Team No. R15

Docket No. 22-123

In The
Supreme Court of the United States

FORDHAM PUBLIC EMPLOYEES INVESTMENT FUND

Petitioner,

v.

KATIE GORDON,

Respondent.

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

Brief for Respondent

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QUESTIONS PRESENTED:

1. Is an individual subject to primary liability as a "disseminator" under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5(a) and (c), for instructing an employee to distribute a memorandum that contained allegedly false or misleading statements, even though that individual did not make or personally disseminate the memorandum?

2. Whether the *Affiliated Ute* presumption of reliance applies in "mixed cases," where the plaintiff alleges both affirmative misstatements and omissions?

TABLE OF AUTHORITIES

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STATEMENT OF THE CASE

I. Statement of Facts

Gemstar. The events leading to this case began in 2014 when Grace Underwood and Danielle Scott ("Partners") met in NYC. R. at 1. They decided to combine their wealth and pursue a buyout. R. at 2. In 2017, the Partners learned of McGrath, Inc., a manufacturing firm. R. at 2. They hired Forsyth Financial ("Forsyth") to examine the market and operations of McGrath and MMD Inc., an engineering firm, to examine the property, plant, and equipment. R. at 3. Both Forsyth's and MMD's reports were largely positive, but MMD's investigation noted certain trade literature that suggested the composite of McGrath's best selling machine may lead to "the development of microscopic cracks over time and under stress" R. at 3. This was the Partners' first notice of an issue. Ultimately, MMD's finding was overlooked and the Partners finalized the purchase of McGrath in 2018. R. at 3. The new entity was named Gemstar. R. at 3. Gemstar became very successful, its most popular product, SwiftMax, a machine tool used to produce fastener for various applications. R. at 4.

Private Placement Plan. Despite Gemstar's success, the Partners decided to pursue other career opportunities and sought an exit plan. R. at 4. They hired Allison Ritter, a Junior Managing Director at Carter Capital, to help them structure a liquidity event and advise on the transaction. R. at 4. After analyzing Gemstar's finances, Ritter introduced an exit plan in which the Partners could sell "80 [percent] of Gemstar in a private placement to institutional investors while retaining 20 [percent] in the form of super voting shares." R. at 4. Although initially reluctant, the Partners agreed to the plan and began the private placement transaction in February 2021. R. at 4.

The Partners tasked Katie Gordon ("Katie"), Gemstar's Vice President of Investor Relations, with organizing the transaction. Katie's primary role was to manage the flow of information to Carter Capital, the company advising the Partners on the transaction. R. at 5. One crucial piece of information was the Private Placement Memorandum ("the Memo"), which was used for marketing Gemstar's common stock. R. at 5. The Memo was created by Gemstar attorneys, financial advisors, auditors, engineering firms, and other experts. R. at 5. Katie coordinated the effort. R. at 5.

In May 2021, the principal engineering firm advising on the transaction delivered its report ("the Report") of Gemstar's assets and products to Katie. R. at 5. The Report was largely unproblematic, referencing no material deficiencies, except for a memorandum ("Trade Letter") suggesting that the SwiftMax used a composite which could develop microscopic cracks over time under extreme stress. R. at 5–6. Katie reviewed the Report, including the Trade Letter, and decided not to act until she discussed the Trade Letter with the Partners. R. at 6. Ultimately, Underwood convinced Scott that the Trade Letter, being three years old, was obsolete. R. at 6. Thus, at the direction of the Partners, Katie removed the Trade Letter from the file and delivered the finalized Report to Gemstar's team of experts. R. at 6.

The finalized Memo stated that Gemstar's property, plant, and equipment were in "reasonable condition for their intended use," that "there were no material defects in the products sold to customers," and that "there were no material undisclosed contingent liabilities relating to its products." R. at 6. The Memo did not mention the possibility that the SwiftMax could potentially produce defective composite. R. at 6. Katie's associate distributed the Memo, sending it to twenty-six large, non-bank financial institutions. R. at 6. The Memo was printed on Gemstar stationery but did not identify Katie as the VP of Investor Relations, nor did it invite potential investors to request information about the Memo's contents. R. at 6. For her part, Katie herself engaged in no communication with the investors once the Memo was distributed.

The Fund. Several institutional investors purchased Gemstar shares, including the Fordham Public Employees Investment Fund ("the Fund"), which purchased three million shares at twenty-seven dollars each. R. at 7.

The incident leading to this suit occurred in December 2021 when a Seaboard Airlines cargo jet engine exploded after acceleration of the plane for takeoff. R. at 7. An FAA investigation revealed that the fasteners in the aircraft's left wing were too weak to support the engine, leading to its partial dislodging. R. at 7. The FAA found that, over time, the pressure generated by takeoffs caused microscopic fissures to develop in the fasteners. R. at 7. Silberfarb Solutions, one of Gemstar's biggest clients, manufactured the fastners using Gemstar's SwiftMax. R. at 7. In February 2022, the Fund sold its shares for four dollars each, resulting in a 68-million-dollar loss. R. at 7.

II. Procedural History

District Court. In March 2022, the Fund filed suit in the United States District Court for the District of Fordham against Gemstar, the Partners, and Katie. R. at 8. The fund alleged that defendants engaged in a deceptive scheme to conceal material contingent liabilities, violating Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5. R. at 8. Katie filed a Rule 12(b)(6) motion to dismiss, which the District Court denied in October 2022. R. at 8–9. The court found that Katie was subject to primary liability as a "disseminator" of the allegedly false and misleading statements. R. at 9. Additionally, the Court held that because the Fund primarily alleged omissions it was entitled to a presumption of reliance under *Affiliated Ute*. R. at 9.

