Team No. P11

Docket No. 22-123

In the

Supreme Court of the United States

FORDHAM PUBLIC EMPLOYEES INVESTMENT FUND

Petitioner,

v.

Katie Gordon, et al.

Respondent.

On Writ of Certiorari to the Circuit Court of Fordham

BRIEF FOR PETITIONERS

QUESTIONS PRESENTED

1. Whether Ms. Gordon who neither made nor distributed false or misleading statements can be subject to primary liability as a "disseminator" under Rule 10-b5(a) and (c), for instructing an employee to distribute the statements to investors.
2. Whether the rebuttable presumption of reliance under *Affiliated Ute* applies where the plaintiff asserts "mixed" allegations involving both omissions and affirmative misrepresentations.

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15 U.S.C. §78(j).

15 U.S.C. §78t(e).

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17 CFR §240.10b-5.

STATEMENT OF JURISDICTION

The United States District Court for the District of Fordham had jurisdiction pursuant to 28 U.S.C. § 1331 (2012). The United States Court of Appeals had jurisdiction pursuant to 28 U.S.C. § 1291. The Fund timely filed a petition for a writ of certiorari, which this Court granted on January 9, 2023. This Court has jurisdiction under 28 U.S.C. § 1254(1) (2012).

STATEMENT OF THE CASE

Grace Underwood and Danielle Scott ("The Owners") met in New York City around June of 2014, shortly after graduating from elite post-graduate business institutions. (J.A. 1). In addition to their elite education, both individuals had inherited substantial wealth given to them by their parents: their combined wealth approximated over $50,000,000. (J.A. 1). Soon after, Ms. Scott and Ms. Underwood decided to pool their inherited wealth and purchase an underperforming small or mid-sized manufacturing company. (J.A. 1-2).

In January of 2017, the search was concluded, and a broker introduced the parties to McGrath, Inc., a large manufacturing company that planned to spin off and sell its sophisticated machine tool business. (J.A. 2). The parties agreed to a price of $75,000,000, subject to due diligence and standard closing conditions, and Ms. Underwood and Ms. Scott each put up $10,000,000 in cash to complete the purchase. (J.A. 2-3). As part of the due diligence the Owners retained an engineering firm, MMD Inc. ("MMD"), to examine the

business' property, plant, and equipment to ensure it was suitable for its intended use. (J.A. 2). MMD's report concluded that one of the composites used by their largest selling machine had been reported in the trade literature to have characteristics which might lead to the development of microscopic cracks over time and under stress. The owners were privy to this information but did not include it in the final due diligence review. (J.A. 3).

In January of 2018, after the transaction had close, the Owners renamed the new entity Gemstar. Ms. Underwood served as the Chief Executive Officer (CEO) and Danielle served as the President. (J.A. 3). They shared responsibility for making all material executive decisions. (J.A.). While running the company for the next three years the Owners turned the business into a large player in the sophisticated machine tool business. (J.A. 4). Gemstar's most successful product was called SwiftMax and was used to produce safety fasteners for many applications but was often specifically used for structural application on cargo aircraft. (J.A. 4). In 2021, The Owners began the process of realizing the financial benefits of their ownership. They decided on a sales structure that would involve relinquishing 80% of Gemstar stock ownership to institutional investors through private markets, while retaining 20% of the company in the form of super voting shares, which would allow them continued control of the executive business decisions. (J.A. 4).

Ms. Gordon Gordan, Gemstar's Vice President in charge of Investor Relations was tasked with coordinating the attorneys, financial advisors,

auditors, engineering firms, and assorted other experts to assist in the construction of the Private Placement Memorandum ("the Memo") which was to be used to attract buyers for the private market sale of 80% of Gemstar's stock. (J.A 5). As part of the construction of the Memo, Keane and Company, an engineering firm, delivered its report ("the Report) on the structural integrity of the company's assets to Ms. Gordon. The Report included a memorandum echoing the sentiment of the earlier due diligence that suggested that SwiftMax used a composite which overtime could produce cracks that would cause product failure under stress. (J.A. 5-6). Rather than include this information in the final report, Ms. Gordan decided to consult the Owners before proceeding. (J.A. 6). After meeting with the Owners Ms. Gordon removed this memorandum from the final documents she submitted to the enlisted experts to be included in the Memo construction. (J.A. 6). The Memo stated that Gemstar's property, plant, and equipment were in reasonable condition for their intended use. (J.A. 5-6). It also said there were no material defects in the products sold to customers and there were no material undisclosed contingent liabilities relating to its products which were required to be noted in its financial statements. (J.A. 6).

