September 2023

Skadden

Inside the Courts

A Quarterly Update From Skadden Securities Litigators

Trends and Filings That Matter

2
Spotlight
Two Sides of the Same Coin: Analyzing the Recent *Ripple* and *Terraform* Decisions

5
Cybersecurity
SEC v. Covington & Burling, LLP (D.D.C. July 24, 2023)

6
Financial Institutions
Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc. (2d Cir. August 10, 2023)
Kirschner v. JPMorgan Chase Bank, N.A. (2d Cir. Aug. 24, 2023)

8
Health Care and Life Sciences
In re Teladoc Health, Inc. Sec. Litig. (S.D.N.Y. July 5, 2023)

9
M&A
Karp v. First Conn. Bancorp, Inc. (4th Cir. June 1, 2023)
In re Columbia Pipeline Grp. Merger Litig. (Del. Ch. June 30, 2023)
City of Dearborn Police & Fire Revised Ret. Sys. v. Brookfield Asset Mgmt. Inc. (Del. Ch. June 9, 2023)

12
Media and Entertainment
Simeone v. Walt Disney Co. (Del. Ch. June 27, 2023)

13
SEC
SEC v. Husain (9th Cir. June 13, 2023)

14
Technology
City of Fort Lauderdale Police & Firefighters' Ret. Sys. v. Pegasystems Inc. (D. Mass. July 24, 2023)

15
Other Notable Cases
City of Warren Police & Fire Ret. Sys. v. Prudential Fin., Inc. (3d Cir. June 13, 2023)
Kessev Tov, LLC v. John Doe(s)
Pajoje Development v. John Doe(s)
(N.D. Ill. July 27, 2023)
Steamship Trade Ass'n of Baltimore-Int'l Longshoreman's Ass'n Pension Fund v. Olo Inc. (S.D.N.Y. July 25, 2023)
Steamfitters Local 449 Pension & Ret. Sec. Funds v. Sleep No. Corp. (D. Minn. July 10, 2023)

© Skadden, Arps, Slate, Meagher & Flom LLP. All rights reserved.

Spotlight

Two Sides of the Same Coin: Analyzing the Recent *Ripple* and *Terraform* Decisions

Contributing Partners

Stuart D. Levi

Alexander C. Drylewski

Daniel Michael

Contributing Associates

Brittany E. Libson

Travis D. Bragg

This article was originally published August 31, 2023, on Reuters Legal News *and* Westlaw Today, *Thomson Reuters businesses.*

Key Points

- In July 2023, Judges Torres and Rakoff in the Southern District of New York issued rulings on whether digital asset sales through trading platforms constitute securities transactions subject to the federal securities laws.
- In *SEC v. Ripple Labs*, Judge Torres held in part that Ripple's sales of XRP to retail purchasers through trading platforms did not constitute securities transactions while its direct sales to institutional purchasers did.
- In *SEC v. Terraform Labs*, Judge Rakoff denied the defendants' motion to dismiss the SEC's claims that they violated federal securities laws in part by selling various digital assets to retail purchasers through trading platforms.
- Although the judges seemingly reached different conclusions on the question of whether sales through trading platforms may constitute securities transactions, the facts and procedural postures of the two cases differ in meaningful ways that may explain the outcomes and shed light on how future courts may approach this issue.

In July 2023, two federal district court judges in the Southern District of New York issued rulings that touched on a crucial question for the digital asset space — whether secondary market digital asset sales through trading platforms constitute securities transactions subject to the federal securities laws.

On July 13, 2023, Judge Analisa Torres issued a summary judgment decision in *SEC v. Ripple Labs, Inc.*, No. 20 Civ. 10832, ECF No. 874 (S.D.N.Y. July 13, 2023), holding in part that Ripple's sales of XRP through trading platforms did not constitute securities transactions while its direct sales to institutional investors did. In contrast, on July 31, 2023, Judge Jed Rakoff rejected Judge Torres' distinction based on how the digital assets were sold in *SEC v. Terraform Labs Pte. Ltd.*, No. 23 Civ. 01346, ECF No. 51 (S.D.N.Y. July 31, 2023), denying defendants' motion to dismiss the Securities and Exchange Commission's claims that they violated federal securities laws in part by selling various digital assets through trading platforms.

Although Judge Torres and Judge Rakoff disagreed on whether sales through trading platforms may constitute securities transactions, the facts and procedural postures of the two cases differ in meaningful ways that may explain the outcomes and shed light on how future courts may view this legal issue.

