Docket No. 22-123

In the Supreme Court of the United States

FORDHAM PUBLIC EMPLOYEES INVESTMENT FUND, PETITIONER,

v.

GORDON, KATIE, *et al.*, RESPONDENT

On Writ of Certiorari to the District Court for the District of Fordham

BRIEF FOR RESPONDENTS

TEAM 18

Counsel for Respondent

QUESTIONS PRESENTED

1. Whether an individual who neither "makes" nor distributes false or misleading statements can be subject to primary liability as a "disseminator" under Rule 10(b)-5(a) and (c); for instructing an employee to distribute the statements to investors; and

2. Whether the rebuttable presumption of reliance under *Affiliated Ute* applies where the plaintiff asserts "mixed" allegations involving both omissions and affirmative misrepresentation.

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STATUTORY AND REGULATORY PROVISIONS

This case first presents a question as to whether an individual who neither "makes" nor distributes false or misleading statements can be subject to primary liability under Rule 10(b) – 5(a) and (c). The second question concerns the rebuttable presumption of reliance under *Affiliated Ute*, which operates under Section 10(b) of the Securities Exchange Act of 1934.

INTRODUCTION

This case is a prime example of abusive litigation in the private securities fraud sphere. By implicating Gordon, private lawyers seek to open the floodgates to a variety of suits that this Court has reserved for the Securities Exchange Commission to address. At this critical juncture, this Court can choose to preserve the original anti-fraud intent of section 10(b) of the Securities Exchange Act of 1934 and Rule 10b – 5(a) and (c), or they can allow private suits to subject aiders and abettors to primary liability and drown businesses in asset-guzzling litigation.

STATEMENT OF THE CASE

Respondent, Katie Gordon (hereinafter "Gordon" or "Respondent") was the Vice President of Investor Relations at Gemstar, a successful machine tool manufacturer. R. at 2, 6. Despite Gemstar's success, company executives decided to sell their shares to pursue new business ventures. R. at 4, 5. A private placement process was completed, and Gemstar's common shares were sold to sixteen institutional investors. Two months later, an airplane that used a machine tool manufactured by Gemstar experienced an explosion. R. at 7. An investigation implicated the machine tool manufactured by Gemstar as the cause of the explosion. R. at 7. Petitioner, the Fordham Public Employees Investment Fund (hereinafter "the Fund" or "Petitioner"), purchased Gemstar's shares during the private placement process and incurred losses when they sold their position after the explosion. R. at 7.

I. The Birth of Gemstar

The story of Gemstar begins with the fateful meeting of Grace Underwood (hereinafter "Underwood") and Danielle Scott (hereinafter "Scott") at a business conference in New York City. R. at 1. Both women were recent business school graduates that inherited significant wealth at a young age. R. at 1. More importantly, both women were interested in pursuing independent business careers despite their youth and lack of experience. R. at 1. After their meeting, the ambitious pair spent the next three years balancing their interests, leveraging their business networks, and searching for a company with their desired growth potential. R. at 2.

At last, Underwood and Scott were introduced to McGrath, Inc., a manufacturer with a sophisticated machine tool business for sale. R. at 2. The business blended the interests of the dynamic duo and met their desired growth metrics. R. at 2. Underwood and Scott agreed to purchase the business, after a due diligence review was completed and standard closing conditions were met. R. at 2.

With respect to the due diligence review, Underwood and Scott employed an engineering firm, MMD Inc. (hereinafter "MMD"), to determine whether the business's physical assets were in satisfactory condition for intended use. R. at 3. In their report, MMD deemed the business' property, plant, and equipment suitable. R. at 3. But MMD also noted trade literature describing a composite used by the business's machine as having characteristics that might lead to the development of microscopic cracks over time and under stress. R. at 3. This information was either overlooked or deemed inconsequential to the final due diligence review. R. at 3.

Underwood and Scott also employed Forsyth Financial (hereinafter "Forsyth") to evaluate potential markets for the business and to assist with the search for a suitable senior manager. R. at 3. The pair wanted to hire and work closely with a skilled executive who could lead a turnaround effort, implement a growth plan, and teach them how to manage their own manufacturing business. R. at 2. Forsyth reported that the business was capable of substantial growth and identified Maya Neuberger (hereinafter "Neuberger") as a manager who could run day-to-day operations of the business. R. at 2.

Thus, the business was purchased, and Gemstar was born, with Underwood serving as Chief Executive Officer, Scott serving as President, and Neuberger serving as Vice President of Operations. R. at 3. Underwood and Scott were at the helm of the operation, sharing responsibility all material executive decisions. R. at 3.