Court of Appeals. On appeal, the Circuit Court of Fordham affirmed in part and reversed in part, ultimately granting Katie's motion to dismiss. R. at 23. The Court of Appeals agreed with the lower court that Katie can be held primarily liable as a "disseminator." R. at 23. However, in line with the position of several other circuits, the Court of Appeals found that the Fund alleged primarily affirmative misrepresentations and was therefore not entitled to a rebuttable presumption of reliance. R. at 23.

SUMMARY OF THE ARGUMENT

This Court should find that Katie Gordon cannot be subject to primary liability as a "disseminator" under Rule 10b-5(a) and (c), for instructing an employee to distribute the Memo to prospective investors. Holding Katie primarily liable, and thus subject to the Petitioner's private cause of action, would require the Court to expand the scope of *Lorenzo* because Katie did not "directly transmit" false or misleading statements herself, nor did she invite investors to inquire about or identify herself in the Memo. The Circuit Court erred in its decision because it failed to (1) squarely apply the facts of this case within the holding of *Lorenzo* and (2) follow Justice Breyer's framework in *Lorenzo* for determining when it's appropriate to narrow the reach of primary liability under Rule 10b-5. Following that framework, this Court should determine that primary liability is inappropriate in this case.

Additionally, the Court should find that the Fund is not entitled to a rebuttable presumption of reliance under *Affiliated Ute*. To hold otherwise would void the element of reliance by allowing plaintiffs to claim entitlement to a rebuttable presumption in cases involving omissions *and* affirmative misstatements. The lower court erred in applying *Affiliated Ute* because 1) the Fund alleged primarily affirmative misstatements, and 2) as VP of Investor Relations, Katie had no duty to disclose the information in the Trade Letter. In order to maintain the importance of the reliance element in Section 10(b) actions, this Court should follow the approach of most circuit courts and apply the *Affiliated Ute* presumption only in omissions cases where proving reliance would be impossible. That is not this case.

ARGUMENT

I. KATIE IS NOT A "DISSEMINATOR" UNDER *LORENZO*, BUT SHE IS A "BORDERLINE CASE" WHERE THE REACH OF PRIMARY LIABILITY UNDER RULE 10b-5(a) AND (c) SHOULD BE NARROWED BY PURPOSE, PRECEDENT, AND CIRCUMSTANCE.

Congress did not expressly provide a private cause of action for violations of § 10(b) of the Securities Exchange Act of 1934. Rather, this Court recognized an implied cause of action under § 10(b) and SEC Rule 10b-5 in some circumstances. *Superintendent of Insurance v. Bankers Life & Cas. Co.*, 404 U.S. 6, 13 n. 9 (1971). Due to the nature of this judicial creation, this Court has acknowledged that "narrow dimensions [must be given] to a right of action Congress did not authorize when it first enacted the statute and did not expand when it revisited the law." *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta*, 552 U.S. 148, 167 (2008). Thus, this private cause of action should not be implied where it is "unnecessary to ensure the fulfillment of Congress' purposes." *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1, 41 (1977).

To ensure that this judicially created private cause of action fulfills the intent of Congress, this Court established a line between "primary liability" and "secondary liability" in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver*, N.A., 511 U.S. 164, 177 (1994). Private plaintiffs can reach "primary violators," *id.* at 141, but cannot bring suit against "secondary violators" for aiding and abetting, which can only be prosecuted by the SEC. 15 U.S.C. § 78t(e). This court last touched on the line between primary and secondary liability under Rule 10b-5 in two seminal cases. In *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135, 144 (2011), this Court held that only the "*maker*" of a false or misleading statement under Rule 10b-5(b) is subject to primary liability. Then, in *Lorenzo v. Securities & Exchange Commission*, 139 S. Ct. 1094, 1096 (2019), this Court expanded the scope of primary liability under Rules 10b–5(a) and (c) to "[t]hose who disseminate false statements with intent to defraud." In this case, the Court must decide whether to extend *Lorenzo* to capture Katie's conduct, or to narrow its holding and reign in the private right of action under Rule 10b-5, which has gone far beyond Congressional intent.

A. Katie does not fall in either of *Lorenzo*'s two disseminator categories, so she is not a disseminator unless this Court expands its holding.

There are two explicit categories of disseminators under *Lorenzo*. First, an individual is a "direct" disseminator by engaging in the same conduct as Lorenzo. Second, and more determinant here, the majority opinion implies that "other actors tangentially involved in dissemination" may *sometimes* be held primarily liable as a disseminator. *Lorenzo*, 139 S. Ct. at 1101. In this case, the Fund seeks to hold Gordon primarily liable under *Lorenzo* even though her conduct does not conform with the first category of a disseminator and *Lorenzo* left the second category undefined. This Court would thus have to expand the scope of *Lorenzo* under the second category to capture Katie's conduct.

i. <u>Unlike Lorenzo, Katie Gordon is not a "direct" disseminator.</u>

Katie's conduct does not fit within the defined scope of *Lorenzo*'s first category, and she is thus not a "direct" disseminator. In that case, this Court found Lorenzo primarily liable as a disseminator because he "sent false statements directly to investors, invited them to follow up with questions, and did so in his capacity as vice president of an investment banking company." *Lorenzo*, 139 S. Ct. at 1101. Unlike Lorenzo, Katie is not a "disseminator" under this Court's decision because she did not engage in the same conduct.

Lorenzo expressly holds that "*direct transmission* of false statements to prospective investors***" will subject an individual to primary liability as a disseminator. *Id.* at 1104 (emphasis added). The relevant definitions of "direct" are (1) "proceeding from one point to another in time or space without deviation or interruption," (2) "stemming immediately from a source," and (3) "marked by an absence of an intervening agency, instrumentality, or influence." *Direct*, The Merriam-Webster's Dictionary (2019 ed.). Applying these definitions, Katie's conduct did not involve "direct dissemination." The transmission did not proceed from one point to another without deviation or interruption; Katie sent the Memo to her employee, who then sent it to the prospective investors. R. at 6. Likewise, the transmission did not stem immediately from Katie. Finally, the transmission was not "marked by an absence of an intervening agency [or] instrumentality" as the employee is an intervening agent between Katie and the prospective investors. Under any relevant definition, Katie did not directly transmit the Memo to investors and thus did not engage in the same kind of conduct that subjected Lorenzo to primary liability as a "direct" disseminator.