In August of 2021, Ms. Gordan directed one of her subordinate associates to distribute the Memo to twenty-six large, non-banking financial institutions for the purpose of soliciting investments. (J.A. 6). In October 2021, the private placement had been completed, and the Fordham Public Employees

Investment Fund ("the Fund") had placed their beneficiaries retirements in the hands of Gemstar to the tune of $81,000,000. (J.A. 7)

Only two months later, a cargo plane, using fasteners fabricated using SwiftMax, suffered an explosion on the right side of the plane. (J.A. 7). The FAA conducted an investigation following the explosion and determined that it occurred because the fasteners used were unable to support the engines weight and conclusively determined that this was because the fasteners had developed cracks that caused the product to fail during takeoff: exactly as the Report warned. A month after this failure, the Fund sold its entire position at a loss of $68,000,000 to the retirement funds of Fordham public employees. (J.A. 7).

Having suffered severe losses after Gemstar's product failure caused an explosion, the Fund sought damages from Gemstar commiserate with the loss suffered due to Gemstar's omission of the structural risks of their product in the Memo. (J.A. 8). The Fund points to three specific statement's to show material misstatements and omissions: (1) Gemstar's physical assets are in reasonable condition for their intended use, (2) None of Gemstar's products are materially defective, (3) There are no material undisclosed contingent liabilities relating to Gemstar's products. (J.A. 8).

The Fund alleges that Gemstar and its executives, Grace Underwood, Danielle Scott, and Ms. Gordon Gordon ("the Executives"), committed securities fraud in violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder ("the securities laws"), by engaging in a deceptive

scheme to conceal material contingent liabilities relating to the defective composite. (J.A. 8). In her individual motion to dismiss, Ms. Gordan argued that she did not disseminate the memos false and misleading statements, and thus could not be held liable as a primary violator under § 10(b) and Rule 10b-5. (J.A. 8). In October 2022, the District Court for the District of Fordham issued its opinion denying Ms. Gordon's motion to dismiss. (J.A. 8-9). The court held that Ms. Gordon could be held primarily liable, and that the Fund was entitled to a rebuttable presumption of reliance. (J.A. 8-9).

The Appellate Court stated that to recover damages the Fund must prove six factors: To prevail, the Fund must show: "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation." (J.A. 18). The Appellate court upheld the District court's ruling that Ms. Gordon can be held primarily liable under Rule 10b-5(a) which would satisfy the standing issue and allow a private right of action, but found that requiring the Fund to show positive proof of reliance would not impose an unrealistic burden, and thus they were not entitled to a rebuttable presumption of reliance and thus had not offered sufficient facts to prove element four. (J.A. 23). The Supreme Court granted Certiorari on these two issues. (J.A. 30).

SUMMARY OF THE ARGUMENT

Individuals, rather than the SEC, may bring suit for securities fraud when certain circumstances arise. These circumstances are not limited to occasions when a party "makes" or personally distributes false and misleading information. Primary liability arises when one disseminates such information and commits something beyond omission. Here, the fact that Ms. Gordon disseminated false and misleading information is not diluted by her instructing an associate to physically distribute the information.

STANDARD OF REVIEW

Appellate review of a District Court's denial of a motion to dismiss per Federal Rule of Civil Procedure 12(b)(6) is performed de novo. *See Crystallex Int'l Corp v. Petroleos De Venezuela, S.A.*, (3d Cir. 2018). To survive a 12(b)(6) motion to dismiss, the complaint must include "sufficient factual matter, accepted as true, to state a claim for relief that is plausible" that allows the court to "draw the reasonable inference that the defendant is liable for the misconduct alleged." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009).