II. The Sale of Gemstar

Over the next three years, Gemstar gained notoriety in the machine tool industry and attracted customers via its most popular product, the SwiftMax. R. at 4. The SwiftMax was used to produce a fastener that could be applied in a variety of settings, including cargo jet aircrafts. R. at 4. Although Gemstar proved to be a successful venture, Underwood and Scott were ready to move on. R. at 4. The pair recruited Underwood's friend, Allison Ritter (hereinafter "Ritter"), to assist them with an exit strategy. R. at 4. Ritter was a Junior Managing Director at Carter Capital and agreed to advise Underwood and Scott on the sale of Gemstar. R. at 4. After reviewing the Gemstar's financial statements, Ritter presented three options for Underwood and Scott to discharge the business: a buyout, a strategic sale, or a private placement. R. at 4. A private placement would entail selling 80% of Gemstar to institutional investors while Underwood and Scott would retain 20% of the business via super voting shares. R. at 4. Although the Gemstar executives were reluctant to opt for private placement, they agreed to pursue it after Ritter explained that they needed to keep a substantial position in Gemstar for marketing purposes, even if they went on to run another company. R. at 5.

The private placement process was complicated and drawn out over a period of several months. R. at 5. Gordon served as Gemstar's Vice President of Investor Relations during this time and was tasked with organizing the process. R. at 5. Although Gordon's primary responsibility was to manage the flow of information to Carter Capital and others, her tasks included coordinating attorneys, financial advisors, auditors, engineering firms, and Gemstar's experts, who were constructing the Private Placement Memorandum (hereinafter "the Memo") to market the common stock to investors. R. at 5.

The principal engineering firm that Gordon worked with, Keane & Company (hereinafter "Keane"), gave her a report (hereinafter "the Report") detailing the structural integrity of Gemstar's assets and products. R. at 5. During her review of the Report, Gordon noted that Keane referenced no material deficiencies in Gemstar's facilities, capital machinery, and products. R. at 5. However, the Report included a memorandum (hereinafter "Trade Letter") by a former junior structural engineer that suggested the SwiftMax used a composite that could develop microscopic cracks under stress in extreme conditions over time. R. at 5, 6. The Trade Letter also included an article that supported the engineer's theory. R. at 6. Gordon was initially alarmed by the Trade Letter but calmed upon realizing it was over three years old. R. at 6. Gordon then decided to bring the Trade Letter to the attention of Gemstar's executives, Underwood and Scott. R. at 6.

When Gordon brought the Trade Letter to Gemstar's CEO and President, a contentious discussion between the two executives ensued. R. at 6. Underwood aggressively stated that the discussion was a waste of time because the Trade Letter was clearly outdated and written in error. R. at 6. Scott had her reservations, pondering aloud whether auditors were entitled to review the Trade Letter. R. at 6. Ultimately, Underwood's argument prevailed, and the executives decided it was best to remove the Trade Letter from the Report. R. at 6. Per the pair's instructions, Gordon removed the Trade Letter and delivered the Report to Gemstar's experts. R. at 6.

Soon after, the Memo was completed and established that Gemstar's property, plant, and equipment were in reasonable condition, there were no material defects in products sold to customers, and that there were no material undisclosed contingent liabilities relating to its products which were required to be noted in its financial statements. R. at 6. Gordon directed her associate to distribute the Memo to twenty-six of the country's largest non-bank financial institutions. The Memo was distributed on Gemstar's stationery and did not identify Gordon as the Vice President of Investor Relations. R. at 6.

Gemstar's common shares were sold to sixteen institutional investors at $27 per share and the private placement was officially complete. R. at 7. Underwood and Scott were made very wealthy and well-poised to chase their next business opportunity. R. at 7.

III. Explosion Aftermath

Shortly after the private placement process was completed, a cargo jet that utilized two fasteners manufactured by Gemstar's SwiftMax experienced an explosion. R. at 7. The Federal Aviation Administration (hereinafter "FAA") conducted investigations that pointed to the fasteners being the cause of the explosion, due to their having developed microscopic fissures over time and due to pressure. R. at 7. After FAA released its investigatory findings, the Fund, who purchased 3,000,000 shares of Gemstar's common stock during the private placement process, sold its entire position and incurred a loss of $68,000,000. R. at 7. The Fund filed suit against Gordon, Underwood, and Scott soon after, seeking compensatory damages for the same amount as their incurred loss. R. at 8.

SUMMARY OF THE ARGUMENT

The issue here is whether the lower court, by applying primary liability to the Respondent, carries out the purpose of section 10(b) and Rule 10(b) – 5. As an employee relying on instructions from her employers, who were experienced corporate executives and well-versed in the machine-tool industry, the Respondent does not fit the picture of a fraudster intending to deceive investors. Thus, this Court should reverse the lower court's decision.

To prevail on a claim under section 10(b) and Rule 10(b) – 5, the Fund must plead that Gordon made a false statement or omitted a material fact, with scienter, and that the Fund's reliance on Gordon's action caused the Fund's injury. At issue, are whether Gordon had the requisite scienter to be classified as a "disseminator" subject to primary liability and whether the Fund's reliance should be presumed under Affiliated Ute if they are making "mixed" allegations of both omissions and affirmative misrepresentations.

