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Skadden

# Inside the Courts
# An Update From Skadden Securities Litigators

## Derivative Litigation

### Eighth Circuit Affirms Dismissal of Derivative Securities Action

*Carpenters' Pension Fund of Ill. v. Neidorff*, No. 20-3216 (8th Cir. 2022)

Following Centene Corporation's merger with Health Net, Inc., several shareholders brought a derivative action against some of Centene's directors and officers, alleging violation of Section 14(a) of the Exchange Act and various breaches of fiduciary duties. The shareholders did not make a pre-suit demand on Centene's board, and the district court dismissed their complaint with prejudice, holding that they failed to adequately plead that demand would have been futile. The shareholders appealed.

In their amended complaint, the shareholders alleged that the defendants failed to disclose Health Net's financial issues and problematic business practices in the proxy statement asking for shareholder approval of the merger. After the merger closed, Centene released financial results revealing a $390 million increase in reserves for Health Net's increased liabilities. Following this disclosure, Centene's stock price dropped 8%.

The U.S. Court of Appeals for the Eighth Circuit first denied the shareholder-appellants' request to remand and replead due to Delaware's new demand futility test, which was issued after the district court dismissed the shareholders' amended complaint, since the new test "'is consistent with and enhances *Aronson*, *Rales*, and their progeny,' which 'remain good law.'"

Reviewing the district court's decision *de novo*, the court proceeded to analyze the appellants' claims and allegations under the *Tri-State* test. The only question at issue was whether at least half of the board would face a substantial likelihood of liability on the claims in the amended complaint. As to the Section 14(a) claims, the court held that the cautionary language in Centene's proxy statement rendered the omission of Health Net's problems immaterial as a matter of law and that Centene was not required to update the proxy statement.

The court then reviewed the appellants' breach of fiduciary duties claims, holding first that the director defendants faced no substantial likelihood of liability for breaches of the duty of care under Delaware law because Centene's articles of incorporation contained an exculpation provision. The court then affirmed the district court's assessment that the shareholder-appellants failed to show that the director defendants acted in bad faith, and thus failed to plead a substantial likelihood of liability as to the breach of duty of loyalty claim. The court held that demand was futile as to the insider trading claim — which was brought against only two of the eight director defendants — since the claim was not "so intertwined" with the other claims that its pursuit would expose the other directors to a risk of liability. Finally, the court found that the unjust enrichment claim was "entirely duplicative" of the breach of fiduciary duty claim and affirmed its dismissal.

Holding that the appellants failed to plead particularized facts demonstrating that at least half of the board faced a substantial likelihood of liability as to the claims brought in the amended complaint, the court affirmed the district court's dismissal of that complaint.

## Fiduciary Duties

### Court of Chancery Dismisses 220 Suit for Failure To Show That Documents Were 'Necessary and Essential'

*Okla. Firefighters Pension & Ret. Sys. v. Amazon.com, Inc.*, C.A. No. 2021-0484-LWW (Del. Ch. June 1, 2022)

The Delaware Court of Chancery dismissed a plaintiff's complaint seeking inspection of additional books and records relating to purported mismanagement of Amazon.com, Inc.'s directors and officers in connection with Amazon's compliance with certain antitrust and tax laws. The court held that the plaintiff had neither substantiated a proper purpose for inspection nor demonstrated that the books and records sought were necessary and essential to its stated purpose.

In June 2020, the plaintiff, an Amazon stockholder, sent Amazon a demand pursuant to Del. Code Ann. tit. 8, § 220 to inspect books and records to (i) investigate possible mismanagement by Amazon's directors and officers regarding domestic antitrust and state tax laws; and (ii) assess the independence and disinterestedness of Amazon's directors. The demand sought 19 categories of documents across an 11-year period. Amazon responded that the demand was overbroad and lacked a proper purpose for failure to set forth a credible basis to infer wrongdoing by Amazon's officers or directors. Nevertheless, in December 2020, Amazon produced formal board materials from meetings relating to antitrust investigations in the 18 months prior to the demand. Amazon then made a supplemental production in March 2021. In total, Amazon produced 729 pages of board materials with nonresponsive material redacted. Without further negotiation with Amazon about its production of documents, the plaintiff filed its Section 220 complaint on June 3, 2021.

Following a trial on a paper record, the court addressed two issues: (i) whether the plaintiff had a proper purpose; and (ii) assuming the plaintiff had stated a proper purpose, whether records beyond those already produced by Amazon were necessary and essential to the stated purpose. The court answered both questions in the negative.

First, the court acknowledged that although investigating mismanagement and assessing the directors' independence have been "consistently recognized" as proper under Delaware law, the plaintiff still had not carried its burden to plead a credible basis from which the court could infer possible mismanagement. With respect to investigating mismanagement, the plaintiff failed to provide evidence of wrongdoing that would warrant further investigation. The court recognized that while "[o]ngoing investigations and lawsuits can provide the necessary evidentiary basis to suspect wrongdoing" to warrant further investigation, this evidence does not "necessarily beget[] a credible basis from which the court can infer possible mismanagement." Indeed, the scale of investigations and lawsuits, the severity of those inquiries and corporate trauma inform whether there is potential wrongdoing to support a stockholder's books and records demand. The court concluded that the plaintiff's attempt to use government antitrust or tax investigations that had either closed without consequence or were pending fell below the level needed to warrant further investigation. The court also rejected the plaintiff's purported purpose of assessing director independence because the plaintiff offered no evidence that might cast doubt on the directors' impartiality or independence.

Second, the court held that even if the plaintiff had demonstrated a proper purpose, it was not entitled to further books and records. The court praised Amazon attempting to avoid litigation and for taking "the lessons of [Delaware] case law to heart" and responding to a "facially valid" demand by producing "the core, formal board materials that generally satisfy a company's obligations under Section 220," rather than "reject[ing] the demand out of hand, plac[ing] unreasonable conditions on inspection, or rais[ing] a panoply of merits-based defenses." Because the plaintiff did not introduce evidence of "atypical circumstances" or "wide-ranging mismanagement" that would justify going beyond the formal materials Amazon produced, the court found that the plaintiff had not shown that additional documents were necessary and essential to achieving its stated purposes, and thus the plaintiff was not entitled to further books and records.

Finally, the court held that the plaintiff had no grounds to challenge Amazon's responsiveness redactions. Although responsiveness redactions are disfavored in civil discovery, the court explained that Section 220 inspection "[is] a different matter entirely" because it only entitles a stockholder to information in board materials that is essential to the stockholder's purpose.