Furthermore, Katie did not engage in the other factors that the majority opinion found dispositive in *Lorenzo*. These include (1) inviting prospective investors to inquire with follow-up questions, and (2) identifying oneself in the contents of the disseminated message. *Id.* at 1101. Unlike Lorenzo, Katie did not send the Memo herself, invite investors to inquire about the contents of the Memo, nor did the Memo identify Katie at all—in her role as Vice President of Investor Relations or otherwise. R. at 6. Applying these factors, Katie cannot be held primarily liable as a "direct" disseminator.

Accordingly, Katie is not subject to primary liability under *Lorenzo*'s first disseminator category. On that basis alone, this Court should overturn the Circuit Court's finding that Katie can be held primarily liable as a disseminator under Rules 10b-5(a) and (c). Still, there arguably lies an ambiguity in *Lorenzo*'s majority opinion that can be vaguely construed to extend primary liability to Katie under the second category of *Lorenzo*.

ii. <u>Whether Katie is primarily liable as a tangential disseminator is indeterminable because *Lorenzo* left that term undefined.</u>

The second category of disseminator is much more ambiguous. This category stems from an acknowledgment in *Lorenzo*'s key paragraph that "one can readily imagine *other actors tangentially involved in dissemination—say, a mailroom clerk—for whom liability would typically be inappropriate****." *Lorenzo*, 139 S. Ct. at 1101 (emphasis added). The deliberate inclusion of the word "typically" implies that the actor tangentially involved in dissemination ("tangential disseminator") will *sometimes* be held primarily liable. And while Justice Breyer did not further define this classification or explain when the tangential disseminator will be primarily liable, the inclusion of an example, "a mailroom clerk" is telling because it sets the boundaries of primary liability. Ultimately, this Court should apply the framework in *Lorenzo*'s key paragraph to narrow the tangential disseminator rule and render it inapplicable to Katie.

B. Applying Justice Breyer's key paragraph, this is a "borderline" case because Katie Gordon is situated between Lorenzo and a mail clerk on the *Lorenzo* spectrum of primary liability.

The key paragraph of this Court's opinion in *Lorenzo* recognizes that primary liability as a disseminator is not appropriate in every case:

> [Rule 10b-5's antifraud] provisions capture a wide range of conduct. *Applying them may present difficult problems of scope in borderline cases. Purpose, precedent, and circumstance could lead to narrowing their reach in other contexts.* But we see nothing borderline about this case, where the relevant conduct*** consists of disseminating false or misleading information to prospective investors with the intent to defraud. *And while one can readily imagine other actors tangentially involved in dissemination—say, a mailroom clerk—for whom liability would typically be inappropriate*, the petitioner in this case sent false statements directly to investors, invited them to follow up with questions, and did so in his capacity as vice president of an investment banking company.

Lorenzo, 139 S. Ct. at 1101 (emphasis added). Justice Breyer cites a mailroom clerk as an example of someone who should obviously be excluded from the reach of private causes of action, but he also states more broadly that primary liability may be appropriately narrowed in "borderline cases." *Id.* If the case is "borderline," Justice Breyer instructs the Court to apply "[p]urpose, precedent, and circumstance [of Rule 10b-5's antifraud provisions and the facts at hand]" to determine whether primary liability is appropriate. *Id.*

Accordingly, determining whether a case is "borderline" is the first step that must be taken to determine whether someone is subject to primary liability. While Justice Breyer did not define "borderline," his meaning can be established through a simple dictionary definition. The definition of "borderline" is "being in an intermediate position or state: *not fully classifiable as one thing or its opposite.*" *Borderline*, <u>The Merriam-Webster's Dictionary</u>

(2019 ed.) (emphasis added). Thus, a "borderline" case is between two things but is not definitvely classifiable as one thing or the other.

Justice Breyer's majority opinion established a linear spectrum of primary liability as a disseminator. Lorenzo, a direct disseminator that is always subject to primary liability, is at one end of the spectrum. A mail clerk is at the other end as a tangential disseminator not subject to primary liability. As explained above, Katie is not a direct disseminator. Nor is Katie a mail clerk; her position and duties as Gemstar's Vice President of Investor Relations logically make her more involved in the conduct at issue here than a mail clerk. However, Katie is not unequivocally a tangential disseminator subject to primary liability because, as stated above, *Lorenzo* left this category undefined. Katie falls somewhere in the middle between Lorenzo and a mail clerk and is thus necessarily "borderline."

Because Katie is a "borderline case," this Court must apply "[p]urpose, precedent, and circumstance" to determine whether primary liability should extend to Katie as an actor "tangentially involved in dissemination." *Lorenzo*, 139 S. Ct. at 1101. Because extending this rule would contravene Congressional intent and contradict this Court's precedent, this Court should confine application of the tangential disseminator rule.

C. Purpose, precedent, and circumstance warrant narrowing the scope of primary liability under Lorenzo.

This Court should not extend primary liability to Katie as a tangential disseminator. Doing so would contravene Congressional intent by muddling the distinction between primary and secondary liability and is redundant given the role of the SEC in prosecuting secondary violators of securities fraud. Further, this Court's precedent has held that the conduct at issue in this case is insufficient to establish primary liability. Finally, Katie should not be held primarily liable given the innocuous circumstances in this case. For these reasons, this Court should narrow the tangential disseminator rule and determine that Katie is not subject to primary liability.

i. Extending primary liability to Katie does not square with the legislative purpose of enacting § 10(b) of the Securities Exchange Act of 1934.