The United States District Court for the District of Fordham incorrectly held that the Respondent is subject to primary liability under Rule 10(b) – 5(a) and (c) and that the Petitioner was entitled to the *Affiliated Ute* presumption. Though the lower court correctly held that the Respondent did not qualify as a "maker" of false or misleading statements under Rule 10b–5(b) because she did not have ultimate authority over the statements, the lower court used the Respondent's instruction to an associate to disseminate the Memo as an act that qualifies her as a "disseminator" under Rule 10b–5(a) and (c) and consequently, subjected her to primary liability. The Respondent should not be classified as a "disseminator" because she lacks factual similarities to the defendant in *Lorenzo*. *Lorenzo v. Sec. & Exch. Comm'n*, 203 L. Ed. 2d 484 (2019). Furthermore, the Petitioner has failed to establish the requisite scienter for the Respondent, from which the "disseminator" classification in *Lorenzo* springs. For these reasons, the Respondent respectfully requests the Court to reverse the lower court's ruling on her motion to dismiss.

ARGUMENT

I. GORDON IS NOT SUBJECT TO PRIMARY LIABILITY UNDER 10(b) – 5(a) and (c) BECAUSE SHE LACKS SCIENTER.

Both the Securities Act of 1933 ("Securities Act") the Securities Exchange Act of 1934 ("Exchange Act") sought to address catalysts of the Wall Street Crash of 1929, including fraud and misrepresentation within the securities markets. Section 10(b) of the Exchange Act makes it unlawful "for any person … [t]o use or employ, in connection with the purchase or sale of any security … any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe[.]" *ESG Capital Partners, LP v. Stratos*, 828 F.3d 1023, 1032 (9th Cir. 2016). Section 10(b) laid the groundwork for the Securities Exchange Commission ("SEC") to promulgate Rule 10(b) – 5, which has become the primary mechanism for enforcing antifraud objectives in the securities markets today. Rule 10(b) – 5 states the following:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5. The plain text of Rule 10(b) – 5 does not provide for a private cause of action. However, in 1947, courts began to imply private causes of action to enforce "duties and liabilities" available to plaintiffs under the Exchange Act. *Kardon v. Nat'l Gypsum Co.*, 73 F. Supp. 798, 800 (E.D. Pa. 1947). In 1971, this Court confirmed via footnote that an implied private cause of action did exist under Section 10(b). *Superintendent of Ins. of State of N. Y. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 13 (1971). However, in the litigation that ensued, this Court cut back on the implied private cause of action. Nuisance suits brought by hawkish private lawyers to drain corporate assets did not serve the purpose of the Exchange Act. Congress responded to this curtailment accordingly. Through the Private Securities Litigation Reform Act of 1995 ("PSLRA"), Congress confirmed this Court's holding in *Central Bank of Denver v.*

First Interstate Bank of Denver, giving the SEC the right to bring suits against those who aid and abet violations of the securities laws. 15 U.S.C.A. § 78t. *See also Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver,* N.A., 511 U.S. 164, 173 (1994).

Irrespective of the debate surrounding the value of private causes of action under section 10(b) and Rule 10(b) – 5, these suits cannot proceed in the absence of any allegation of scienter or "a mental state to deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976). Since section 10(b) and Rule 10(b)–5 concern fraud, Rule 9(b) of the Federal Rules of Civil Procedure applies to the Fund's pleading of Gordon's scienter: "In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." Fed. R. Civ. P. 9. This requirement is further heightened in PSLRA, which sought to limit "abusive litigation in private securities fraud actions." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 308 (2007). PSLRA requires the Fund to "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C.A. § 78u-4. This Court has held that a strong inference under PSLRA is one that is "more than merely plausible or reasonable—it must be cogent and at least as compelling as any opposing inference of nonfraudulent intent." *Id.* at 314.

There are two ways for the Fund to adequately plead Gordon's scienter: first, by alleging facts establishing a motive to commit fraud and an opportunity to do so, and second, by alleging facts constituting circumstantial evidence of either reckless or conscious misbehavior. *In re Time Warner Inc. Sec. Litig.*, 9 F.3d

259, 269 (2d Cir. 1993). The lower court fails to establish Gordon's scienter by relying solely on her instruction to an associate to illustrate her furtherance of a deceptive plan. R. at 14.

In this case, opportunity is automatically transferred to Gordon as a result of her position within Gemstar in relation to investors. R. at 5. Since Gemstar controlled assembly of the Report, Gordon retained the opportunity to remove the Trade Letter per her employers' request. R. at 5. The inquiry into Gordon's motive, however, is trickier.

Gordon's motive should be demonstrated by the Fund through "concrete benefits" she could realize by omitting the Trade Letter. *Shields v. Citytrust Bancorp Inc.*, 25 F.3d at 1124, 1128 (2nd Cir. 1994). Specifically, concrete benefits refer to "economic" or personal reasons for fraudulent activities. *Atl. Gypsum Co., Inc. v. Lloyds Intern. Corp.*, 753 F. Supp. 505, 514 (S.D.N.Y. 1990). In this case, the Fund has not identified a distinct economic benefit to Gordon as a result of the Trade Letter's omission and her subsequent instruction to an associate. Economic benefits to Underwood and Scott are evident – both Gemstar executives were made "very wealthy" via completion of the private placement process. R. at 7. But the record is silent on any concrete economic benefits to Gordon that sprung from successful completion of the private placement. Moreover, any motive alleged by the Fund against Gordon to maintain the appearance of Gemstar's success and thereby protect her "position and compensation" is insufficient because these sentiments are "common to all corporate executives." *Kalnit v. Eichler*, 264 F.3d 131, 139 (2d Cir. 2001).