### Court of Chancery Denies Motion To Dismiss Breach of Fiduciary Duty Claims Involving Company's Sales Process

*Goldstein v. Denner*, C.A. No. 2020-1061-JTL
(Del. Ch. May 26, 2022)

The Delaware Court of Chancery denied in part a motion to dismiss breach of fiduciary duty claims against Bioverativ, Inc.'s. directors and officers that challenged the company's sale process and related disclosures.

In May 2017, Sanofi S.A. approached two of Bioverativ's directors, Alexander J. Denner and Brian S. Posner, and expressed interest in making an offer to buy the company for roughly $90 per share, a significant premium to the stock's market price. Neither director disclosed this information to Bioverativ's board of directors. Instead, Denner allegedly caused a hedge fund that he controls to buy more than a million shares of Bioverativ's common stock, which allegedly violated the company's insider trading policy. Denner allegedly did not disclose these purchases to the board. Months later, after expiration of the short swing profits period under the Securities Exchange Act of 1934, Denner and Posner invited Sanofi to participate in a single-bidder process. The transaction, structured as a friendly tender offer for $105 per share, closed on March 8, 2018.

The stockholder plaintiff alleged that the directors breached their fiduciary duties by failing to obtain the highest value reasonably available for Bioverativ's stockholders in the transaction, and that certain directors and officers breached their fiduciary duties by preparing and approving a false, incomplete and materially misleading Schedule 14D-9. The defendants moved to dismiss the complaint.

First, the court found it was reasonably conceivable that *Corwin*, a standard under which breaches of fiduciary duty can be cleansed by a fully informed stockholder vote in the absence of a controlling stockholder, was inapplicable because of multiple disclosure deficiencies that prevented fully informed stockholder approval. Specifically, the court took issue with, *inter alia*, the series of incomplete or inaccurate disclosures about Denner's and Posner's interactions with Sanofi, the timing of Denner's hedge fund's stock purchases, and downward adjustments made to Bioverativ's projections.

Concluding that *Corwin* cleansing was unavailable, and because the transaction involved a sale of Bioverativ for cash, the court applied enhanced scrutiny, acknowledging that "[t]he sins of just one fiduciary can support a viable *Revlon* claim." The court agreed with the plaintiff that it was reasonably conceivable that Denner faced a conflict because (i) he wanted to achieve a near-term sale as part of his activist playbook; and (ii) he sought to lock in quick and massive profits on the shares he caused his hedge fund to acquire based on inside information.

Notably, the court observed that "[o]rdinarily … significant holdings of Company common stock would help undermine any concern about a divergent interest," but activist hedge funds "may espouse short-term investment strategies and structure their affairs to benefit economically from those strategies, thereby creating a divergent interest in pursuing short-term performance at the expense of long-term wealth." Because Denner was allegedly acting "in accordance with a known playbook, the plaintiff [received] the benefit of an inference at the pleading stage that the defendant is following the playbook." Similarly, the court found the plaintiff entitled to the inference that but for Denner's undisclosed conflicts, the sale process would have unfolded differently.

The court also noted that a viable claim under the enhanced scrutiny standard is necessary but not sufficient to survive a pleading-stage motion to dismiss when the plaintiff seeks to impose personal liability on a director. Because of Bioverativ's exculpatory provision, the plaintiff needed to allege that each director was interested in the transaction, lacked independence or acted in bad faith.

Because of his alleged violation of Bioverativ's insider trading policy, concealment of illicit stock purchases and manipulation of the sale process, the court found the complaint "easily" pled that Denner acted in bad faith. Similarly, the complaint supported a reasonable inference that Posner acted in bad faith by engaging in early discussions with Sanofi and concealing this material information from the board.

As for Bioverativ's CEO, John G. Cox, in his capacity as the lone inside director, the court focused on his $72.3 million severance benefits that "dwarfed" his average annual compensation of $11.6 million. After acknowledging prior Delaware case law stating that change-in-control benefits do not create a conflict of interest, the court determined that this precedent "did not assert that proposition as a matter of law, but rather determined on the facts presented ... that a specific change-in-control payment did not give rise to a disabling interest for a specific defendant." Because the change-in-control payment that Cox received constituted a benefit not shared with Bioverativ's other stockholders and was sufficiently large to be material to him, it therefore constituted a compromising interest.

With respect to the other three directors, the court focused on their relationships with Denner. For two directors, though "close call[s]," the court found the directors lacked independence from Denner based on either their relationship history with him or the circumstances surrounding their board appointment. On the other hand, due to the timing of his board appointment and lack of other history with Denner, the court found a third director did not lack independence. The court rejected the plaintiff's argument that vesting of options and other equity awards and the immediate payout on those awards created a material conflict of interest for all the directors.

The court also concluded that the complaint sufficiently pled that the CEO and CFO were interested in the transaction and acted disloyally when failing to disclose Denner's hedge fund's stock purchases to the board, and in revising Bioverativ's projections downward allegedly for the purpose of justifying a lower deal price from the buyer. Similarly, the court found Bioverativ's chief legal officer (CLO) was interested in the transaction, as she stood to receive severance payments more than four times her annual compensation. The complaint also alleged that the CLO took steps to create a paper record that would enable the transaction to close. The court credited the plaintiff's allegation, that rather than creating a record in the sense of creating documents that accurately reflected what had taken place, the CLO "embellished" and documented events that did not occur and described other events in a manner that made the process seem better than it was. Further, the CLO then allowed those exaggerated accounts to become the basis of Bioverativ's disclosures.

Finally, the court held that the plaintiff successfully pled a disclosure claim. The court concluded that the officer defendants were not protected by the exculpatory provision, and it was reasonable to infer that they could be liable for the material misstatements or omissions in the Schedule 14D-9. Likewise, even though the director defendants were protected by the exculpatory provision, the court concluded that it was reasonably conceivable that they were either interested or acted in bad faith in approving the disclosures.

### Court of Chancery Applies Equitable Principles and Finds Compelling Justification for Stock Sale

*Coster v. UIP Cos.*, C.A. No. 2018-0440-KSJM (Del. Ch. May 2, 2022)

On remand from the Delaware Supreme Court, the Delaware Court of Chancery, applying equitable review, determined that a stock sale was valid because the board had a compelling justification for the transaction and did not approve it for inequitable purposes. In a prior decision, the Court of Chancery had concluded that the stock sale satisfied the entire fairness standard. After the Delaware Supreme Court reversed and remanded due to the Court of Chancery's failure to engage in an equitable review of the stock sale, the court applied equitable principles under *Schnell* and *Blasius* and found that the transaction did not run afoul of these cases.