ARGUMENT

I. MS. GORDON IS SUBJECT TO PRIMARY LIABILITY UNDER RULE 10b-5 BECAUSE SHE "DISSEMINATED" THE MEMO TO GEMSTAR'S INVESTORS CONTAINING FALSE AND MISLEADING INFORMATION.

Congress enacted securities laws in part to "root out all manner of fraud in the securities industry" by adopting broad and overlapping proscriptions that were designed to "meet the countless and variable schemes devised" by fraudsters. *Lorenzo v. Securities & Exchange Commission*, 139 S. Ct. 1094, 1102-1104 (2019); *Securities & Exchange Commission v. W.J. Howey Co.*, 328 U.S. 293, 299 (1946).

Specifically, §10(b) of the Securities Act of 1934 prohibits fraud in connection with the purchase and sale of any security; it grants the U.S. Securities and Exchange Commission (SEC) authority to make rules that target securities fraud. 15 U.S.C. §78(j). The SEC implements §10(b) through Rule 10b-5, which in turn contains three anti-fraud provisions: 10b-5(a), (b), and (c). 17 CFR §240.10b-5. Rule 10b-5 states that "it shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce. . . (a) to employ any device, scheme, or artifice to defraud, (b) to make any untrue statement of a material fact . . . or, (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit . . ." *Id.* This Court previously held that, in drafting and passing 10(b) into law, Congress expected courts to construe these anti-fraud proscriptions "not technically and restrictively, but flexibly." *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 151 (1972) (quoting *SEC v. Capital Gains Rsch. Bureau*, 375 U.S. 180, 195 (1963)).

As Circuit Judge Evaristo's majority opinion notes, this Court has recognized a private right of action for 10b-5 violations for over fifty years since

their decision in *Superintendent of Ins. of N.Y. v. Bankers Life & Casualty Co*. 404 U.S. 6, 13 n.9 (1971) ("it is now established that a private right of action is implied under s 10(b)."). Because this private action is "implied," as opposed to expressly written into the 1934 statute, the Court describes the action as a "judicial construct" and limits its extension. *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta*, 552 U.S. 148, 164-65 (2008). For example, in *Stoneridge* the Court rejected an interpretation of the 1934 Act that would extend primary liability in a private action to aiders and abettors of parties that have violated 10b-5's provisions. *Id.* at 165 ("[T]he decision to extend the cause of action is for Congress, not for us. Though it remains the law, the §10(b) private right should not be extended beyond its current boundaries."). The Court came to this conclusion in part because Congress had already reserved prosecution of aiders and abettors of 10b-5 violations–along with other types of "secondary violators"–to the SEC exclusively per 15 U.S.C. §78t(e). *Id.* at 158. Thus, primary violators of Rule 10b-5 can be the target of a private action, while secondary violators can only be brought into court by the SEC.

Given the broad and overlapping nature of 10b-5 proscriptions on fraudulent conduct, it can be difficult to distinguish the difference between a "primary" or "secondary" violator. In 2011, the Court attempted to draw a "clean line" through this rather blurry distinction in *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135 (2011). In *Janus*, the Court held that there was no private right of action per Rule 10b-5(b) for plaintiffs in a lawsuit against an investment advisory firm that helped draft misleading statements

that were later used in one of that firms' clients' prospectuses. *Id.* at 142. The Court ruled that because the defendants did not "make" the statements featured in the prospectus, the advisory firm did not have "ultimate authority" over the document, and therefore could not be a "primary violator" per Rule 10b-5(b). *Id.* at 142-143.

However, as the majority opinion in the present case notes: "the Court has recognized that an individual who is not liable under Rule 10b-5(b), for "making" false or misleading statements can still be held liable for "disseminating" those statements with the intent to defraud, under Rule 10b5-(a) and (c)." In *Lorenzo v. Securities & Exchange Commission*, the defendant (Lorenzo) worked for a broker-dealer firm and knowingly sent emails containing false statements to clients along with an invitation for his clients to call him if they had any questions. 139 S. Ct. 1094, 1099-1100 (2019). The Court found that Lorenzo could be found liable as a "primary violator" under 10b-5(a) and (c) because, by disseminating false statements to his firms' clients, he was "employing devices and schemes to defraud" and was "engaging in fraudulent or deceptive acts or practices." 17 CFR §240.10b-5(a) and (c); *see also Lorenzo*, 139 S. Ct. at 1100. Lorenzo's conduct therefore fell within Rule 10b-5's "expansive language." *Lorenzo*, 139 S.Ct. at 1101-02. The Court did, however, caution against applying 10b-5(a) and (c) to parties who are only "tangentially involved" in the dissemination of fraudulent information. *Id.* at 1099-1100.