Without establishing Gordon's motive, the Fund's last hope is to plead facts alleging Gordon's reckless or conscious misbehavior. In *Kalnit*, the court declined to consider the defendant's failure to disclose a release, despite knowing of its existence, as reckless or conscious misbehavior because the duty to disclose the release was "not so clear." *Id.* The same holds true for Gordon – the Trade Letter contained hypotheses, not hard facts relating to the integrity of the composite. R. at 6. Furthermore, Gordon's confusion over the "outdated" Trade Letter and her duty to disclose it is apparent – she did not take any independent action with the Trade Letter and instead waited to consult with her employers, Underwood and Scott, before proceeding. R. at 6. Thus, the Fund has not established Gordon's scienter via motive and opportunity or reckless and conscious misbehavior.

A. Gordon's instruction to an associate was not inherently deceptive.

The attachment of scheme liability to Gordon under Rule 10b–5(a) and (c) "hinges on the performance of an inherently deceptive act…" *S.E.C. v. Kelly*, 817 F. Supp. 2d 340, 344 (S.D.N.Y. 2011). To determine whether an act is deceptive, courts consider an act's timing in relation to the alleged fraud. For example, in *Kelly*, the court held that the defendants could not be held liable under Rule 10(b)– 5(a) and (c) for organizing allegedly fraudulent round-trip transactions because the transactions only became deceptive in light of subsequent public misrepresentations. *Id.* Engaging in these transactions was a part of normal practice in the industry – fraud only attached to the misrepresentation. Similarly, Gordon's instruction to an associate was not deceptive in and of itself. R. at 6.

Instructing an associate is within the purview of her regular duties as a manager at Gemstar. The instruction only becomes deceptive at the time of the following misstatement: “There are no material undisclosed contingent liabilities relating to Gemstar’s products.” R. at 8. Fraudulence attaches to the misrepresentation, not to Gordon’s typical action of instructing an associate.

Gordon’s action is benign when compared to the flagrant actions of the defendant in *U.S. Environmental, Inc.*, who tried to avoid primary liability under Rule 10(b) – 5 by claiming that he did not share the manipulative purpose of his employer. *S.E.C. v. U.S. Envtl., Inc.*, 155 F.3d 107, 110 (2d Cir. 1998). The defendant was either reckless in not knowing or knew that his employer sought to manipulate stock prices and still effectuated trades to further his employer’s scheme. *Id.* at 112. At the time Gordon instructed an associate to distribute the Memo, she believed that the omitted Trade Letter was outdated and clearly written in error, thanks to her employer. R. at 6. The defendant in U.S. Environmental, Inc., in contrast, never received a similar reassurance from his employer. Similarly, the defendant in *Lee* “engaged in a deceptive course of conduct to defraud” because he personally assisted another defendant to disguise their underlying losses and knew that his assistance perpetuated fraudulent activity by the other defendant. *S.E.C. v. Lee*, 720 F. Supp. 2d 305, 334 (S.D.N.Y. 2010). He was not led to believe by the other defendant that his actions were innocent and commonplace, as Gordon was in the present instance.

The lower court leans heavily on the reasoning from *Lorenzo* to paint Gordon’s instruction to an associate as a deceptive act. *Lorenzo v. Sec. & Exch.*

Comm'n, 203 L. Ed. 2d 484 (2019). However, the factual distinctions between the two cases support Gordon's weakened liability. In *Lorenzo*, the defendant sent emails after he was made aware via public announcements that they contained statements that were categorically false, which, regardless of his boss's ultimate authority of the statements, made his actions inherently deceptive. *Id*. Furthermore, the defendant in *Lorenzo* sent the emails himself, not through an associate, and ratified his deceptive behavior by signing his emails with his name, identifying himself as "Vice President – Investment Banking, and encouraging the email recipient to call him directly with any questions, as opposed to his boss. *Id*. The defendant's knowingness is further supported by his failure to challenge his finding of scienter on appeal. *Id.*

Here, Gordon has not conceded to a finding of scienter because she relied exclusively on her employer to determine whether the Trade Letter was a "undisclosed contingent liability" – she did not have the luxury of the defendant in *Lorenzo*, who was made knowledgeable via public announcement of a company's depreciated assets. R. at 6. Moreover, the Memo disseminated by the associate did not contain any mention of Gordon and her position at Gemstar or otherwise encourage investors to approach her with concerns about the Memo. R. at 6. This further removes Gordon from the clutches of scheme liability, whereas the defendant in *Lorenzo* appeared to take ownership of the fraudulent misrepresentations by including his information. *Id*. Despite categorical similarities between the defendant in *Lorenzo* and Gordon, which include their leadership positions and oversight of communications, the glaring differences between the contexts of their actions should not be ignored.