Prior to the litigation, UIP Companies, Inc.'s common stock was owned equally by plaintiff Marion Coster and Steven Schwat, both of whom were directors. After unsuccessfully negotiating a substantial buyout of her interest, Coster called two special meetings of stockholders to elect directors to fill vacant board seats. Coster and Schwat deadlocked at those meetings, prompting Coster to sue seeking appointment of a custodian. Coster sought broad powers for the custodian, which jeopardized UIP's contracts and therefore threatened the company's revenue stream. In response to Coster's request for a custodian and in an effort to thwart that action, Schwat caused UIP to sell its outstanding but unissued voting equity to longtime employee Peter Bonnell.

Coster filed a second suit seeking to invalidate this stock sale. In its original post-trial memorandum opinion, the court held that the stock sale satisfied the entire fairness standard and entered judgement accordingly. On appeal, the Delaware Supreme Court criticized the trial court's failure to conduct an equitable analysis, writing "[i]f the board approved the Stock Sale for inequitable reasons, the Court of Chancery should have cancelled the Stock Sale." The Delaware Supreme Court remanded and directed the Court of Chancery to evaluate the transaction under *Schnell* and *Blasius*.

Faced with a "vexingly complicated or unique" situation, the court found that the stock sale did not run afoul of *Schnell* or *Blasius*. First, the court determined that *Schnell* can only apply to disenfranchising actions made in bad faith. The court acknowledged that the stock sale had some improper purposes like disenfranchisement, but "did not totally lack a good faith basis" because it was also motivated to serve the company's best interests. Interpreting *Blasius* as a "carve-out" to *Schnell* for disenfranchising actions taken in good faith, the court analyzed whether UIP's board's "primary purpose" was to disenfranchise Coster and, if so, whether UIP's board could show a "compelling justification." The court answered both questions in the affirmative: the stock sale was implemented for the primary purpose of mooting Coster's lawsuit seeking a custodian and reducing her leverage in trying to force a buyout of her equity. However, the court concluded that the board carried its burden of demonstrating a compelling justification for the stock sale because allowing the action seeking a custodian to proceed posed an existential threat to UIP. The court also held that the stock sale was appropriately tailored to achieve the goal of mooting the custodian action while also achieving other important goals. Therefore, the court declined to cancel the stock sale.

## Materiality

### Northern District of Illinois Dismisses Securities Fraud Putative Class Action Against Fifth Third Bancorp With Prejudice

*Heavy & Gen. Laborers' Local 472 & 172 Pension & Annuity Funds v. Fifth Third Bancorp*, No. 20 2176 (N.D. Ill. May 24, 2022)

Judge Sara L. Ellis of the Northern District of Illinois dismissed a putative securities class action against Fifth Third Bancorp for the second time (this time with prejudice). The plaintiff alleged violations of Sections 10(b) and 20(a) of the Exchange Act against Fifth Third and two of its executives. The court dismissed the first complaint for failure to plead scienter, and dismissed the amended complaint, at issue in this litigation, for both failure to plead false statements or omissions and failure to plead scienter.

This litigation arose out of the Consumer Financial Protection Bureau's (CFPB's) action filed against Fifth Third for alleged improper sales practices still pending in the Southern District of Ohio. The plaintiff alleged that four categories of statements made by Fifth Third were false and misleading: "(1) business practices, risk management systems, and risk environment; (2) Code of Business Conduct and Ethics; (3) product cross-selling and consumer practices and relations; and (4) incentive compensation." The plaintiff argued that Fifth Third's failure to disclose "the CFPB investigation; the bank's admissions, during the course of the investigation, of unauthorized sales practices; and the conscious failure of senior management to identify additional misconduct and remediate those practices" rendered those statements misleading.

The court held that, as an initial matter, Fifth Third had no duty to disclose the CFPB investigation. It then reviewed the allegedly misleading statements and held that (i) Fifth Third's risk management statements were too general to be actionable; (ii) its code of conduct statements did not include factual representations supporting a claim of materiality; (iii) its consumer practice statements were too vague, general and optimistic to be actionable; and (iv) its incentive compensation statements were not misleading, as the plaintiff had mischaracterized them.

The plaintiff further argued that an inference of scienter was warranted due to an internal email about alleged misconduct, consumer complaints, Fifth Third's own public disclosure of fewer than 2,000 unauthorized accounts, the CFPB's civil investigative demands to Fifth Third and the CFPB investigation. Several of these alleged events took place before the class period.

The court held that events preceding the class period could not support an inference of scienter during the class period. It then held that the allegations did not support the plaintiff's conclusion that "there were persistent account problems or a culture of abusive sales practices" or widespread misconduct that would have been escalated to Fifth Third's executives. It further held that the CFPB investigation, given the weakness of the plaintiff's other allegations, did not support an inference of scienter.

The court held that the plaintiff failed to state a claim for a violation of Section 10(b), and thus failed to state a claim for a control person violation of Section 20(a) against the executives as well. The court dismissed the amended complaint with prejudice and terminated the case.

### Eastern District of Tennessee Denies Defendants' Motion To Dismiss Putative Securities Class Action

*In re CBL & Assocs. Props., Inc. Sec. Litig.*,
No. 1:19-CV-00181-JRG-CHS (E.D. Tenn. May 3, 2022)

Judge James Ronnie Greer of the Eastern District of Tennessee dismissed claims alleging that CBL & Associates Properties, Inc. and several of its directors and officers (the individual defendants) violated Sections 10(b) and 20(a) of the Exchange Act. Judge Ronnie Greer dismissed the claims as to CBL because a bankruptcy court had approved a plan that barred the plaintiffs from pursuing the claims. The court declined to dismiss the allegations against the individual defendants after analyzing the plaintiffs' Section 10(b) claims against CBL in order to determine whether the Section 20(a) claim against the individual defendants could survive the defendants' motion to dismiss.

Central to the dispute was a separate litigation in which CBL was sued (Florida litigation) for allegedly reselling electricity to its commercial tenants for a profit, even though its contracts with them stated otherwise. CBL settled that suit. The plaintiffs in this case alleged that CBL violated Section 10(b), and that the individual defendants violated Section 20(a) by failing to disclose the alleged fraudulent scheme, making false statements about the litigation, overstating CBL's revenue and certifying that its SEC filings were prepared in accordance with GAAP. The court first held that CBL's statement that the Florida litigation was meritless was materially misleading because the Florida plaintiffs' claims had already survived summary judgment when the statement was made. The court further held that the plaintiffs could bring their allegations under GAAP and Item 303 as a subset of their § 10(b) claim, and that those claims were sufficiently pled because CBL's failure to disclose the Florida litigation violated ASC 450.