Following *Lorenzo*, the Second Circuit attempted to delineate the specific difference between primary and secondary liability for a "scheme liability claim"

per Rule 10b-5(a) and (c) in *Securities & Exchange Commission v. Rio Tinto plc.*, 41 F.4th 47 (2d Cir. 2022). In *Rio Tinto*, the SEC brought a 10b-5 claim against defendants alleging that the defendants had circulated financial statements that contained false information about the quality of one of their coal mines. *Id.* at 48. The Second Circuit held that the defendants could not face primary liability under Rule 10b-5(a) and (c), because "something beyond misstatements and omissions" is required to form an actionable scheme liability claim. *Id.* at 49 (citing *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161 (2d Cir. 2005)). Among various actions constituting "something beyond" is the dissemination of false or misleading information. *Id.* at 54. *Rio Tinto*'s holding adhered to prior Second Circuit case law, such as *Lentell*, which held that misstatements and omissions cannot form the "sole basis" for liability under Rule 10b-5(a) and (c). *Id.* at 177 ("We hold that where the sole basis for such claims is alleged misrepresentations or omissions, plaintiffs have not made out a market manipulation claim under Rule 10b-5(a) and (c)."). While the court in *Rio Tinto* made it clear that its holding was "limited to the legal issue" of that specific case, the Court of Appeals in the present case held that the actions alleged in *Rio Tinto*–corrupting an audit and concealing information from auditors–is another type of "something beyond" behavior that can give rise to scheme liability under 10b-5(a) and (c). *Id.* at 53.

On appeal, Ms. Gordon argues she is not subject to primary liability under Rule 10b-5 because: (1) she did not "make" the false or misleading statements in the Memo sent to Gemstar's experts that would trigger 10b-5(b)

liability; and (2) her directing an employee, and not personally disseminating, the Memo to investors excludes her from the "disseminator" standard for 10b5(a) and (c) liability as demonstrated in *Lorenzo* and *Rio Tinto*. We concede Ms. Gordon did not incur 10b-5(b) liability but disagree with Ms. Gordon's argument that 10b-5(a) and (c) liability does not apply. As a disseminator of fraudulent information in violation of 10b-5(a) and (c), she should be subject to primary liability, as the District Court and Court of Appeals both found.

A. Finding Primary Liability with Ms. Gordon Is Consistent with Previous Applications of 10b-5(a) and (c).

Ms. Gordon should not dodge primary liability merely because she did not personally press "send" on the Memo with false or misleading information. While she did not send the Memo to investors personally, she instructed an associate to do so on her behalf, and therefore a private right of action should still be available to the petitioners, the Fordham Public Employees Investment Fund ("the Fund"). The Court of Appeals' decision in this case remains consistent with the Supreme Court's interpretation of 10b-5(a) and (c) as demonstrated in *Lorenzo*. Moreover, while we think that the Second Circuit's decision in *Rio Tinto* is consistent with the Court's decisions in *Janus* and *Lorenzo*, we believe that the facts of the present case are much closer to that of *Lorenzo* than *Rio Tinto*. Accordingly, Ms. Gordon should be subject to 10b-5(a) and (c)'s anti-fraud provisions.