This Court should not extend primary liability as a tangential disseminator to Katie. Expanding the judicially created private cause of action under Rule 10b-5 would contravene the legislative purpose of enacting § 10(b) of the Exchange Act. A Senate Committee report discussing the Senate's version of the Exchange Act reveals what the contemporaries had in mind: the provision was "intended to confer extensive power on administrators" because "speculation was a terrible problem, and flexible regulation by an agency with broad discretion was the answer." S. Rep. No. 792, 73d Cong., 2d Sess. 6 (1934); see also Steve Thel, *The Original Conception of Section 10(b) of the Securities Exchange Act*, 42 Stan. L. Rev. 385, 454 (1990).[1] Indeed, there is substantial evidence that Congress intended to penalize potential violations of § 10(b) through administrative action by the SEC, and not private causes of action.

[1] Available at: https://ir.lawnet.fordham.edu/faculty_scholarship/831

a. Where Congress intended to create private civil actions, it did so expressly throughout the 1933 and 1934 Acts, but not in § 10(b).

Congress used express language throughout the Securities Act of 1933 and the Exchange Act when it intended to create private causes of action. For example, § 11(a) of the 1933 Act expressly permits "any person acquiring such security… [to] sue [for material misstatements or omissions in registration statements]." 15 U.S.C. § 77K(a). Likewise, § 9(f) of the Exchange Act expressly permits private causes of action for "any person who shall purchase or sell any security [affected by stock price manipulation under § 9(a), (b), and (c)]." 15 U.S.C. § 78i(f). Express language in the Exchange Act is also used to create private civil actions in §§ 16(b), 18(a), 20(a), 20A, and 29(b).

However, Congress did not use express language to establish private civil actions in § 10(b) of the Exchange Act. Rather, Congress made it unlawful to use "any manipulative or deceptive device… in contravention of [the Commission's] rules and regulations." 15 U.S.C. § 78j(b). The Acts show that Congress intended to create private civil actions in certain sections but declined to supply this right in § 10(b). This does not mean that Congress meant for § 10(b) to be toothless; Congress instead empowered the SEC to enforce and regulate violations of § 10(b).

b. Congress tasked the SEC with prosecuting aiding and abetting securities law violations, which Katie could already be subject to.

After *Central Bank* foreclosed private civil actions against aiders and abettors under Rule 10b-5, Congress debated at length whether to expressly create a private cause of action for aiding and abetting when drafting the

Private Securities Litigation Reform Act of 1995 (“PSLRA”). S. Rep. No. 104-98, 104th Cong., 1st Sess. 1, 64 (1995). However, in enacting the PSLRA Congress ultimately decided that “to provide explicitly for private aiding and abetting liability actions under Section 10(b) would be contrary to the [PSLRA]’s goal of reducing meritless securities ligation.” *Id.* at 65. Instead, by revising the Exchange Act through the PSLRA, Congress tasked the SEC with prosecuting persons who provide “substantial assistance to another person in violation of a provision of [the Exchange Act].” Private Securities Litigation Reform Act, Pub. L. No. 104-67, 109 Stat. 737 (1995).

By enacting the PSLRA, Congress drew a line to distinguish primary and secondary liability. See *Alexander v. Sandoval,* 532 U.S. 275, 290 (2001) (“The express provision of one method of enforcing a substantive rule suggests that Congress intended to preclude others”). Congress provided statutory guidance for making that distinction by defining an aider and abettor as someone who provides “substantial assistance” to a violation of securities law. If substantial assistance is required for aiding and abetting, *primary liability must require more*; otherwise, there would be no difference between a primary violator and someone who aids and abets. If that were the case, someone who provides substantial assistance to another would be liable both as a primary violator and an aider and abettor for violating Rule 10b-5, and Congress’ command to distinguish primary and secondary liability would serve no purpose.

As explained below, Katie’s conduct cannot amount to more than substantial assistance of the underlying fraud, so she cannot be subject to primary liability. However, Katie could be subject to secondary liability. Because the SEC could seek to prosecute Katie for aiding and abetting, Congress' intent has been fulfilled and expanding the holding of *Lorenzo* serves no real aim besides emboldening plaintiffs' attorneys to file vexatious lawsuits.

c. Congress empowered the SEC to bring claims for disgorgement under § 10(b), which reach aiders and abettors so that victims of securities law violations are not left without recourse.

The disgorgement provisions of the Exchange Act express Congress' intent to have the SEC enforce violations of § 10(b), which renders expanding the holding of *Lorenzo* unnecessary. §§ 21(a)(7) and (8) of the Exchange Act allow the SEC to "bring a claim for disgorgement under [§ 21(a)(7)]… (ii) not later than 10 years after the latest date of the violation… if the violation involves conduct that violates (I) section 10(b)." 15 U.S.C. § 78u(a)(8). Claims for disgorgement extend to aiders and abettors. *Securities and Exchange Commission v. Gemstar-TV Guide International, Inc.*, Case No. CV 04-04-4506 RGK (CTx) (C.D. Cal. 2004) (ordering $150,000 in disgorgement for aiding and abetting against a company's attorney). The disgorgement provisions ensure victims of securities fraud are not left without recourse, so expanding primary liability under *Lorenzo* would not serve a legitimate Congressional purpose.

This Court has previously recognized that "when Congress wished to provide a private damage remedy [in securities law], it knew how to do so and did so expressly." *Touche Ross & Co. v. Redington*, 442 U.S. 560, 572 (1979). It follows, then, that when Congress did not provide a private damage remedy it never intended to permit such a remedy in the first place. Holding Katie primarily liable as a disseminator would stretch the judicially created private cause of action beyond reasonable limits even though Congress never intended such a private right in the first place. As the legislative history and the text of the Acts make clear, Congress tasked the SEC with regulating and prosecuting violations of § 10(b). This Court should not continue to interfere with a deliberate Congressional choice by extending *Lorenzo*.

ii. This Court's precedent has already foreclosed primary liability for the same conduct at issue in this case.