The court also found that the plaintiffs sufficiently pleaded that CBL's revenue statements were materially misleading because CBL attributed revenue to legitimate business practices rather than the fraudulent scheme. The court also rejected CBL's argument that the plaintiffs' allegations failed to satisfy the PSLRA because they were copied and pasted from the Florida litigation. Finally, the court rejected CBL's argument that the statements about revenue were not material given that the amount allegedly generated from the fraudulent scheme was less than 5% of its revenue, noting that the Sixth Circuit "appears to disapprove of the dismissal-by-numbers approach that CBL invites the Court to embrace."

The court considered the *Helwig* factors to determine whether these gave rise to a strong inference of scienter. Finding that the plaintiffs' allegations satisfied several of these factors, the court held that the plaintiffs sufficiently pled scienter.

The court rejected CBL's argument that its disclosure of the Florida litigation could not have caused a stock price decline because the litigation was already public. The court noted that CBL produced many discovery materials and filed court documents under seal, and then pointed to its discussion of CBL's statements about the Florida litigation, which implicitly rejected CBL's loss causation argument.

Finally, the court held that the plaintiffs sufficiently pled that the defendants were the "makers" of the statements under *Janus* because the plaintiffs alleged that the fraudulent scheme was the "brainchild" of two of the individual defendants and included specifics about when, where and how they devised the scheme. After holding that the plaintiffs adequately pled their § 10(b) claim, the court held the same regarding their § 20(a) claim and denied the defendants' motion to dismiss the plaintiffs' complaint.

## Securities Act Claims

### New York Supreme Court Dismisses Securities Act Suit Against Identity Management Platform

*Ret. Bd. of Allegheny Cnty. v. Ping Identity Holding Corp.*,
No. 654912/2021 (N.Y. Sup. Ct. 2022)

Justice Andrew Borrok of the New York Supreme Court dismissed claims against an identity management platform and its underwriters under Sections 11, 12(a)(2) and 15 of the Securities Act for allegedly false and misleading statements and omissions concerning purported sales slowdown before the COVID-19 pandemic. The plaintiff alleged that the offering documents prepared in connection with the company's secondary public offering misled investors to believe that it experienced a sales slowdown due to the COVID-19 pandemic, when it allegedly had been caused by the company's transition to SaaS solutions and failed to adequately disclose the impact the COVID-19 pandemic was having on the business.

The court held that the complaint failed to adequately allege a claim because the offering documents disclosed "the very performance" that the plaintiffs alleged was not disclosed. The complaint did not allege that the company's disclosed actual historical results were false or overstated, and acknowledged that the results were accurate. The court also reasoned that the company disclosed that it might experience additional COVID-19 pandemic disruptions. A confidential witness' allegations concerning certain downturn events that had occurred did not support a claim because those events were disclosed in the company's offering documents. The court also reasoned that, to the extent the complaint alleged that the offering documents failed to disclose the shift in revenue from term licenses to SaaS, the company made a financial projection, which it met.

## Securities and Exchange Commission

### Second Circuit Agrees With SEC, Denying Whistleblower Award

*Hong v. SEC*, No. 21-529 (2d Cir. July 21, 2022)

The Second Circuit affirmed the SEC's final ruling, finding that an alleged whistleblower was not entitled to an award for information that he provided to the SEC when the commission never initiated enforcement proceedings or secured a settlement, but shared the information with other federal agencies which then secured financial settlements.

The whistleblower, who worked as a managing director at an investment bank, alleged that he became aware of certain securities law violations involving the bank's residential mortgage-backed securities (RMBS). The whistleblower filed a tip, complaint or referral (TCR) form with the SEC, providing the commission with information about the possible securities law violations he learned about while working at the bank. The TCR was shared with federal RMBS working groups and other federal agencies, including the Department of Justice (DOJ) and the Federal Housing Finance Agency (FHFA), which interviewed the whistleblower and subpoenaed documents from him. In 2017, the FHFA settled with the bank for $5.5 billion. The following year, the DOJ settled with the bank for $4.9 billion.

The whistleblower applied to the SEC for a whistleblower award. The SEC whistleblower program provides that in any "covered judicial or administrative action, or related action," the SEC shall pay an award to individuals who voluntarily provided "original information" to the SEC "that led to the successful enforcement of the covered judicial or administrative action, or related action" in an amount between 10% and 30% "of what has been collected of the monetary sanction imposed in the action or related actions." 15 U.S.C. § 78u-6(b)(1). The SEC issued a final determination that the whistleblower was not entitled to an award because the FHFA and DOJ settlements were not actions "brought by the [SEC] under the securities laws," as required to qualify as "covered judicial or administrative action[s]" (alteration in original). The SEC further held that a "related action" could not be a basis for an award in the absence of a "covered action."

The Second Circuit agreed with the SEC's interpretation, applying *Chevron* deference. First, the court considered the SEC's interpretation of what constitutes a "covered judicial or administrative action," "brought by the [SEC]." The court concluded, at *Chevron* step one, that the statutory language was ambiguous. At *Chevron* step two, however, the court held that the SEC's interpretation that covered actions did not include settlements by other federal agencies was reasonable and, therefore, entitled to deference. Second, the court considered the meaning of "related action[s]" (alteration in original), and the SEC's ruling that a related action cannot serve as the basis for a whistleblower award in the absence of a covered action. The court held that, to the extent the statutory definition of "related action" is ambiguous, the SEC reasonably interpreted the phrase to require a predicate action brought by the SEC (*i.e.*, a covered action). The court identified no error in the SEC's interpretation of the whistleblower award provisions or the SEC's finding that, despite his contributions to recoveries obtained from the bank by the DOJ and the FHFA, he was ineligible for a whistleblower award from the SEC.

The court noted that it was "mindful that [its] decision may strike some as inconsistent with the principal statutory goal of the [SEC's Whistleblower] Program — namely, Congress's desire to incentivize and reward whistleblowers who may risk their reputations and careers to help hold financial institutions responsible for unlawful behavior." But the court explained, "it is not [the court's] role to rewrite the limitations on eligibility set forth in the Exchange Act, nor to override the SEC's reasonable interpretations of that statute, in order to ensure that this goal is satisfied in every instance."