The defendant in *Lorenzo* was found to be a "disseminator" of information and a "primary violator" of Rule 10b-5(a) and (c) because, in his capacity as

vice president, he knowingly emailed false statements to clients with an accompanying invitation for clients to personally call him if they had questions. 139 S. Ct. at 1099-1100. The Second Circuit did not find the defendant in that case to be a "disseminator" that was primarily liable under Rule 10b-5(a) and (c) because, while the SEC could prove that a misstatement and omission took place, it could not prove that the defendant did "something beyond" that. 41 F.4th 47 at 49, 54. In coming to their conclusion, the Court of Appeals in this case held that the "something extra" language from *Rio Tinto* was not limited to the "dissemination" of the misleading statement or omission, but could also include behavior such as "corrupting" an audit by "concealing information from auditors." While notable differences exist between the facts of the present case and the facts in *Lorenzo*, there is little doubt that Ms. Gordon was also responsible for "something extra" to the material misstatements and omissions that were circulated in the Memo to investors, unlike in *Rio Tinto*. Ms. Gordon not only disseminated the memo, but also corrupted the "Report" featured within the "Memo."

The "Memo" sent to investors in this case contained both misstatements and omissions of a material fact. The Memo, distributed to investors in August 2021, made no mention of the presence of "microscopic cracks" within Gemstar's SwiftMax composite. Rather, the document incorrectly stated that "Gemstar's property, plant, and equipment were in reasonable condition for their intended use." Not only did the document not mention the defective composite within Gemstar's product that led to Seaboard Airlines's accident in

December of 2021, but the document also stated that "there were no material defects in the products sold to customers and there were no material undisclosed contingent liabilities relating to its products." It was Ms. Gordon who personally "directed one of her associates to distribute" this Memo "to twenty-six of the country's largest non-bank financial institutions, under cover of Gemstar's stationery." This "plainly fraudulent" conduct falls within the scope of Rule 10b-5's "expansive language."

B. The Dissenting Circuit Court Opinion Mischaracterizes Ms. Gordon's Circumstance as Dissimilar to Precedent Finding Primary Liability.

Circuit Judge Kastenbaum's dissent argues that Ms. Gordon did not disseminate the false information within the Memo, but rather aided and abetted Grace and Danielle's plan, and should therefore not be held primarily liable under Rule 10b-5(a) and (c). We respectfully but fundamentally disagree with Judge Kastenbaum on this particular point. In reaching this conclusion, Judge Kastenbaum appears to argue that because the facts of *Lorenzo* are so different from the facts pertaining to Ms. Gordon, a different conclusion from that of *Lorenzo* must be reached. First, a one-to-one direct similarity between the facts of two cases is not required to reach the same conclusion of law. Second, the facts and themes between the defendant's conduct in *Lorenzo* and Ms. Gordon's at present contain enough similarities to render similar conclusions. While there are factual similarities between *Lorenzo* and the present case, such as the fact that both Lorenzo and Ms. Gordon conducted themselves in their "capacity as vice president" of their respective companies,

there are indeed several factual differences. Unlike in *Lorenzo*, Ms. Gordon did not personally correspond with Gemstar's investors when the Memo was given to them. Instead, she ordered her assistant to conduct this task on her behalf. In addition, unlike the defendant in *Lorenzo*, Ms. Gordon did not invite the investors to reach out to her if they had any questions, and Ms. Gordon's name was not mentioned on the Memo's cover letter.

However, the Court in *Lorenzo* did not implement stringent requirements that every future disseminator under Rule 10b-5(a) and (c) must share the same specific facts found in *Lorenzo*, such as the personal mailing of relevant documents or an invitation to follow up with the recipient of those documents. The Court rather saw "nothing borderline about this case," leaving room for other circumstances to give rise to dissemination of false or misleading material. *Lorenzo*, 139 S. Ct. at 1101. The differences between Ms. Gordon's situation and *Lorenzo* does not take away from the fact that, just like in *Lorenzo*, Ms. Gordon facilitated the Memo's dissemination. Similar to the defendant in *Lorenzo*, Ms. Gordon held responsibility for the document. Although her associate physically delivered the Memo to investors, we agree with the Court of Appeals that this employee served no role beyond that of a "mailroom clerk." Ms. Gordon was therefore not "tangentially involved" in this dissemination of false and misleading information to Gemstar's investors but firmly in the muck of it. *Id.* at 1100.