The lower court cites language from *Rio Tinto* to support its application of the holding from *Lorenzo* to Gordon. R. at 13. However, the clarification of *Lorenzo* from *Rio Tinto* supports Gordon's lack of primary liability. According to *Rio Tinto*, to implicate Gordon under this Court's reasoning in *Lorenzo*, Gordon must have disseminated the misstatements herself. *Sec. & Exch. Comm'n v. Rio Tinto PLC*, 41 F.4th 47, 55 (2d Cir. 2022). Despite the lower court's hastiness to qualify Gordon as a disseminator via her instruction to an associate, the record is clear – Gordon did not click "send" on the Memo. R. at 7. Regardless of attempts by the lower court to trivialize this fact, it speaks to an individual's ownership of the alleged fraud. Subjecting Gordon to primary liability in the absence of this ownership is to wield the tool of private securities fraud actions abusively.

B. Subjecting Gordon to primary liability will extend the scope of Rule 10(b)-5.

The anti-fraud purposes of section 10(b) and Rule 10(b) – 5 are undisputed. However, the spirit of these anti-fraud provisions is easily marred through nuisance suits brought by private actors. Acknowledging this potential for abusive litigation, this Court has upheld requirements such as "scienter" and Congress has enacted legislation like PSLRA. The lower court misapplies *Lorenzo* and shirks the demands of precedent and purpose to hastily assign primary liability to Gordon.

The lower court admits that Gordon is not subject to primary liability by way of Rule 10(b) – 5(b) because she did not “make” the misstatements in the Memo, and she did not have “ultimate authority” over them. R. at 14. However, they believe classifying Gordon as a “disseminator” will subject her to primary liability under Rule 10(b) – 5(a) and (c). This is because the lower court incorrectly views *Lorenzo* as an extension of liability to disseminators. Primary liability only attaches to the “disseminator” in *Lorenzo* after the plaintiff established the tried-and-true requisite of scienter.

To subject Gordon to primary liability without establishing scienter and in light of the factual distinctions between Gordon and the defendant in *Lorenzo*, would constitute an extension of the scope of Rule 10(b) – 5. This Court has refrained from an extension of this sort because the origins of the private cause of action in securities fraud litigation was implied by courts to begin with. *Stoneridge Inv. Partners, LLC v. Sci.-Atlanta*, 552 U.S. 148, 167 (2008). This Court has also declined to dismantle the distinction between primary violators and aiders and abettors by applying “broad liability.” *Janus Capital Group, Inc. v. First Derivative Traders*, 564 U.S. 135, 146 (2011). Gordon does not fit the description of a “disseminator” as put forth by this Court in *Lorenzo* because she lacks scienter. For this reason, the lower court’s decision should be reversed.

II. The judicially inferred presumption of reliance under *Affiliated Ute* does not apply to the petitioner’s allegations

The *Affiliated Ute* precedent judicially infers the reliance element of both section 10(b) and Rule 10b-5, penciling in the “requisite causal connection” between a defendant's alleged misconduct and a plaintiff’s economic loss. *Stoneridge Inv. Partners, LLC v. Sci.-Atlanta*, 552 U.S. 148, 159 (2008) (quoting *Basic Inc. v. Levinson*, 485 U.S. 224, 243 (1988)).

This Court held that "[u]nder the circumstances of [the] case, ***involving primarily a failure to disclose***, positive proof of reliance is not a prerequisite to recovery[.] … This ***obligation to disclose and this withholding of a material fact*** establish the requisite element of causation in fact." *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 153–54 (1972). (emphasis added). Thus, any party seeking this presumption will need to prove that they [1] primarily allege omissions [2] by a defendant owing a special duty to disclose [3] who omitted material facts. Petitioner's claim fails if they do not concurrently satisfy all three aforementioned elements.

This Court has the opportunity to affirm the course of the *Affiliated Ute* presumption among the circuits. The majority of the circuits sail synchronously in accordance with *Affiliated Ute*, only applying the presumption to cases that primarily allege omissions. *Binder v. Gillespie*, 184 F.3d 1059, 1064 (9th Cir. 1999). Further, the Second, Third, Fourth, Fifth, Eighth, Ninth, Tenth, and Eleventh circuits have consistently held that a case does not primarily allege omissions if "a misrepresentation is necessary to create the specific expectation that the omission does not negate." *E.g. Johnston* v. *HBO Film Mgmt., Inc.*, 265 F.3d 178, 193 (3d Cir. 2001); *see Waggoner* v. *Barclays PLC*, 875 F.3d 79, 95 (2d Cir. 2017) (*Affiliated Ute* does not apply to "'half-truths … ' [or] misstatements whose only omission is the truth that the statement misrepresents"); *Cox* v. *Collins*, 7 F.3d 394, 395-96 (4th Cir. 1993) (same); *Smith* v. *Ayres*, 845 F.2d 1360, 1363 (5th Cir. 1988) (same) *Joseph* v. *Wiles*, 223 F.3d 1155, 1163 (10th Cir. 2000) (same); *Vervaecke* v. *Chiles, Heider & Co.*, 578 F.2d 713, 717-18 (8th Cir. 1978) (same); *Kirkpatrick* v. *J.C. Bradford & Co.*, 827 F.2d 718, 722 (11th Cir. 1987) (same).