Recognizing the need to distinguish primary and secondary liability, this Court should rely on deeply rooted precedent to establish when tangential disseminators are subject to primary liability. This Court's precedent has long articulated principles that define the main ingredients for primary liability. In *Stoneridge*, this Court held that "reliance by the plaintiff upon the defendant's deceptive acts is an essential element of the §10(b) private cause of action" and that "deceptive acts…not disclosed to [investors]…are too remote" to be relied on for primary liability. *Stoneridge*, 552 U.S. at 159, 161. The Second Circuit elaborated that "absent attribution," identifying that the misstatements came from the defendant, "plaintiffs cannot show that they relied on the defendant's own false statements" for scheme liability claims. *Pacific Inv. Mgmt. Co. LLC v. Mayer Brown LLP*, 603 F.3d 144, 148, 161 (2d Cir. 2010). Moreover, the defendant's role and conduct must have been "necessary or inevitable" in carrying out the fraud. *Stoneridge*, 552 U.S. at 162. In *Lorenzo*, the Court distinguished *Stoneridge* on the basis that Lorenzo engaged in "the direct transmission of false statements to prospective investors intended to induce reliance" and not "the concealed fraud at issue in *Stoneridge*" that would not subject someone to primary liability. *Lorenzo*, 138 S. Ct. at 1104.

This Court's precedent makes it clear that Katie cannot be subject to primary liability as a tangential disseminator. Katie's act of removing the Trade Letter from the Memo delivered to Gemstar's experts, at the behest of the Partners, was "not disclosed" to the Fund and is thus "too remote" to be relied upon. *Stoneridge*, 552 U.S. at 161. Furthermore, the Memo drafted by Katie cannot be attributed to her because it did not refer to Katie, and the Memo in its final form was altered from Katie's draft by someone who prepared a cover letter with Gemstar's letterhead, which also did not mention Katie. R. at 6. Katie's "participation in the creation of those statements amounts, at most, to aiding and abetting securities fraud." *Pacific Inv. Mgmt.*, 603 F.3d at 148. Primarily, it was Gemstar, through the ultimate authority of the Partners, who decided to create and disseminate the misstatements to the Fund.

The Fund's knowledge that Katie was involved in the private placement is not enough to attribute the misstatements to or establish the Fund's reliance on Katie. The mere knowledge that a person was involved is not this Court's standard for establishing reliance. The appropriate standard is to look at the defendant's "deceptive acts," determine if the acts were concealed or disclosed, and then decide if the plaintiffs were induced by the defendant's acts to their detriment. *Stoneridge*, 552 U.S. at 161; *Lorenzo*, 139 S. Ct. at 1104. Again, Katie took no affirmative action to put herself before the Fund to induce them to invest in Gemstar, nor was any of the memo's content attributable to her.

Moreover, her preparation of the Memo and role in ordering its distribution was not "necessary or inevitable" for Gemstar to engage in the underlying fraud, *Stoneridge*, 552 U.S. at 162, because Grace and Danielle could have removed the Trade Letter and included the misstatements themselves or given the command to distribute the Memo to another officer if Katie had refused.

Ultimately, this Court should draw a line between the conduct at issue in this case and *United States Securities & Exchange Commission v. Kameli*, No. 17 C 4686, 2020 WL 2542154 (N.D. Ill. May 19, 2020) to establish when tangential disseminators are subject to primary liability. The facts of *Kameli* are analogous to this case to the extent that the defendant, Kameli, was also a tangential disseminator who instructed his employees to distribute private placement memorandums, but he did not directly distribute them himself. *Kameli* at 15. However, the remaining facts are distinguishable from this case and demonstrate why, according to Court precedent, tangential disseminators like Kameli should be subject to primary liability, but Katie should not.

The Northern District of Illinois held that Kameli was subject to primary liability as a disseminator under Rules 10b-5(a) and (c) pursuant to *Lorenzo*. *Id.* at 15. Kameli was the head of an immigration law firm and owned and controlled two corporations. *Id.* at 1-2. Kameli personally planned fraudulent EB-5 Investment Visa projects that were the subjects of the private placement memorandums, which induced investors to participate in those projects. *Id.* at 2, 13, 15, 17. Although Kameli did not personally distribute the memos, the court found that the statements were still directly attributable to Kameli for the "purposes of primary liability" because of his "control over all aspects of the Funds' operations." *Id.* at 13-15. Because the statements were attributable to Kameli, he could not avoid primary liability by simply instructing an employee to disseminate the misstatements.

Unlike Kameli, Katie was not in charge of Gemstar, had no real authority over the Memo, and did not help plan the commission of the underlying fraud. Katie was dispensable in her role for the commission of the underlying fraud facilitated by the Partners. The Partners' actions closely parallel Kameli's deceptive acts because their roles were necessary for executing a plan to defraud investors. *Stoneridge*, 552 U.S. at 162. The Partners and Kameli are the appropriate parties to be held primarily liable for dissemination because the misstatements contained in both private placement memorandums were controlled by and attributed to them, not the employees who sent out the misinformation. *Janus*, 564 U.S. at 142–143 ("attribution within a statement or implicit from surrounding circumstances is strong evidence that a statement was made by … the party to whom it is attributed").