Ms. Gordon's status as a disseminator of the false and misleading information within the Memo is not the sole "something extra" to

misstatements or omissions from which primary liability under Rule 10b-5(a) and (c) can be found. Ms. Gordon, in her capacity as Vice President of Gemstar, "was tasked with . . . coordinat[ing] the attorneys, financial advisors, auditors, engineering firms, and other experts" while "the Memo" was being constructed for investors. She personally removed the information pertaining to the "defective composite" from the Report that Gemstar's experts were supposed to review. This certainly falls within the scope of "corrupting an audit" and "concealing information from auditors" that the Court of Appeals in this case held should also count as "something extra" for finding someone primarily liable under 10b5(a) and (c).

Judge Kastenbaum's dissenting opinion failed to consider how Ms. Gordon deliberately concealed deeply relevant information from expert auditors, lawyers, and engineers regarding the safety of one of Gemstar's products. There was purpose to her actions. Unlike the defendant in *Lorenzo*, Ms. Gordon did not merely send a drafted message, without collaborating on its substance. Ms. Gordon herself brought the defective composite to the attention of the presidents, which began the "plan, scheme, design, or strateg[y]." Therefore, Ms. Gordon committed the "something extra" for 10b-5(a) and (c) purposes not only by ordering her subordinate to distribute the Memo to investors, but also by misleading Gemstar's experts as to the quality of Gemstar's products.

In summary, Ms. Gordon participated in "something beyond" mere misstatements to incur primary liability. It was Ms. Gordon who personally

misled Gemstar's experts in the creation of the Report that would be included in the Memo. Further, she disseminated "the Memo" to Gemstar's investors when she ordered one of her subordinates to send the document on her behalf. Therefore, we agree with the District Court and the Court of Appeals that Ms. Gordon is a "primary violator" of Rule 10-b5(a) and (c), and it is Ms. Gordon who should be found personally liable for the damages that were done to "the Fund" as a result of her actions. Ms. Gordon's 12(b)(6) motion to dismiss should be denied.

II. PROPER APPLICATION OF AFFILIATED UTE ENTITLES THE FUND TO A REBUTTABLE PRESUMPTION OF RELIANCE.

To prevail in this private action under §10b-5(a), (c) of the Securities Act of 1934, the plaintiff must show: "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation." (). In front of the court today is element number four. In Affiliated Ute, the Supreme Court held that a rebuttable presumption of reliance applies to omissions of material information where a duty to disclose exists. The court does this because in some cases, requiring affirmative proof of reliance would impose an unreasonable evidentiary burden on private plaintiffs and further require the private plaintiff to prove counter-factuals of evidentiary negatives.

In *Affiliated Ute Citizens v. United States* the Supreme Court case that established a rebuttable presumption of reliance for omissions in securities

fraud cases under Rule 10b-5. *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972). The case involved a tribe that sold its shares in a company to individual buyers without disclosing the material fact that the shares were worth significantly more than what the tribe was selling them for. *Id.* The Court held that in cases where the defendant had a duty to disclose material information and failed to do so, the plaintiff need not prove actual reliance on the omission. *Id.* Instead, the plaintiff can rely on a rebuttable presumption of reliance, meaning that the defendant has the burden of proving that the plaintiff did not rely on the omission. *Id.* The case also established the principle that silence can be a form of misrepresentation and that omissions can be just as deceptive as affirmative misrepresentations. *Id.* The Affiliated Ute presumption of reliance has been reaffirmed and applied in subsequent Supreme Court cases. In Basic Inc. v. Levinson, the Supreme Court established the "fraud on the market" theory, which presumes that investors in an efficient market rely on the integrity of market prices, and that any material misstatements will affect the market price. *Basic Inc. v. Levinson*, 485 U.S. 224 (1988) This case established the rebuttable presumption of reliance in securities fraud cases beyond omissions and allowed plaintiffs to prove reliance through circumstantial evidence. In Halliburton Co. v. Erica P. John Fund, Inc., the Supreme Court clarified the "fraud on the market" theory and reaffirmed the rebuttable presumption of reliance in securities fraud cases. *Halliburton Co. v. Erica P. John Fund, Inc.*, 573 U.S. 258 (2014).

