*, 445 U.S. 222, 228 (1980) (finding that "one who fails to disclose material information . . . commits fraud only when he is under a duty to do so"); *see also Basic*, 485 U.S. at 239 n.17 (holding that "[s]ilence, absent a duty to disclose, is not misleading under Rule 10b–5"). This is why the *Affiliated Ute* court focused on the plaintiffs' "right to know" information that the defendants possessed. *Affiliated Ute*, 406 U.S. at 153.

To determine whether there is a duty to disclose, courts will look at whether there is a relationship of trust and confidence between parties to a transaction. *Chiarella*, 445 U.S. at 230. Determining whether there is a relationship of trust and confidence is case-specific, and courts will look to multiple factors, including the relationship between the parties, their relative access to information, and the benefit that the defendant derives from the relationship. *Jett v. Sunderman*, 840 F.2d 1487, 1493 (9th Cir. 1988).

The relationship between the Fund and Ms. Gordon was one of trust and confidence, which creates a duty to disclose. Compared to parties in an impersonal market transaction who owe no duty of disclosure absent an agency or fiduciary relationship, the Memo was distributed directly to financial institutions for the purpose of marketing Gemstar's stock. R. at 5–6. By creating the Memo used to market the stock, Ms. Gordon clearly owed a duty to disclose all facts material to the promoted transaction. Courts have recognized a duty to disclose in cases involving much less between parties. *See, e.g.*, *Grae*, 329 F.R.D. at 583 (holding that a duty to disclose can arise when a party "make[s] public statements on a topic material to a securities transaction"). Moreover, because Ms. Gordon, along with Ms. Underwood and Ms. Scott, had an interest in engaging in the private placement, the defendants were in a position to benefit from the transaction. Finally, Ms. Gordon's "primary responsibility was to manage the flow of information." R. at 5. Ms. Gordon's role as VP of Investor Relations within the company as well as her role in creating the Memo put her in a position with significantly more access to information relative to the Fund, further underscoring her obligation to disclose.

Materiality, although often seen as an element independent of reliance, is a factor considered in determining whether a presumption of reliance is consistent with *Affiliated Ute*'s underlying purpose. Courts look toward the materiality of an undisclosed fact in their reliance inquiry because "the test [for determining reliance] is properly one of tort 'causation in fact,'" meaning that reliance establishes the causal connection between the fraudulent conduct, the transaction, and ultimately the injury. *Chasins v. Smith*, 438 F.2d at 1172 (quoting *Crane Co. v. Westinghouse Air Brake Co.*, 419 F.2d 787 (2d Cir. 1969)). Courts determine a fact's materiality because only nondisclosure of a *material* fact will cause a reasonable investor to engage in the fraudulent transaction. *See Bell v. Cameron Meadow Lands Co.*, 669 F.2d 1278, 1283 (holding that a "finding of nonreliance implies that plaintiffs would have acted no differently had they known the truth"). Thus, "reliance is no longer 'an element independent of causation and materiality in a case under Rule 10b–5.'" *Rowe v. Maremont Corp.*, 850 F.2d 1226, 1233 (7th Cir. 1988).

For a court to recognize a causal connection, and thus a presumption of reliance, the fact in question must be material such that there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." *Basic*, 485 U.S. at 231–232 (quoting *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)). The undisclosed product defect eventually caused an explosion on a plane, with a subsequent 85% decrease in Gemstar's share price. R. at 7. Information concerning this product defect would definitely alter the "total mix" of information that reasonable investors use to forecast potential investment opportunities. Even Ms. Gordon was alarmed when she initially read the Trade Letter. R. at 6. Even though she calmed down upon seeing that the letter was three years old, this was a peculiar reaction given that the defective composite develops microscopic cracks *over time*. *Id.* Information about the product defect is unquestionably material to reasonable investors because any reasonable investor would be interested in a potential defect in a company's most popular product.

It is no answer to point out that the probability of the product defect was low. "Whether information concerning speculative or contingent events . . . is material depends 'upon a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity.'" *Rowe*, 850 F.2d at 1235 (quoting *Basic*, 485

U.S. at 986–987). The record gives us no indication of how large or small the probability was of the SwiftMax developing microscopic cracks. But even if the chance of a product defect transpiring is low, that probability is still balanced against the remarkable magnitude of the negative consequences flowing from a defect in "[Gemstar's] most popular product[,] the SwiftMax." R. at 4. Because of the sheer magnitude of these consequences, information about the product defect is material, even if the probability of the defect actually materializing is relatively low.

Finally, and perhaps most importantly, courts will recognize a presumption of reliance as consistent with the underlying purpose of *Affiliated Ute* when a plaintiff faces an impossible or otherwise unreasonable evidentiary burden. In *Wilson v. Comtech*, a court found that "the rationale for a presumption" is that "reliance as a practical matter is impossible to prove." *Wilson v. Comtech*, 648 F.2d 88, 93 (2d Cir. 1981); *see also Blackie*, 524 F.2d at 907 (recognizing a presumption of reliance when the plaintiff faces "an unreasonable and irrelevant evidentiary burden"); *Joseph v. Wiles*, 223 F.3d at 1162 (holding that "the *Affiliated Ute* presumption of reliance exists in the first place to aid plaintiffs when reliance on a negative would be practically impossible to prove").

Without a presumption of reliance, it would be impossible for the Fund to bear the burden of proof. In *Blackie*, a court recognized a presumption of reliance when bearing the burden of proof would require the plaintiff to determine some "speculative possibility in an area where motivations are complex and difficult to determine." *Blackie*, 524 F.2d at 908. The circumstances under which the product defect was omitted certainly constitutes "an area where motivations are complex," and the Fund cannot bear the burden of specifically proving their reliance on Ms. Gordon's actions, or lack thereof. Ms. Gordon, the external engineering firm, the departed junior engineer, Ms. Scott, and Ms. Underwood all had a hand in creating the Memo. R. at 5–6. There are simply too many interactions between too many people to require the Fund to bear the burden of proof. The Respondent, as someone who took part in such interactions, is in a far better position to bear the burden of proof. This Court should thus use a presumption of reliance to shift the burden onto the party best equipped to bear it. The purpose of *Affiliated Ute* is best served by shifting the burden away from the Fund, which would otherwise face insurmountable obstacles to proving reliance.

Regardless of which standard this Court adopts, the Fund is entitled to a rebuttable presumption of reliance under *Affiliated Ute*. Holding otherwise would contravene both the language and purpose of *Affiliated Ute*.

PRAYER FOR RELIEF

For the foregoing reasons, Petitioners respectfully request that both holdings of the lower court be REVERSED. We ask this Court to hold (1) that an officer be held primarily liable under §10b of the Securities Exchange Act of 1934 when she organizes all information included in a memorandum and directs an employee to distribute that memorandum toward potential investors, and (2) recognize a presumption of reliance under *Affiliated Ute* in mixed cases when the case primarily alleges omissions, there is a duty to disclose, the omitted fact is material, and the plaintiff cannot bear the burden of proof.