This Court's precedent clearly distinguishes Katie from the Partners and Kameli whose controlling acts were necessary to carry out their respective fraudulent acts. Katie's actions were too remote to sufficiently establish that the Fund was induced by her acts to invest in Gemstar. *Stoneridge*, 552 U.S. at 159, 161. Since the Memo's misstatements cannot be attributed to Katie, the Fund did not rely upon her in any capacity. Furthermore, Katie was not necessary for the attainment of the fraud. Thus, the Fund should not be able to bring a primary cause of action against Katie as a tangential disseminator.

iii. Katie's circumstances do not warrant subjecting her to primary liability.

Justice Breyer's overarching concern in *Lorenzo* is that there might be circumstances in which "those who disseminate false statements with the intent to cheat investors might escape liability" without proper safeguards. *Lorenzo*, 139 S. Ct. at 1103. Drawing on this concern, the Fund predictably argues that the scope of primary liability for disseminators should be expanded to prevent allowing someone to insulate themselves from primary liability by simply instructing a subordinate to disseminate false or misleading statements. However, broadening the scope of primary liability would contravene this Court's deep-rooted precedent by sweeping into the defendant class too many people who lack control, are not being relied upon by plaintiffs, and are not necessary for the execution of the fraud. Furthermore, such an expansion would contradict Justice Breyer's admission that the scope of primary liability should be narrowed in "borderline cases," such as this one. *Id.* at 1101.

To distinguish between tangential disseminators who should be primarily liable from those who should be secondarily liable, courts should look at the circumstances of each case to determine if the principles asserted by this Court's precedent, including reliance, necessity, control, and ultimate authority, are present to an extent that warrants subjecting someone to private causes of action. Applying the same principles that were required for primary liability in *Lorenzo* and prior precedent to the circumstances of each case will prevent culpable actors from escaping primary liability. Courts should ask the following questions to balance the totality of the circumstances to distinguish between primary and secondary liability in cases of tangential disseminators:

- How much input did the person have on the misleading content of the statement? *See Janus*, 564 U.S. at 144, 147.
- How much control did the person have over the decision to disseminate the misleading statement? *See Lorenzo*, 139 S. Ct. at 1101.
- Could dissemination of the misleading statements occur without the prospective defendant's acts? *See Stoneridge*, 552 U.S. at 162.
- Is the person identified in the misleading statement as the contact person for questions? *See Lorenzo,* 139 S. Ct. at 1101.

Applying these principles, Katie should not be found primarily liable based on her circumstances. First, Katie did not have any input on the decision to remove the Trade Letter from the Report that was delivered to Gemstar's experts. This might be different had Katie never brought the Trade Letter to the attention of the Partners because then Katie would have made the final choice to not include it in the Report. Rather, the Partners ultimately decided to exclude the Trade Letter from the Report, which Katie delivered at their instruction and which Gemstar's experts ultimately used to construct the Memo. R. at 5–6. Second, upon first blush, Katie might seem to have some authority over the decision to disseminate the Memo. However, such authority is illusionary because the authority was derived from the Partners tasking Katie with the private placement's marketing process, and the task of ordering the Memo to be distributed was merely part of her job as Vice President of Investor Relations. *Id.* Furthermore, Katie had no input in deciding to engage in a private placement transaction or to create the Memo in the first place. Third, as stated above, Katie was not necessary, and the dissemination could have taken place if she had refused to disseminate the Memo. The Partners could have simply given the command to distribute the Memo to another officer or done it themselves. Finally, Katie is not named as the contact person to inquire about questions regarding the Memo, nor does the Memo even invite prospective investors to inquire with anyone if they have further questions. Rather, the Memo is attributed to Gemstar and Katie is not mentioned in the Memo or the attached cover letter at all.

Based on these questions, Katie should not be held primarily liable as a tangential disseminator. The Court should adopt these questions as dispositive in determining whether there is primarily liablity as a tangential disseminator. First, they invoke well-established principles that this Court has long relied on. Second, they make the necessary distinction between primary and secondary liability. Finally, they separate the more culpable actors from those who had no meaningful role in the commission of the fraud and therefore address Justice Breyer's main concern that such actors will escape liability. For these reasons, Katie should not be subject to the Fund's private cause of action.

II. THE FUND IS NOT ENTITLED TO *Affiliated Ute*'s PRESUMPTION OF RELIANCE BECAUSE THE ALLEGED FRAUD CENTERS AROUND AFFIRMATIVE MISSTATEMENTS AND THUS RELIANCE IS NOT IMPOSSIBLE OR EVEN DIFFICULT TO PROVE.

In *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 153–154 (1972), this Court held that plaintiffs are entitled to a rebuttable presumption of reliance in cases involving a material omission by a person with a duty to disclose. This Court reasoned that proving reliance would be impossible in omissions cases. *Id.* This rebuttable presumption removes the "difficulty of proving a 'speculative negative'"—that the plaintiff relied on what was not said." *In re Volkswagen "Clean Diesel" Marketing, Sales Practices*, 2 F.4th 1199 (9th Cir. 2021), quoting *Binder v. Gillespie,* 184 F.3d 1059, 1064 (9th Cir. 1999). In the court below, the Petitioner turned Rule 10b-5's element of reliance on its head by invoking the *Affiliated Ute* presumption even though it alleged both omissions and affirmative misstatements.

The Fund's argument is nothing new. Plaintiffs have asserted this tactic in almost every federal jurisdiction, and courts have taken different approaches in applying the presumption in "mixed" cases where the plaintiff alleges both material omissions and affirmative misstatements. Still, circuits caution against interpreting *Affiliated Ute* in a way that would blur the distinction between omissions and affirmative misstatements. *Binder v. Gillespie*, 184 F.3d 1059, 1064 (9th Cir. 1999) (noting that most circuits have limited *Affiliated Ute* to cases that primarily allege omissions). This Court should decline Petitioner's efforts to extend the *Affiliated Ute* presumption in cases where, such as here, a plaintiff primarily alleges affirmative misstatements. In these instances, the rationale for the presumption is unnecessary: reliance is always possible to prove when affirmative misstatements are primarily alleged.