## Fifth Circuit Vacates SEC Administrative Judgment as Unconstitutional

*Jarkesy v. SEC*, No. 20-61007 (5th Cir. 2022)

A split panel of the Fifth Circuit vacated and remanded a decision of the Securities and Exchange Commission (SEC) concerning an enforcement action against a hedge fund founder and investment adviser for alleged violations of the Securities Act of 1933, the Exchange Act and the Advisers Act. Before reaching the Fifth Circuit, an initial hearing on this matter had been conducted by an administrative law judge (ALJ), who concluded that the petitioners had violated federal securities laws. The petitioners appealed and sought review of the ALJ's ruling by the SEC. The SEC affirmed the ruling against the petitioners. The petitioners then filed a petition for review in the Fifth Circuit. In a 2-1 decision, the Fifth Circuit sided with the petitioners and held that the SEC proceedings at issue suffered from three constitutional defects.

First, the court held that the administrative hearings violated the petitioners' right to a jury trial under the Seventh Amendment. In so doing, the court applied a two-part test. The test's first prong asked whether the action's claims arose "at common law" under the Seventh Amendment. If the action involves common-law claims, the second prong of the test then asked whether the U.S. Supreme Court's public rights cases would nonetheless permit Congress to assign it to agency adjudication without a jury trial.

Addressing the first prong, the court concluded that the rights the SEC sought to vindicate in its enforcement action arose "at common law" under the Seventh Amendment, and therefore typically require a trial by jury. The court referred to the Supreme Court's decision in *Tull v. United States*, 481 U.S. 412 (1987), in which the Supreme Court held that the right to a jury trial applied to an action brought by an agency seeking civil penalties for violations of the Clean Water Act. The court found this ruling applicable to actions brought by the SEC, which typically seek civil penalties under the securities laws. Thus, the court found that the claims at issue arose at common law under the Seventh Amendment.

With respect to the second prong, the court ruled that action the SEC brought against the petitioners was not the sort that could be properly assigned to agency adjudication under the public rights doctrine. The court noted that common-law courts have heard fraud actions for centuries. The court also stated that securities fraud enforcement actions were typically not suited for agency adjudication because Congress had not explicitly limited the SEC's ability to bring enforcement actions in Article III courts. The court also reasoned that the public rights doctrine did not apply here because fraud claims were "quintessentially about the redress of private harms."

The court determined that the second reason the proceedings were constitutionally defective was that Congress had unconstitutionally delegated legislative power to the SEC when it gave the commission the authority to choose whether to bring enforcement actions in Article III courts or within the agency. The court found that Congress should have, but failed to, provide an intelligible principle by which the SEC would exercise the delegated power so as to avoid violating Article I of the Constitution. The court found that the SEC's ability to choose whether to bring enforcement actions in courts or within the agency is a legislative determination, given prior case law holding that the power to assign disputes to agency adjudication lay uniquely within the legislative branch's authority. The court rejected the SEC's argument that such decisions were prosecutorial in nature, which would have made it an executive, not legislative, function. In so doing, the court reasoned that the power to decide which defendants should receive certain legal processes was a power unique to Congress, not the executive branch.

The third constitutional infirmity the court identified involved the restrictions applicable to removal of ALJs. ALJs are provided two layers of protection: they can only be removed for good cause by a board, whose members, in turn, can only be removed for cause by the president. The court deemed these protections to be unconstitutional and stated that the key question at issue was whether ALJs "serve sufficiently important executive functions, and whether the restrictions on their removal are sufficiently onerous, that the President has lost the ability to take care that the laws are faithfully executed."

The court noted that the Supreme Court in *Lucia v. SEC* held that ALJs were "inferior officers" of an executive agency, at least for the purposes of the appointments clause. In addition, the court noted that the Supreme Court held in *Free Enterprise Fund v. Public Company Accounting Oversight Board*, 561 U.S. 477 (2010), that the president must have adequate control over officers and how they carry out their functions. The court concluded that ALJs, as inferior officers, were "sufficiently important to executing the laws that the Constitution requires that the President be able to exercise authority over their functions." Because the ALJs' statutory removal restrictions were deemed sufficiently onerous to prevent this exercise of authority, the court deemed the restrictions unconstitutional.

Upon finding that the proceedings at issue suffered from these three constitutional defects, the court vacated the SEC's decision and remanded for further proceedings consistent with the court's opinion. Judge W. Eugene Davis filed a dissent disagreeing with the majority's analysis and conclusions. The SEC has filed a request for *en banc* review, which remains pending.

## Securities Fraud Pleading Standards

### Misrepresentations and Omissions

#### Second Circuit Upholds Dismissal of Scheme Liability Claims Based Solely on Misstatements and Omissions

*SEC v. Rio Tinto PLC*, No. 21-2042-cv (2d Cir. July 15, 2022)

The Second Circuit upheld the dismissal of scheme liability claims under Sections 17(a)(1) and 17(a)(3) of the Securities Act, Section 10(b) of the Exchange Act and Rules 10b-5(a) thereunder against a mining company alleging that public statements regarding a 2011 acquisition were misleading because the company was allegedly aware of serious issues with the acquisition before the statements were made. The complaint alleged the company continued to state that the acquisition's earning potential was high after it was clear that transportation issues and lower-than-expected amounts of coal limited potential earnings.

Relying on *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161 (2d Cir. 2005), the district court narrowed the SEC's scheme liability claims to only specific statements, and dismissed the remainder of the scheme liability claims on the ground that they were based solely on purported misrepresentations or omissions. The Second Circuit affirmed, stating that "misstatements and omissions can form part of a scheme liability claim, but an actionable scheme liability claim also requires something *beyond* misstatements and omissions, such as dissemination." In doing so, the Second Circuit reaffirmed its holding in *Lentell* until further guidance from the Supreme Court or *en banc* consideration. The court noted that the SEC's position would undermine key features of Rule 10b-5(b) by expanding primary liability beyond the "maker" of a false statement and allowing for misstatements and omissions to be the basis for liability without applying the heightened pleading standards of the Private Securities Litigation Reform Act, which otherwise governs liability for misstatements and omissions. The court determined that "[m]aintaining distinctions between the subsections of Rule 10b-5 and between the subsections of Section 17(a) is consistent with the text of each" and upheld the dismissal on the grounds that "[w]ere misstatements and omissions alone sufficient to constitute a scheme, the scheme subsections would swallow the misstatement subsections."