The Court held that the rebuttable presumption of reliance applies in cases where a misstatement has affected the market price but may be rebutted by a defendant showing that the alleged misstatement did not actually influence the market price. *Id.* Based on this theory, a plaintiff must make the following showings to demonstrate that the presumption of reliance applies in a given case: (1) that the alleged misrepresentations were publicly known, (2) that they were material, (3) that the stock traded in an efficient market, and (4) that the plaintiff traded the stock between the time the misrepresentations were made and when the truth was revealed. *Id.* at 2408. The fraud-on-the-market theory holds that in an efficient market, the price of a security reflects all publicly available information, and investors rely on that information when they make their investment decisions. Thus, if a company makes a material misstatement or omission that affects the stock price, investors who purchased the stock during that time period are presumed to have relied on the misstatement or omission. The fraud-on-the-market theory has traditionally been applied to cases involving publicly traded securities, where the stock price reflects the available public information. *In re Nine Systems Corp. Shareholders Litigation*, 801 A.2d 1208 (Del. Ch. 2002). However, in recent years, some courts have extended the theory to cases involving private stock sales that are not traded on the public market. *In re Petrobras Securities Litigation*, 862 F.3d 250 (2d Cir. 2017). In these cases, the plaintiffs must show that (1) the private market is efficient and (2) that the defendant made a misstatement or omission that affected the stock price in the private market. *Dura Pharmaceuticals, Inc. v.*

Broudo, 544 U.S. 336 (2005) If the plaintiffs can establish these elements, the fraud-on-the-market theory can be applied, and a rebuttable presumption of reliance can be established. Whether the misstatement or omissions affected the stock price is not of issue in this court today.

The issue of whether a private market is efficient for the purposes of the fraud-on-the-market theory is a matter of fact that must be determined by the court based on the evidence presented in the case. While there is no one-size-fits-all test for demonstrating market efficiency, the Supreme Court has provided guidance on the factors that courts may consider in making this determination. One key factor is whether there is a large number of buyers and sellers in the market, which makes it more likely that the market price reflects all available information. Another factor is whether the market is transparent and information is readily available to investors. In *Matrixx Initiatives, Inc. v. Siracusano*, the Supreme Court held that an allegedly false statement need not be disclosed to the public for the fraud-on-the-market theory to apply, so long as the information was available to a significant group of investors. *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27 (2011). The Supreme Court has also noted that courts may consider other factors, such as the nature of the securities, the trading volume, and the sophistication of the investors in the market. *Id.* Ultimately, this court must make a fact-specific determination based on the evidence presented in the record.

Although admittedly, the record is sparse with facts relating to the market, there are several facts provided that would allow this court to make a finding

that the market is sufficiently efficient enough to satisfy the requirement for a rebuttable presumption. The information about Gemstar that was put into the Memo by Ms. Gordon was distributed to the 26 largest non-banking financial institutions within the United States. This is a substantial amount of investors with the ability to trade millions of dollars in shares quickly. What is most important though, is that the Supreme Court has said that courts have the ability to consider the sophistication of investors in the market to determine whether the market is efficient. By the defendants own admission, the market consisted of specifically the 26 largest and most sophisticated non-banking institutions in the country. While in *Desai v. Deutsche Bank Securities Ltd.*, the court fails to allow the extension of the fraud-on-the-market theory, it does show that courts may extend the theory an that open access by all 26 of the nations largest non-banking financial institutions would be a significantly stronger indicator of an efficient market than has been alleged in private markets in the past. *Desai v. Deutsche Bank Sec. Ltd.*, 573 F.3d 931, 941 (9th Cir. 2009).

A. The Omissions and Misstatements Omitted and Stated by Ms. Gordon were Material

In *Matrixx Initiatives, Inc. v. Siracusano,* the Court addressed the issue of whether a company can be liable for omitting information about adverse events that have not yet been statistically significant. The Court held that companies have a duty to disclose any material information that would be important to a reasonable investor. *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27 (2011).