This Court is faced with a pivotal decision. With a solidifying judgment here, the near-parallel paths of the circuits could be tied together into one clear holding. Such a holding would responsibly apply *Affiliated Ute* to the appropriate circumstances of evidentiary impossibilities and "speculative negatives", not to cases with a blurred delineation between alleged omissions and misrepresentations. *Binder*, 184 F.3d at 1064. To hold that the Fund's allegations invoke the weighty presumption would be to go beyond what necessitated the precedent and would cloud modern securities law.

Because the petitioner's allegations contain relevant affirmative misrepresentations, Gordon had no duty, and the alleged omitted information was immaterial, this Court should affirm the circuit court's decision and find that the petitioner is not entitled to the anomalous *Affiliated Ute* presumption.

A. Petitioner alleges numerous affirmative misrepresentations, which renders the *Affiliated Ute* presumption inappropriate and inapplicable.

Affiliated Ute's purpose is to remedy "the difficulty of proving 'a speculative negative'—that the plaintiff relied on what was not said." *Binder v. Gillespie*, 184 F.3d at 1064. (quoting *Blackie v. Barrack*, 524 F.2d 891, 905 (9th Cir. 1975)). Since "reliance is impossible or impractical to prove when no positive statements were made", *Affiliated Ute* serves an important purpose. *In re Volkswagen "Clean Diesel" Mktg., Sales Practices, & Products Liab. Litig.*, 2 F.4th 1199, 1206 (9th Cir. 2021).

However, Just the mere presence of affirmative misrepresentations can disqualify the necessity of *Affiliated Ute*. *In re Volkswagen*, 2 F.4th at 1206. This is because the suing party *could* prove reliance upon the alleged relevant misrepresentations. This opportunity to show reliance on the affirmative misrepresentations eliminates the necessity that is presented in cases that are primarily involving a failure to disclose. Expanding this precedent to cases that are mixed, including both omissions and affirmative misrepresentations, is against the majority of holdings of the circuit courts and gives plaintiffs an unfair advantage that sidesteps the legislatively imposed requirement of reliance. *Binder*, 184 F.3d at 1064.

Further, "mixed" allegations are not the appropriate realm for constructive reliance because the reasonable inability to prove reliance is absent. There is no need to presume the reliance of an alleged omission if several alleged misrepresentations of the same content were available to the petitioner. This reality is explored by the Ninth Circuit in *In re Volkswagen.*

In *In re Volkswagen*, "Volkswagen failed to disclose—for years—it was secretly installing defeat devices in its 'clean diesel' line of cars to mask unlawfully high emissions from regulators and cheat on emissions tests." *In re Volkswagen*, 2 F.4th at 1206. Volkswagen was concealing its "defeat devices" while simultaneously making affirmative misrepresentations in offering memoranda about the financial results and environmental regulation compatibility of its vehicles. *Id.* The Ninth Circuit held that the affirmative misrepresentations provided to the investor "push[ed] th[e] case outside Affiliated Ute's narrow presumption." *Id.* The court reasoned that it "look[ed] to the justification underlying the Supreme Court's decision in Affiliated Ute: reliance is impossible or impractical to prove when no positive statements were made." *Id.* Since there were adequate statements upon which reliance *could* be shown, the court found that *Affiliated Ute* would be inapplicable. Further, the court reasoned that the allegations were "based as much on what is there as what is purportedly missing." *Id.* at 1205 (quoting *Poulos v. Caesars World, Inc.*, 379 F.3d 654, 666 (9th Cir. 2004)). based as much on what is there as what is purportedly missing.

Moreover, The Ninth Circuit, as well as the Second, stated that the presumption cannot apply if the omission is ultimately just "the inverse" of the alleged misstatements. *Id.* at 1206–08; see also *Waggoner*, 875 F.3d at 96.

With respect to the Fund's allegations, there is a variety of affirmative representations and one omission. R. at 8. The positive representations state that Gemstar's assets and products are "in reasonable condition for their intended use", not "materially defective", and have no "material undisclosed contingent liabilities". *Id.* Inversely, the alleged omission is a hypothesis and supporting article suggesting that Gemstar's products have material defects. R. at 5-6. The alleged omission here is inescapably tethered to these misrepresentations which *could* be used to show reliance, removing the speculative negative debacle that summons the *Affiliated Ute* presumption.

This identifiable inverse nature of the misrepresentations and omissions exemplifies how omissions alone are not the heart of the case. Further applying the Ninth Circuit's reasoning, saying that there are no material undisclosed contingent liabilities relating to Gemstar's products is the "inverse" of concealing information on contingent liabilities relating to Gemstar products. The conjoined nature of these allegations accentuates the "mixed" nature of the present case. Since the affirmative statements were provided in the memo, there would be no reason to grasp for the evidentiary life raft that is *Affiliated Ute*. *Id.* This application is supported by this Court's reasoning in *Affiliated Ute* itself.