#### Ninth Circuit Affirms Dismissal of Putative Securities Fraud Class Action for Failure To Plead Falsity

*Macomb Cnty. Emps.' Ret. Sys. v. Align Tech., Inc.*, No. 21-15823 (9th Cir. July 7, 2022)

The Ninth Circuit affirmed the dismissal of a putative securities fraud class action, holding that six of 12 statements the plaintiffs claimed were misleading were nonactionable puffery, while the other six did not create a false impression and therefore were not misleading.

Align Technology is a medical device manufacturer that sells "Invisalign" aligners that, unlike traditional braces, are see-through, created with digital files and treatment plans, and can be removed for meals and brushing. In this case, the plaintiff, Macomb County Employees' Retirement System, filed a putative securities fraud class action against the company and certain individuals, claiming 12 public statements concerning the company's growth in China were actionable as misrepresentations under Sections 10(b), 20(a) and 20A of the Exchange Act. The complaint alleged that Align experienced significant growth through international sales, including in China from 2013-17. The complaint further alleged that the growth rate fluctuated over the course of 2019, which affected Align's stock price. During that period, according to the pleading, Align executives made 12 allegedly false or misleading statements about (i) China being a "great growth market"; (ii) Align's *ongoing* growth in China; (iii) Align's *past* growth in China; (iv) the effect of an Align competitor's entry into the market; and (v) the way demand for Align's products might decrease due to global economic conditions.

The district court dismissed the action, concluding that the statements were not false or misleading, and were otherwise nonactionable.

On appeal, the Ninth Circuit affirmed. It agreed that broad statements about China being a "great growth market" or a "huge market opportunity" for Align were corporate "puffing," expressing a broad and general optimism rather than a specific, objectively verifiable and testable point of view. This type of statement is not actionable under the securities laws because investors recognize that they are merely statements of optimism and do not use them as a basis for valuing a company. It held that six of the alleged statements all used similarly vague, generally positive terms that do not present the kind of information investors rely on to value corporations. Additionally, the statements were all made at a time when the company's sales *were growing* in China, suggesting they did not create a misleading impression of the state of affairs.

The court also held that the other alleged misstatements were nonactionable because they did not create a false impression of Align's growth in China. Three of the statements contained factual assertions that Macomb's complaint did not contradict. A fourth referred to past growth that the panel held would not give a reasonable investor the impression of a state of affairs differing from reality. A fifth statement assessing the effect of a competitor's entry into the market was simply an optimistic prediction.

As to the final alleged misstatement, Macomb failed to make any arguments on appeal.

### Second Circuit Affirms in Part Claims Against Cannabis Company for Alleged Failure To Disclose SEC Investigation

*Noto v. 22nd Century Grp., Inc.*, No. 21-0347-cv
(2d Cir. May 24, 2022)

The Second Circuit affirmed in part the district court's dismissal of claims under Sections 10(b) and 20(a) of the Exchange Act and Rule 10b-5 thereunder against a company that genetically engineers tobacco and cannabis products. The plaintiffs alleged that the company engaged in an illegal stock promotion scheme in which they paid authors to write promotional articles about the company while hiding the fact that the company paid the authors for the articles, and failed to disclose an SEC investigation about the company's alleged financial control weaknesses.

The Second Circuit rejected the plaintiffs' argument that the company had a duty to disclose that it allegedly paid authors of promotional articles because the company had edited, reviewed and approved the articles, holding that "only an article's maker, not its benefactor, has a duty to disclose that it was paid for." The court found that the plaintiffs alleged that the CEO reviewed and approved the company's press releases, but a "person's preparation of a press release that is then repeated in a separate article by a different author does not qualify that person as the 'maker' of the separate article's statements." The court further found that even if the CEO had provided some input on the articles' content, the complaint did not sufficiently allege that the CEO had ultimate authority necessary to make him the maker of the articles, and it was pure speculation that the company collaborated with the author to the extent that they controlled the articles' publication. Because the plaintiffs failed to adequately allege that the company had a duty to disclose that they paid for the publication, they failed to allege that the existence of a stock promotion scheme constituted an actionable omission.

The Second Circuit determined that the company had a duty to disclose the SEC investigation because the company's statements concerning certain financial control weaknesses were rendered misleading by failing to disclose the pending SEC investigation. The court held that the alleged omission was material because "the fact of the SEC investigation would directly bear on the reasonable investor's assessment of the severity of the reported accounting weaknesses." The court reasoned that the company "specifically noted the deficiencies and that they were working on the problem, and then stated that they had solved the issue," and thus a reasonable investor would have made an overly optimistic assessment of the risk. The court also found that the company's public denial of the SEC investigation further indicated that the nondisclosure was material because otherwise the company would not have tried to hide it.

### First Circuit Affirms Dismissal of Claims Concerning Puerto Rican Government Bonds

*Ponsa-Rabell v. Santander Sec. LLC*, No. 20-1857
(1st Cir. May 20, 2022)

The First Circuit affirmed the dismissal of claims under Section 10(b) of the Exchange Act and Rule 10b-5 thereunder against a bank and its affiliates. The plaintiffs alleged that the bank misled investors into purchasing Puerto Rican municipal bonds and related securities (the PRMB securities) by omitting material information about the state of the market and its own active efforts to rid itself of those securities while selling them to the plaintiffs. The plaintiffs alleged that the PRMB securities were marketed as attractive investments that offered high interest and were exempt from Puerto Rican and federal income and estate taxes, but when Puerto Rico began experiencing an economic recession, there was downward pressure on the PRMB securities. By October 2013, the market for PRMB securities had crashed, resulting in financial losses for those who invested in PRMB securities.

The plaintiffs alleged that two material omissions in a fund prospectus that they contend are actionable. The bank disclosed that "[t]here is no Assurance that a Secondary Market for the Offered Bonds will Develop," and that "the Underwriters are not obligated to do so [meaning to guarantee a secondary market] and any such market making may be discontinued at any time at the sole discretion of the Underwriters" (alterations in original). The plaintiffs allege that the bank should have disclosed that the Puerto Rican bond market was deteriorating and that it was ridding itself of PRMB securities. The First Circuit rejected the plaintiffs' argument that the bank should have disclosed information regarding the deteriorating market conditions, holding that the bank "was simply not under any duty to repeat information already known or readily accessible to investors." The First Circuit reasoned that "it is not a material omission to fail to point out information of which the market is already aware" and added that the "plaintiffs' own complaint points to public statements about the deteriorating economy in Puerto Rico." With respect to the second omissions, the court found that the plaintiffs made no allegations that they had a special relationship or had given any particularized investment instructions to the bank that would support a duty to disclose, and that the plaintiffs merely alleged the bank solicited that they purchase the PRMB securities. The plaintiffs made no allegation that the bank promised to outline the risks of their investment or failed to inform the plaintiffs of a market crash they knew was occurring.