A. The Fund primarily alleges affirmative misstatements, so *Affiliated Ute* cannot apply.

The Fund alleges primarily affirmative misstatements, so it is not entitled to *Affiliated Ute*'s rebuttable presumption. Although *Affiliated Ute*'s application in mixed cases is varied, the presumption's purpose is clear: to ensure that plaintiffs can meet § 10(b)'s pleading standard in situations where "reliance is impossible or impractical to prove [because] no positive statements were made." *In re Volkswagen*, 2 F.4th at 1206. Multiple positive statements were made in this case. As such, *Affiliated Ute* cannot apply.

i. Petitioner alleges reliance on three affirmative misstatements; baldly stating that together the misstatements create a material omission does not invoke *Affiliated Ute*'s rebuttable presumption.

Determining whether a "mixed case" involves primarily misstatements or omissions is a fact-specific inquiry. *Joseph v. Wiles*, 223 F.3d 1155, 1162 (10th Cir. 2000), *abrogated by California Pub. Employees' Ret. Sys. v. ANZ Sec., Inc.*, 137 S. Ct. 2042 (2017). Because misstatements both assert false information and omit truthful information, defining the primary type of fraud can be difficult. *Id.* at 1162–63. The key, therefore, is to determine whether "reliance as a practical matter is impossible to prove." *Wilson v. Comtech Telecom. Corp.*, 648 F.2d 88, 93 (2d Cir.1981).

Several circuits have held that affirmative misstatements prove the possibility of reliance. In *In re Interbank Funding Corporation Securities Litigation*, 668 F. Supp. 2d 44, 51 (D.D.C. 2009), aff'd, 629 F.3d 213 (D.C. Cir. 2010), the D.C. Circuit Court held that reliance was not "impossible to prove" because the investment company's auditor "offer[ed] positive statements" in its private placement memoranda sent to potential investors. As such, *Affiliated Ute*'s presumption did not apply. *Id.* at 52. The Second Circuit's precedent accords. In *Waggoner v. Barclays PLC*, 875 F.3d 79, 96 (2nd Cir. 2017), the court held that the plaintiffs were not in a situation where it was impossible to prove reliance because their complaint alleged "numerous" affirmative misstatements. Additionally, the Ninth Circuit has held that where a plaintiff complains of numerous affirmative misstatements made by the defendant, the plaintiff "expressly alleges that it relied on the misstatements," so *Affiliated Ute*'s presumption does not apply. *In re Volkswagen*, 2 F.4th at 1206.

In alleging both positive statements and an omission, the Fund shows that reliance is possible to prove. Start with the Fund's complaint. It expressly points to three affirmative statements in the Memo on which it could have relied when it decided to purchase Gemstar stock: that "Gemstar's physical assets are in reasonable condition for their intended use" and "[n]one of Gemstar's products are materially defective." R. at 8. Like the situation in *In re Interbank Funding*, these allegedly affirmative misstatements are controlling. If the Fund believed the truth of these affirmative statements and relied on them in deciding to purchase stock, it would have proven so. But it could not, which is why the lower court correctly dismissed this case. Ultimately, whether Gemstar failed to include specifics about the potentially defective composite is of no matter in determining reliability. Moreover, *Affiliated Ute* cannot apply.

ii. <u>To find this case as primarily involving omissions will blur the distinction between affirmative misstatements and omissions and severely undercut § 10(b)'s reliance element.</u>

Applying *Affiliated Ute* in this instance will destroy any meaningful distinction between positive misstatements and omissions. Reliance is an essential element of the § 10(b) private cause of action because it establishes that a defendant's misrepresentation caused the plaintiff's injury. *Stoneridge*, 552 U.S. at 149 (quoting *Basic Inc. v. Levinson*, 485 U.S. 224, 243 (1988)). Thus, *Affiliated Ute*'s presumption of reliance is the exception, not the rule. *Affiliated Ute*, 406 U.S. at 154 ("*Under the circumstances of this case* . . . a failure to disclose, positive proof of reliance is not a prerequisite to recovery") (emphasis added). As such, many courts are weary of expanding *Affiliated Ute* and allowing the presumption "to swallow the reliance requirement." *Joseph*, 223 F.3d 1155 at 1163; see also *Binder*, 184 F.3d at 1064. Finding that the Fund, which alleged affirmative statements, is entitled to a presumption of reliance would do just that.

Such an overreach of *Affiliated Ute* is inconsistent with congressional intent. To be sure, Congress enacted the Exchange Act to curb securities fraud. *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 728 (1975). But Congress did not intend that every plausible fraud would lead to § 10(b) litigation. On the contrary, proving actual reliance is a key element of a § 10 (b) claim. *Stoneridge*, 552 U.S. at 149. If the Court applies *Affiliated Ute* here, where the Fund alleges primarily affirmative misstatements, plaintiffs will be incentivized to "intertwine affirmative acts with omissions" and "attempt to recharacterize the alleged wrongdoing" so they can avoid having to meet their evidentiary burden. *Joseph*, 223 F.3d at 1163. Not only will this subject courts to increased litigation, but it will needlessly increase defendants' burdens in defending statements on which plaintiffs did not rely. In sum, where actual reliance is evident, a presumption of reliance should not apply. To hold otherwise would contravene the Court's narrow holding in *Affiliated Ute* and Congress's intent in enacting § 10(b).

iii. Limiting Affiliated Ute to its proper scope does not create an "evidentiary hurdle" for plaintiffs.