Background

Ripple develops and manages a digital asset exchange network that operates on the XRP Ledger blockchain. When the XRP Ledger launched, a fixed supply of 100 billion XRP tokens were generated to facilitate international currency transactions. Ripple received 80 billion XRP, some of which it sold and transferred in three ways: (i) directly to counterparties — primarily institutional buyers — pursuant to written contracts ("Institutional Sales"); (ii) on trading platforms through the use of trading algorithms ("Programmatic Sales"); and (iii) to employees and third parties as a form of payment for services ("Other Distributions").

Terraform develops and manages an ecosystem of digital assets and launched the Terra blockchain to record transactions in two of its digital assets, TerraUSD ("UST") and a companion cryptocurrency called "LUNA." UST was developed as an algorithmic stablecoin, which in this case meant its price was algorithmically pegged to another asset, the U.S. dollar. For a while, one UST could be traded for $1.00 of LUNA, and $1.00 of LUNA could be traded for one UST. Owners of UST could also deposit their tokens into a smart contract associated with the "Anchor Protocol" to earn returns Terraform allegedly advertised as 19-20%, to be derived through lending UST deposits to borrowers. Terraform allegedly sold UST, LUNA and three other digital assets — "wLUNA," "mAssets," and "MIR" — directly to institutional investors and through trading platforms to U.S. retail investors.

The SEC brought enforcement actions against Ripple and Terraform (and certain of their executives) in 2018 and 2023, respectively, alleging that the defendants' sales and distributions constituted unregistered sales of securities in violation of Section 5 of the Securities Act of 1933.

Decisions

Under the federal securities laws, investment contracts are a type of security and, therefore, their sale must comply with registration requirements. In *Ripple* and *Terraform*, the parties disputed whether the digital asset sales and distributions were investment contracts.

Both courts relied on the same body of law dealing with investment contracts stemming from and including *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946). To determine whether a transaction is an investment contract, courts assess whether a person (i) invests his money (ii) in a common enterprise and (iii) has a reasonable expectation of profit based on the entrepreneurial and managerial efforts of the promoter. *Howey*, 328 U.S. at 299.

SEC v. Ripple

In an order deciding competing summary judgment motions, Judge Torres analyzed the three categories of transactions in which Ripple engaged and found that only the Institutional Sales were offered and sold as investment contracts.

In assessing the third prong of the *Howey* test for the Institutional Sales, the court found that the institutional investors had a reasonable expectation of profits derived from Ripple's efforts, noting that, "[f]rom Ripple's communications, marketing campaign, and the nature of the Institutional Sales, reasonable investors would understand that Ripple would use the capital received from its Institutional Sales to improve the market for XRP and develop uses for the XRP Ledger, thereby increasing the value of XRP." *Ripple Labs*, ECF No. 874 at 19.

Importantly, the court determined the Programmatic Sales — Ripple's sales on digital asset trading platforms — did not constitute investment contracts because the "expectation of profits" prong of *Howey* was not met. The court noted these sales occurred on secondary trading platforms that match buyers and sellers without disclosing the identity of either. Because the buyers in Programmatic Sales did not know they were buying XRP from Ripple, the court found they did not reasonably expect that Ripple would use their funds to increase the value of XRP. Contrasting these buyers to the purchasers in Institutional Sales, the court also concluded that, due to their lack of sophistication, there was no evidence the buyers in Programmatic Sales had their expectations informed by Ripple's public statements and, therefore, the court did not consider Ripple's statements in its analysis.

On August 18, 2023, the SEC filed a motion to certify an interlocutory appeal of the court's ruling on Programmatic Sales and Other Distributions.

SEC v. Terraform

In deciding the motion to dismiss in *Terraform*, Judge Rakoff was required to accept as true the allegations in the SEC's complaint. At that juncture, the court held that the SEC adequately pled that Terraform's sales of its various digital assets were investment contracts.

When considering the SEC's allegations regarding secondary market sales to retail investors, the *Terraform* court stated that it "reject[ed] the approach recently adopted" by Judge Torres

in *Ripple* and declined to distinguish between the assets sold directly to institutional investors and the assets sold through secondary market transactions to retail investors. *Terraform Labs*, ECF No. 51 at 40. The court explained, "[t]hat a purchaser bought the tokens directly from the defendants or, instead, in a secondary re-sale transaction has no impact on whether a reasonable individual would objectively view the defendants' actions and statements as evincing a promise of profits based on their efforts." In contrast to *Ripple*, the *Terraform* court considered defendants' public statements, accepted as true, including that Terraform and its founder promised all purchasers "rates of returns of 19-20%" and that "sales from purchases of *all* crypto-assets — no matter where the tokens were purchased — would be fed back into the Terraform blockchain and would generate additional profits for *all* crypto-asset holders." The court concluded that these alleged statements gave secondary-market purchasers good reason to believe that Terraform would use their capital contributions to generate profits on their behalf.