In *Affiliated Ute*, the financial entity had allegedly lied about its adherence to financial procedures and omitted a secondary market scheme. *Affiliated Ute*, 406 U.S. at 133-39. The financial entity had told its shareholders that it was selling equity at the prevailing market price but concealed a secondary market that it had constructed to break procedure and sell stock at manipulated prices. *Id.* This Court held that, "[u]nder the circumstances of this case", positive proof of reliance was not necessary. *Id.* at 153. The circumstances prompting the presumption were that the omission of the secondary market and secret equity distribution scheme were the primary allegations of the suit. *Id.* This Court reasoned that it would be "unnecessarily unrealistic" to require the plaintiffs to show "how [they] would have acted" if they had known about the secondary market for their stock. *Basic Inc.*, 485 U.S. at 245 (citing *Affiliated Ute Citizens of Utah*, 406 U.S. at 153–54).

The allegations against Gordon are not on the same plane as those in *Affiliated Ute* because of the omission's substance. In *Affiliated Ute*, the omissions were not just the "inverse" of the misrepresentations, but a concealment of an entirely different sale scheme that broke procedures and economically abused the investors. The affirmative misrepresentations about stock prices were not in the same vein as the construction of a secondary market and subsequent procedural desecration of the Ute contract. There was no affirmative misrepresentation that substantively held the gravamen and provided an opportunity to show reliance.

Here, unlike *Affiliated Ute*, the misrepresentations and omissions are of the identical substance. Suing over a statement that Gemstar's products have no material defects or liabilities is the same as suing that you did not know that Gemstar's products had material defects or liabilities. The Second Circuit comments on this mix of allegations by holding that the presumption does not apply to "misstatements whose only omission is the truth that the statement misrepresents" *Waggoner*, 875 F.3d at 96.

An application of *Affiliated Ute* here would be far from a clearing of evidentiary burdens like those presented in omissions allegations where proof of reliance on an absent item is "virtually impossible" 24 *Wilson v. Comtech Telecomms. Corp.*, 648 F.2d 88, 93 (2d Cir. 1981). An application here would give the petitioner an evidentiary advantage as opposed to an even playing field.

Ultimately, "the Affiliated Ute presumption of reliance does not apply [here] because Plaintiff can prove reliance through ordinary means by demonstrating a connection between the alleged misstatements and its injury." *In re Volkswagen*, 2 F.4th at 1209.

Similar to the Ninth Circuit's lead, most circuits have confined *Affiliated Ute* to cases that are primarily omissions to avoid any application that would smudge the chalk line of applicability between omissions and affirmative misstatements. *Binder*, 184 F.3d at 1064. Otherwise, the presumption would "swallow the reliance requirement [and] fail to serve the Affiliated Ute presumption's purpose since this is not a case where reliance would be difficult to prove because it was based on a negative." *In re Volkswagen*, 2 F.4th at 1205–06, quoting *Joseph v. Wiles*, 223 F.3d 1155, 1163 (10th Cir. 2000), *abrogated by California Pub. Employees' Ret. Sys. v. ANZ Sec., Inc.*, 198 L. Ed. 2d 584, 137 S. Ct. 2042 (2017).

A decision keeping the *Affiliated Ute* presumption in check is a fundamentally good outcome. This Court cautioned against expanding the slippery notion that a "defendant could be liable without any showing that the plaintiff relied upon the aider and abettor's statements or actions" *Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 180 (1994). This Court further stated that Section 10(b) "is surely badly strained when construed to provide a cause of action . . . to the world at large," and "[a]llowing plaintiffs to circumvent the reliance requirement would disregard the careful limits on 10b-5 recovery mandated by our earlier cases." *Stoneridge*

Inv. Partners, LLC, 552 U.S. at 157, 162, (quoting *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 733 (1975)). This direction of caution has led the majority of circuits to refuse to apply the *Affiliated Ute* presumption to cases in which a plaintiff alleges both misstatements and omissions, the exact setting of the Funds allegations. *Binder*, 184 F.3d at 1064.

B. Even if the allegations are primarily omissions, Gordon did not withhold material information.

Even if this Court finds that the allegations are primarily omissions, the petitioner must also satisfy that Gordon had a duty of disclosure and this information was material. *Affiliated Ute Citizens of Utah*, 406 U.S. 128, 153–54 (1972).

This Court has "defined a standard of materiality under the securities laws" in *TSC Industries v. Northway Inc.* that has been "expressly adopt[ed]'" as the standard for the section 10(b) and Rule 10b–5 context. *Basic Inc.*, 485 U.S. at 231–32. For an omission to be material, "there must be a *substantial* likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having *significantly altered the 'total mix'* of information made available." *Id.* (emphasis added).

Further, in the 2011 decision of *Matrixx*, this Court stated "We were 'careful not to set too low a standard of materiality,' for fear that management would 'bury the shareholders in an avalanche of trivial information.'" *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 38 (2011), (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 448–449 (1976)). Such an avalanche would force “a result that is hardly conducive to informed decisionmaking.” ***TSC Industries, Inc.*****, 426 U.S. at 448–449**.