### Ninth Circuit Affirms Dismissal in Anti-Cancer Drug Trial Case

*In re Nektar Therapeutics Sec. Litig.*, No. 21-15170 (9th Cir. May 19, 2022)

The Ninth Circuit affirmed the dismissal of securities fraud claims brought against Nektar Therapeutics and certain of its officers based on allegedly misleading statements about an anti-cancer drug's clinical trial results, holding that the complaint did not adequately allege the statements were false or misleading, or plausibly allege loss causation.

Nektar Therapeutics' anti-cancer drug NKTR-214 is its flagship drug candidate. The drug stimulates the production of cancer-fighting cells. As part of NKTR-214's development, Nektar carried out a Phase 1 clinical trial and reported interim results at various points. Nektar published a chart claiming that the Phase 1 trial had promising results and suggesting that cancer-fighting cells increased by an average of "30-fold" in 10 patients dosed with NKTR-214. A second clinical trial evaluated NKTR-214's effectiveness when dosed alongside another drug, Opdivo, and found that the response rate in treating melanoma declined from the 85% found in November 2017 to 50% in the June 2018 release, a significant drop. When the markets opened two days after this data was released, Nektar's stock price fell about 42%.

In October 2018, two pension funds filed a securities fraud complaint alleging that Nektar made materially misleading statements by touting the "30-fold" chart because it allegedly included outlier data that seriously skewed the results. The pensions relied on (i) an analysis put together by anonymous short-sellers (the Plainview Report) that analyzed the Phase 1 trial data; and (ii) statements by a confidential witness who worked at Nektar. The district court dismissed the complaint, finding that the pensions failed to adequately plead falsity, scienter or loss causation.

The Ninth Circuit affirmed, concluding that the pensions failed to adequately plead falsity or loss causation. The court first rejected the pensions' argument that the statements about the "30-fold" chart's data were misleading because a three-patient subsection of the data indicated only a 1.8-fold increase in cancer-fighting cells. The court pointed out that the pensions did not explain why cherry-picking three patients' data plausibly showed the falsity of Nektar's claims. The court also rejected the pensions' arguments that the confidential witness' criticisms of how the trial reported results proved Nektar's statements were misleading, holding that the witness' "conclusory adjectives" could not meet the heightened pleading standards applied to securities fraud complaints. The court further rejected the pensions' expert's analysis of the results excluding the alleged outlier patient, explaining that the expert made significant, unjustified assumptions in his analysis. The court also noted that the complaint did not explain why the difference in results would have been material to a reasonable investor.

The Ninth Circuit additionally affirmed on the grounds that the complaint failed to plead loss causation. The court concluded that the second trial's results did not reveal the falsity of any statements with respect to the first trial, and instead simply revealed results from a different and more comprehensive test. The short-seller's report, the last remaining piece of evidence in the complaint, was inadequate to show loss causation because the report was written by anonymous and self-interested short-sellers who disavowed any accuracy in their "reporting." As the panel explained, pharmaceutical companies often suffer setbacks in their clinical trials after promising earlier results, and that does not necessarily mean the company committed securities fraud.

### Fourth Circuit Affirms Dismissal of Shareholder Suit Against Hotel Chain Regarding Public Statements on Data Security

*In re Marriott Int'l, Inc.*, No. 21-1802 (4th Cir. 2022)

The Fourth Circuit affirmed the Southern District of Maryland's dismissal of a plaintiff investor's claims against a hotel chain alleging violations of Sections 10(b) and 20(a) of the Exchange Act and SEC Rule 10b-5 thereunder.

The plaintiff in this case, the Construction Laborers Pension Trust for Southern California, brought claims against Marriott International, Inc. and nine of its corporate officers and directors. In 2016, before the lawsuit commenced, Marriott merged with Starwood Hotels and Resorts Worldwide, another hotel company. Marriott later learned that malware had impacted Starwood's guest records, resulting in a data breach. The plaintiff filed a complaint alleging that Marriott failed to disclose vulnerabilities in Starwood's IT systems. The district court dismissed the complaint, holding that the plaintiff failed to adequately allege a false or misleading statement or omission, a strong inference of scienter and loss causation. The plaintiff appealed.

On appeal, the plaintiff argued that Marriott violated the federal securities laws by allegedly making misleading statements or omitting material information about data vulnerabilities from 73 public statements. The statements at issue fell into three categories: (i) statements about the importance of protecting customer data; (ii) privacy statements on Marriott's website; and (iii) cybersecurity-related risk disclosures.

The first set of statements involved the importance of data protection to Marriott's business. For example, in SEC filings Marriott stated that "the integrity and protection of customer, employee, and company data is critical to us as we use such data for business decisions and to maintain operational efficiency." The plaintiff argued that such statements misled investors to believe that Marriott was securing and protecting customer data acquired from Starwood. The court disagreed. It reasoned that the theory behind the plaintiff's suit actually relied on this statement being true, in that data integrity indeed was critically important to Marriott and its investors. This basic truth, the court found, did not "assign a quality to Marriott's cybersecurity that it did not have," which made the statements nonactionable. The court also found that these statements amounted to puffery and thus were not actionable. Finally, the court found that Marriott's SEC submissions also disclosed key risks about its cybersecurity, meaning that a reasonable investor reading these public statements would not have understood Marriot to have overrepresented the extent of its data protection.

The second set of statements involved privacy statements that Marriott posted on various websites. For example, Marriott stated that it sought "to use reasonable organizational, technical and administrative measures to protect" personal data, while noting that "no data transmission or storage system can be guaranteed to be 100% secure." The court determined that these statements were neither false nor misleading, explaining that the plaintiff's own complaint conceded that Marriott took steps to strengthen the security of its systems. Moreover, the court noted that the fact that a security breach took place did not demonstrate that Marriott did not place an emphasis on maintaining data security. Finally, the court found that other privacy statements were accompanied by "sweeping caveats" that would not have misled a reasonable investor.