Analysis and Implications

The question of whether digital asset sales on trading platforms constitute securities transactions is of central importance to the SEC's broader enforcement initiatives, as the SEC recognized in its August 18, 2023 motion seeking an interlocutory appeal in *Ripple*. While we await further potential guidance from the Second Circuit Court of Appeals, a closer look at the facts in *Ripple* and *Terraform* may provide insights into why the district courts reached seemingly different conclusions.

Although Judge Rakoff stated that he rejected Judge Torres' ruling on Programmatic Sales, that rejection does not appear to have been a total one. Both decisions sought to answer the same two questions. First, can an unsophisticated purchaser have an expectation of profit informed by the promoter's marketing campaign and public statements? And, second, could secondary-market purchasers who buy from unknown sellers reasonably expect profits based on the promoters' use of the money paid by the buyer?

As to the first question, Judge Rakoff, in deciding a motion to dismiss, answered "yes." Judge Torres, in deciding competing motions for summary judgment, ruled that the record demonstrated that Ripple's statements were made across various platforms and were sometimes inconsistent, and thus there was no evidence that an unsophisticated purchaser would have had a reasonable expectation of profit based on this varied collection of statements. On the second question, both judges appear to have aligned on the answer. Given this consistency, the differing results of the two decisions appear to be more driven by important factual distinctions and procedural posture than differing legal analysis.

In answering the second question, Judge Torres ruled that the evidentiary record failed to show that secondary-market purchasers had a reason to believe their sales proceeds would be used by the promoters to generate profits for purchasers because sales on secondary markets are not typically made by the issuer or promoter but rather by unknown third parties. Unlike in *Ripple*, the SEC in *Terraform* alleged that the defendants told all purchasers that funds from *all* digital asset sales — including those on secondary markets — would be fed back into the Terraform ecosystem to generate profits for purchasers. Given this allegation (assumed as true at the pleading stage), Judge Rakoff ruled that "secondary-market purchasers had every bit as good a reason to believe that the defendants would take their capital contributions and use it to generate profits on their behalf." *Terraform Labs*, ECF No. 51 at 42. In *Ripple*, however, even if Judge Torres agreed with Judge Rakoff on the answer to the first question, there was no evidence of a comparable statement being made by the defendants. And, conversely, given Judge Rakoff's heavy reliance on this uncommon allegation, it is not clear he would have reached the same result if that allegation was not made.

Although it was not directly addressed by either decision, it is possible that these factual distinctions would also impact how a court might analyze the "common enterprise" prong of *Howey* when evaluating secondary market sales not made by the issuer. In those circumstances, purchasers' funds would not be pooled and used by the promoters to generate profits, but would go to myriad unknown third parties who would not use the funds to generate profits for the purchasers.

Notably, *Ripple* and *Terraform* are both SEC enforcement actions against digital asset issuers rather than secondary trading platforms. Because those who act as a broker-dealer or an exchange for securities may be required to register with the SEC, the treatment of secondary market sales under the *Howey* test will likely have profound implications for many digital asset trading platforms. Because many (if not most) digital asset issuers do not claim, as was alleged in *Terraform*, that secondary market sales proceeds will be used to generate profits, it is possible that the *Terraform* decision may be limited in future decisions to its unique alleged facts.

Cybersecurity

DC District Court Modifies SEC Subpoena, Limiting Number of Clients Law Firm Must Disclose

SEC v. Covington & Burling, LLP (D.D.C. July 24, 2023)

What to know: The District of Columbia granted in part and denied in part the SEC's motion to compel a law firm to disclose its clients whose files had been compromised by a cyberattack on the firm's information technology systems. The court concluded that the SEC was entitled to only see names of clients whose material nonpublic information was accessed during the cyberattack.

Judge Amit Mehta of the U.S. District Court for the District of Columbia granted in part and denied in part the Securities and Exchange Commission's (SEC's) motion to compel a law firm to disclose its clients whose files had been compromised by a cyberattack on the firm's information technology systems, finding that the SEC was entitled to see only the names of clients whose material nonpublic information was accessed during the cyberattack.

On March 21, 2022, the SEC served a subpoena on Covington & Burling, LLP, a multinational law firm headquartered in Washington, D.C. The subpoena sought information, documents and communications relating to a cyberattack on Covington's information technology systems that occurred in 2020. Covington largely complied with the subpoena, but objected to disclosing the names of its nearly 300 public company clients whose files had been compromised by the attack on the grounds of attorney-client privilege and Fourth Amendment protection. The SEC moved to compel disclosure of those client names.