Applying this Court’s standard and preference for avoiding an “avalanche of trivial information”, an outdated trade letter containing an article and a suggestive hypothesis considered by a departed junior structural engineer would fall well short of material. R. at 5.

Along with standard financial statements, some information that Gordon disclosed as a part of “the Memo” included a fifty-six-page report that detailed the firm’s policies and procedures, facilities, capital machinery, products, and other boilerplate financial information. *Id.* Gordon coordinated with attorneys, financial advisors, auditors, engineering firms, and other experts in constructing the financial and physical report of the firm. *Id.*

Among all the financial statements, corporate detail, and routine background information which investors would rely upon, this Court must answer whether there would be a *substantial* likelihood that the disclosure of the departed junior engineer’s over three-year-old hypothesis and the supporting article would have been viewed by the reasonable investor as having *significantly altered the total mix* of information made available. *Id.*

Finding that the hypothesis and article satisfy the *substantial likelihood* to *significantly alter* standard would be to apply a bias of hindsight. This Court should not judge past evaluations with the conclusions of the future. This analysis must be done with the perspective of May 2021, before the FAA’s investigation seemingly proved the dated hypothesis correct. R. at 7.

Given that Gemstar had been operating as a substantial presence for multiple years and provided extensive data on their finances and property, plant, and equipment, a peripheral notion of potential defects in the composite from several years in the past would not, with a substantial likelihood, significantly alter the total accumulation of data available on Gemstar. R. at 4-7.

This Court in *Basic* reasoned that the materiality analysis need not be rigidly formulaic. *Basic Inc.*, 485 U.S. 224, 236 (1988). This Court further referenced a Second Circuit decision identifying the role of materiality in stating that materiality "will depend at any given time upon a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity." *Id.* at 238. (quoting *Sec. & Exch. Comm'n v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 849 (2d Cir. 1968)).

Looking at the probability of this information being material or relevant, a reasonable investor would base their confidence in company history, financial statements, and equipment reports, just as Grace and Danielle did when they purchased the company in 2018. R. at 3. Every investment is risky and this Court should avoid recognizing "fraud by hindsight." See, *e.g., Shields v. Citytrust Bancorp, Inc.*, 25 F.3d 1124, 1129 (2d Cir. 1994) (quoting *Denny v. Barber,* 576 F.2d 465, 470 (C.A.2 1978) (Friendly, J.)).

To hold this information to be material would force the forewarned avalanche upon investors, inhibiting capital market efficiency and congesting the free market with judicial red tape. More time, money, and resources would be spent delineating important information out of the overflow that offering businesses will provide to play it safe if this Court expands the scope of materiality to include such peripheries. Further, business evaluations would be mired by offering organizations trying to cover themselves from liability. Such a precedent would force diligent workers like Gordon to poll ex-employees, even junior engineers, on their outlook and beliefs regarding product qualities and liabilities and then relay such information no matter how discouraging or inaccurate to potential investors. This precedent would overcomplicate the offering process and hurt the ability of the offering company to fight for a competitive sale. Thus, this Court should uphold its avoidance of setting "too low a standard of materiality." *Matrixx Initiatives, Inc.*, 563 U.S. 27, 38 (2011) A decision for the Fund would veer dangerously close to the edge of drowning investors in an overbreadth of miscellaneous information.

C. Gordon had no duty to disclose because she had no fiduciary or other special relationship of trust and confidence, therefore *Affiliated Ute* does not apply.

Gordon was absent a duty to disclose. A duty to disclose arises out of a fiduciary, or other special relationship of trust and confidence. *Chiarella v. United States*, 445 U.S. 222, 228–29 (1980).

As a minuscule cog in Gemstar's corporate machinery, having no contact personally with or name representation to the Fund, Gordon had built no personal relationship of trust and confidence, and thus, formed no duty to disclose the information from the trade letter. The cover letter did not invite investors to inquire further about the contents of the offering memorandum or identify Gordon as Vice President of Investor Relations. R. at 6. She is nothing more than a communicator, carrying out the will of her directors.

Moreover, she has no absolute statutory duty as "it bears emphasis that § 10(b) and Rule 10b-5(b) do not create an affirmative duty to disclose any and all material information." *Matrixx Initiatives, Inc.*, 563 U.S. at 44. Gordon, specifically, and the Fund are just two sophisticated "parties to an impersonal market transaction" and she had no fiduciary duty of affirmative disclosure since she never established a relationship of trust and confidence in her specific role. *Paracor Fin., Inc. v. Gen. Elec. Cap. Corp.*, 96 F.3d 1151, 1157 (9th Cir. 1996). Therefore, *Affiliated Ute* does not apply.

Conclusion

Gordon is not subject to primary liability because she did not disseminate the Memo in a way that was factually parallel to the defendant in *Lorenzo* and she lacks the requisite scienter. Further, *Affiliated Ute* is inapplicable and inappropriate here because: [1] petitioner alleges several misrepresentations upon which they *could* prove reliance, [2] Gordon had no duty to disclose such information, and [3] Gordon did not withhold material information. For the foregoing reasons, this Court should affirm.