The third set of statements involved cybersecurity risk disclosures. The plaintiffs argued that Marriot's disclosures warned about events that could occur, despite the fact that the company knew those events had already occurred. To illustrate this point, the plaintiff argued that Marriott issued only a general warning of the possibility that the company would not be able to comply with the requirements of the payment card industry, despite allegedly knowing that Starwood was not compliant with these requirements. The court rejected this argument, concluding that Marriott actually reported that the company's brand standards "did not mandate" compliance with the payment card industry, and did not insinuate that Starwood's systems were in fact compliant. The plaintiff also argued that Marriott warned of a risk of cybersecurity incidents while allegedly having knowledge that a data breach had already occurred. The court rejected this argument as well, concluding that this statement was not actionable because Marriot later updated its disclosure to state that the company had experienced cyberattacks.

The court concluded that Marriott had provided sufficient information to ensure its statements were neither false nor misleading, and affirmed the district court's judgment.

## Scienter

### Second Circuit Upholds Dismissal of Securities Fraud Claims Against Pharmaceutical Company for Failure To Plead Scienter

*Liu v. Intercept Pharms., Inc.*, No. 20-3488-cv (2d Cir. June 16, 2022)

The Second Circuit upheld the dismissal of claims under Section 10(b) of the Exchange Act and Rule 10b-5 thereunder against a pharmaceutical company alleging that the company failed to disclose certain serious adverse events in connection with its liver disease drug. The plaintiffs alleged that the company made false and misleading statements about the safety and tolerability of the drug and its performance in light of serious adverse events that occurred in less than 1% of patients who were taking the drug for the treatment of a rare liver disease and prescribed a higher dose than recommended by the Food and Drug Administration. The district court dismissed the claims for failure to adequately allege scienter.

The Second Circuit affirmed the dismissal, finding that the plaintiffs failed to adequately allege scienter. The court agreed with the district court that the plaintiffs' allegations were speculative because they did not "allege with any specificity at all when the Individual Defendants reviewed internal data, or even should have reviewed internal data, or how that data rendered their public comments about [the drug's] performance false or misleading." The Second Circuit also found that the plaintiffs abandoned their motive and opportunity allegations.

### District of Arizona Grants Motion To Dismiss Securities Fraud Action

*Alpine 4 Holdings Inc. v. Finn Mgmt. GP LLC*, No. CV-21-041494-PHX-SPL (D. Ariz. April 21, 2022)

Judge Steven P. Logan of the U.S. District Court for the District of Arizona granted a motion to dismiss securities fraud and tortious interference with business expectancy claims brought against Grizzly Research, LLC because the complaint failed to allege that (i) Grizzly made its statements with the requisite scienter; (ii) there was a causal connection between the statements and any purchase or sale of securities by the plaintiff; or (iii) the plaintiff suffered economic loss caused by the allegedly false statements.

On March 10, 2021, Grizzly published a report and video about a company called Alpine, in which Grizzly claimed that Alpine had acquired defunct and nonoperating companies and was an investment scam. The report spread quickly on social media. Alpine claimed that the volume of short selling of its stock went up drastically and that its stock price was affected. Alpine sued Grizzly, alleging, among other things, that Grizzly's statements constituted securities fraud. Grizzly moved to dismiss, arguing that the complaint failed to state a claim.

The court agreed, finding that Alpine failed to plead scienter, connection to purchase or sale of a security, or loss causation.

As to scienter, the court concluded that Alpine did not allege sufficient facts to support a strong inference that the statements were made intentionally or with deliberate recklessness. While Alpine pointed in its briefing to a disclaimer on Grizzly's website as proof of intent, the disclaimer was not alleged in the complaint. Rather, the complaint alleged other conclusory assertions of scienter, which are insufficient to satisfy the heightened pleading standard for that element.

The court also found that Alpine failed to plead a causal connection between the alleged misstatements and a relevant securities transaction. The complaint did not allege with any specificity that Grizzly made a purchase or sale of a security. Yet even if it had, that would not have been enough. As the court explained, to state a claim under federal securities law, the *plaintiff* must be the one who purchased or sold securities based on the defendants' statements. Alleging a purchase or sale *by the defendant* does not state a claim. Here, the complaint did not allege any purchase or sale by Alpine.

Finally, the court found that Alpine failed to plead loss causation. The court noted that Alpine's stock price had already lost more than half its value before Grizzly's statements were made. In fact, the stock price stabilized *after* Grizzly's statements, making it impossible to demonstrate that the company's statements caused the economic loss. Nevertheless, the court granted leave to amend, finding that Alpine could still cure the deficiencies outlined in the court's order.

## SLUSA

### Eleventh Circuit Affirms Dismissal of Putative Securities Class Action Under SLUSA

*Cochran v. Penn Mut. Life Ins. Co.*, No. 20-13477 (11th Cir. May 31, 2022)

The Eleventh Circuit affirmed the dismissal of a putative class action asserting claims for breach of fiduciary duties by a brokerage firm for recommending that its customers invest in variable annuities, holding that the plaintiff's claims rested on alleged misrepresentations or omissions of material facts in connection with the purchase or sale of a security, and were therefore barred by the Securities Litigation Uniform Standards Act (SLUSA).

HTK, a wholly owned subsidiary of Penn Mutual Life Insurance Co., offered investors variable annuities, which are tax-advantaged hybrid insurance and investment products. HTK allegedly steered investors toward these products based on their tax-advantaged status. In February 2013, the plaintiff allegedly followed HTK's advice and invested in variable annuities using a tax-advantaged account.

The plaintiff later brought suit against HTK for breach of fiduciary duty, alleging that HTK misled the plaintiff and failed to disclose that (i) the annuities' tax-advantaged status provided the plaintiff with no added tax benefits; and (ii) variable annuities charge higher fees and are more profitable for HTK. The district court dismissed the lawsuit for lack of jurisdiction, concluding that SLUSA barred the plaintiff's claims.

The Eleventh Circuit affirmed. The court held that the complaint alleged misrepresentations or omissions related to the sale of variable annuities (securities) and was therefore barred by SLUSA's prohibition on state law class actions alleging what are actually securities fraud claims. The court noted that the complaint focused on HTK's marketing of variable annuities, which are securities. The court further noted that the complaint focused on recommendations and investment advice, necessarily making either a misrepresentation or an omission an element of the claim. As the court pointed out, if there had been no misrepresentation or omission, HTK would have been doing nothing more than selling the variable annuity, which could not be a breach of fiduciary duty on its own under Georgia law. Since the claim existed only because of alleged misrepresentations and omissions, it was barred by SLUSA.

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