Limiting *Affiliated Ute* to its proper scope will not prevent deserving plaintiffs from bringing § 10(b) claims. It is a basic tenant of law that plaintiffs have the burden of adequately pleading the elements of their claim. *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). Presumptions are not meant to displace traditional burdens of proof, but rather to assist the process of litigation in situations where direct proof is difficult to obtain. See *Basic, Inc. v. Levinson*, 485 U.S. 224, 245 (1988). As discussed, reliance is an element of § 10(b) actions to ensure that the defendant actually caused the plaintiff's injury. *Stoneridge*, 552 U.S. at 160. *Affiliated Ute*'s presumption is a narrow exception that allows plaintiffs, who were harmed by an action about which they had no knowledge, to meet their evidentiary burden. *Joseph*, 223 F.3d at 1162.

Precedent confirms that many § 10(b) plaintiffs can prove actual reliance, especially when they allege that affirmative misstatements were made. See, e.g., *In re Interbank Funding*, 668 F. Supp. 2d at 51; *Waggoner*, 875 F.3d at 96; *In re Volkswagen*, 2 F.4th at 1206. Specifically, here, where the Fund concedes reliance on affirmative misstatements in the Memo when purchasing Gemstar stock, a rebuttable presumption is unnecessary. No evidentiary hurdle arises because the Fund can, and does, point to the exact statements on which it allegedly relied to establish that Gemstar ostensibly caused it financial harm.

There is no reason that the longstanding policy of proving reliance should be lowered for plaintiffs who have access to direct evidence of actual reliance.

B. This is not primarily an omissions case because the alleged "omissions" are merely the "inverse" of affirmative misstatements.

The Fund cannot show how the alleged omissions, in this case, are anything more than "the inverse" of the alleged positive misstatements. To preserve a distinction between misstatements and omissions, several circuits have held that *Affiliated Ute*'s presumption does not "apply to misstatements whose only omission is the truth that the statement misrepresents." *Waggoner*, 875 F. 3d at 96; *In re Volkswagon*, 2 F.4th at 1208; *Joseph*, 223 F.3d at 1162. For example, where a plaintiff alleges that a defendant failed to disclose that it "materially disregarded its own underwriting standards," but the defendant affirmatively misstated that it "adhered to its underwriting standards," the alleged omission is simply the "flip side" of the affirmative misstatement. *Teamsters Loc. 445 Freight Div. Pension Fund v. Bombardier, Inc.*, No. 05 CIV. 1898 (SAS), 2006 WL 2161887, at *9 (S.D.N.Y. Aug. 1, 2006), aff'd, 546 F.3d 196 (2d Cir. 2008). Such positive statements, not omissions, are central to the alleged fraud, so the Fund cannot rely on *Affiliated Ute*'s presumption. *Id.*

The Fund alleges that the failure to disclose information about the defective composite was an omission. But this argument is simply the inverse of the Fund's allegation that the Memo included affirmative misstatement. The Memo stated that Gemstar's "physical assets [were] in reasonable condition," none of its products were "materially defective," and that there were "no material undisclosed contingent liabilities." R. at 8. Omitting information about the condition of assets that were potentially materially defective is nothing more than the inverse of the affirmative misstatements made.

This Court's holding in *Affiliated Ute* further demonstrates this point. There, plaintiff-investors alleged a scheme to defraud based on affirmative misstatements and omissions. *Affiliated Ute*, 406 U.S. at 146–48. Defendant-bankers told plaintiffs their shares were being sold at competitive market prices. *Id.* at 146. Secretly, defendants created a secondary market where they traded shares at higher prices for personal profit. *Id.* at 146–47. This Court reasoned that a rebuttable presumption of reliance applied because defendants made no positive statements to plaintiffs about the secondary market. *Id.* at 152–54. Defendants' statements to plaintiffs that their stocks were sold at competitive prices is not the inverse of a failure to disclose an entire secondary market. The affirmative statements and omission were distinct concepts. Not so here. As explained, stating that a thing is in a reasonable condition and failing to disclose evidence of an unreasonable condition are two sides of the same coin. This case is not about omissions, and the presumption cannot apply.

C. Katie did not owe the Fund a duty to disclose, so *Affiliated Ute* cannot apply.

Furthermore, even if this Court finds that "mixed" allegations are sufficient under the first element of the *Affiliated Ute*, Katie did not owe the Fund a duty to disclose the contents of the Trade Letter. A duty to disclose under Rule 10b-5 may only arise when "there is a corporate insider trad[ing] on confidential information, a statute or regulation requiring disclosure, or a corporate statement that would otherwise be inaccurate, incomplete, or misleading." *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94, 101 (2d Cir. 2015). First, the duty to disclose material information "because of a fiduciary or other similar relation[ship] of trust and confidence," *Chiarella v. United States*, 445 U.S. 222, 228 (1980), does not apply because this is not an insider trading case. Second, the duty to disclose information "truthfully and completely" once a company has chosen to speak applies only to companies and not their agents. *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 45 (2011); see also *Ong v. Chipotle Mexican Grill, Inc.,* 294 F. Supp. 3d 199, 229–30 (S.D.N.Y. 2018) (holding that Chipotle was under no duty to disclose any further information).

Finally, the only relevant statute or regulation requiring disclosure during private placements is the SEC's Regulation Fair Disclosure ("Regulation FD"), which relates to the disclosure of material nonpublic information by issuers. The SEC's final rule stated that "private liability will not result from a Regulation FD violation, we have revised Regulation FD to make absolutely clear that it does not establish a duty for purposes of Rule 10b-5." 17 C.F.R § 243.102 (2000); see also SEC Selective Disclosure and Insider Trading Final Rule, https://www.sec.gov/rules/final/33-7881.htm. In sum, Katie did not possess a duty to disclose. Therefore, *Affiliated Ute*'s second element cannot be satisfied, and the Fund cannot invoke the presumption.

CONCLUSION

For the foregoing reasons, this Court should affirm the Circuit Court of Fordham's grant of Katie's motion to dismiss, finding that Katie is not primarily liable as a disseminator and that the *Affiliated Ute* presumption does not apply.