The Supreme Court further addressed the issue of whether a plaintiff can establish the materiality of an omission by showing that the information was important to a reasonable investor. *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083 (1991). In City of Westland Police & Fire Ret. Sys. v. MetLife, Inc., the Second Circuit held that information about a subsidiary's alleged misconduct was material because a reasonable investor would have considered the potential liability significant in deciding whether to invest. *City of Westland Police & Fire Ret. Sys. v. MetLife, Inc.*, 866 F.3d 1114 (2d Cir. 2017). In *SEC v. Texas Gulf Sulphur Co.*, the Second Circuit held that information about a significant mineral discovery was material, even if the discovery had not yet been confirmed, because the information would be important to a reasonable investor in making an investment decision. *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833 (2d Cir. 1968).

Ms. Gordon may argue that this event was highly unlikely and was determined not to be material when the Owners did their initial due diligence on the company. However, just because the mistake was made in the past determining that this information was not material, does not mean that that finding is true going forward. In Virginia Bankshares, Inc. v. Sandberg, the Court held that materiality depends not only on the probability that the event will occur, but also on the magnitude of the event in relation to the total enterprise. Virginia Bankshares, Inc. v. Sandberg, 501 U.S. 1083 (1991). SwiftMax was the companies largest selling product, and thus a fact that could potential harm that product line is of great magnitude in relation to the total

enterprise. In *SEC v. Texas Gulf Sulphur Co.*, the potential discovery of an additional mining opportunity was considered material. *SEC v. Texas Gulf Sulphur Co.,* at 848-849. If potential additional productive efforts are considered material, the safety and efficacy of the top selling product of a company is most definitely material.

B. Ms. Gordan Had a Duty to Disclose the Information Omitted, as well as a Duty to Correct the Inaccurate Statements Once Made.

The Supreme Court established a set of guidelines in *SEC v. Ralston Purina Co.* to help determine if a duty to disclose exists in a securities fraud case. *SEC v. Ralston Purina Co.*, 346 U.S. 119 (1953). The court outlined five key factors. Firstly, if the defendant is an insider, like an officer or director of a company, they may be obligated to reveal significant information to investors. Secondly, the information in question must be material, meaning it would be important to a reasonable investor in making a decision. Thirdly, the defendant's relationship to the securities transaction, such as being a seller or underwriter, may impact the duty to disclose. Fourthly, if the information is easily accessible, the defendant may be required to reveal it even if they did not possess exclusive knowledge of it. Lastly, if the defendant made false or misleading representations to the plaintiff, they may be obligated to disclose information, regardless of whether they were otherwise obliged to do so.

In *Mullins v. TestAmerica, Inc.*, The Fifth Circuit held that a vice president of a corporation who was responsible for managing a contract with a government agency had apparent authority to make representations to the agency about

the corporation's compliance with the contract, even though he did not have actual authority to do so. *Mullins v. TestAmerica, Inc.,* 564 F.3d 386 (5th Cir. 2009).

Ms. Gordon is a corporate insider with the title of Vice President of Investor relations. Further, she was charged with organizing the documents designed to illicit investment and disseminate them. In the same vain as *Mullins v. TestAmerica Inc.,* she had apparent authority to make representations about the company. In *Mullins v. TestAmerica,* this apparent authority was found when the employee was not actually given the authority to perform these tasks. In this case, Ms. Gordon was specifically an obviously given this authority, thus under factor one, it is clear that Ms. Gordon is an insider, like an officer or director of a company, they may be obligated to reveal significant information to investors. Materiality has been discussed and dispatched with above. For the third factor, Ms. Gordon was in charge of facilitating and attracting investors to the project which would suggest she absolutely had a duty to disclose known material information. Regarding the fourth factor, the disclosure was easily done, and the information was easily accessible in the report that Ms. Gordon possessed. Finally, Ms. Gordon made, disseminated material misstatements and omissions, meaning that even absent all the other factors, a court could still find that she had a duty to correct those omissions and misstatements.

Conclusion

For the foregoing reasons, Petitioners respectfully requests this Court to reverse the Court of Appeals' decision to grant Ms. Gordon's 12(b)(6) motion, as Ms. Gordon is primarily liable as a "disseminator" under Rule 10b-5(a) and (c), and the Fund is entitled to a rebuttable presumption of reliance under *Affiliated Ute*.