The court granted in part and denied in part the SEC's motion to compel. It found that the attorney-client privilege did not cover communications identifying Covington's clients. The court stated that "Covington's disclosure of a client name would tell the SEC nothing about what, if any, legal advice the client sought, or how the firm responded, with respect to the cyberattack." The court also held that the SEC's demand for the names of affected clients did not exceed its statutory authority or violate the constitution. However, the court found that the SEC did not show that it needed the names of the 291 clients whose material nonpublic information was not accessed. The SEC admitted that those clients were not relevant to its investigation. Accordingly, the court modified the subpoena by ordering Covington to produce the names of the clients as to whom it has not been able to rule out that a threat actor accessed material nonpublic information.

Financial Institutions

Second Circuit Reverses Decision Certifying Class Action Against Major Financial Institution

Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc. (2d Cir. August 10, 2023)

What to know: The Second Circuit reversed a decision to certify a class action against a major financial institution in connection with alleged misstatements about the company's business principles and conflict of interest practices.

The Second Circuit reversed a district court's decision certifying a class action under Section 10(b) of the Exchange Act against a large financial institution, finding that the company adequately rebutted the legal presumption of reliance under *Basic Inc. v. Levinson*. Under *Basic*, plaintiffs can use a fraud-on-the-market presumption of classwide reliance for purposes of class certification, and defendants can rebut that presumption by showing a lack of price impact. The plaintiffs alleged that the financial company made allegedly misleading statements regarding its business principles and conflicts management. In particular, the plaintiffs alleged that generic statements such as "integrity and honesty are at the heart of our business" and that the company had "extensive procedures and controls that are designed to identify and address conflicts of interest" were misleading in light of allegedly undisclosed conflicts. The plaintiffs maintained that these alleged misstatements artificially maintained an inflated stock price that dropped after the disclosure of the alleged undisclosed conflicts.

The Second Circuit relied on the Supreme Court's decision in earlier proceedings in *Goldman Sachs Group, Inc. v. Arkansas Teacher Retirement System* to hold that the company had successfully rebutted the *Basic* presumption of reliance by showing that the alleged misrepresentations did not impact the price of the company's stock. The Second Circuit explained that, under *Goldman*, courts are required to compare, at the class certification stage, the relative genericness of a misrepresentation with its corrective disclosure. As the Supreme Court stated in *Goldman*, the "generic nature of a misrepresentation often will be important evidence of a lack of price impact, particularly in cases proceeding under the inflation-maintenance theory" because "the inference — that the back-end price drop equals front-end inflation — starts to break down when there is a mismatch between the contents of the misrepresentation and the corrective disclosure."

In applying the *Goldman* standard, the Second Circuit determined that none of the alleged corrective disclosures matched the company's generic statements about business principles and conflicts of interest. The Second Circuit reasoned that the district court had acknowledged a "considerable gap in specificity between the corrective disclosures and alleged misrepresentations," but failed to follow *Goldman*'s guidance by reasoning that investors would have relied on more specific statements concerning the details and severity of the company's alleged misconduct. The Second Circuit found that to be an error because the district court substituted the details and severity of the misconduct in place of the challenged generic statements, which undermined an inference that a back-end price drop equaled the alleged front-end inflation. The Second Circuit determined that there was an insufficient link between the corrective disclosures and the alleged misrepresentation to make such a conclusion.

The Second Circuit further explained that going forward, courts must conduct a "searching price impact analysis" where "there is a considerable gap in front-end-back-end genericness" and the corrective disclosures do not directly refer to the alleged misstatements. Where such a gap exists, courts should consider whether a truthful but equally generic substitute for the alleged misrepresentation would have affected the stock price.

Second Circuit Holds Certain Syndicated Commercial Term Loans Are Not Securities Under Federal Laws

Kirschner v. JPMorgan Chase Bank, N.A. (2d Cir. Aug. 24, 2023)

What to know: The Second Circuit affirmed the dismissal of certain state law securities claims against various financial institutions in connection with the issuance of certain syndicated term loans, holding that the plaintiffs failed to plausibly allege that the loans were securities under *Reves*.

The Second Circuit affirmed the dismissal of certain state law securities claims against various financial institutions in connection with the issuance of certain syndicated term loans (the Notes), holding that the plaintiffs failed to plausibly allege that the loans were securities under *Reves v. Ernst & Young*, which governs whether notes are securities under the Securities Exchange Act of 1934 (Exchange Act) and the Securities Act of 1933 (Securities Act). Under *Reves*, notes issued in the investment context are securities, but notes issued in a commercial or consumer context are not.

The Second Circuit held that, based on the four *Reves* factors, the Notes at issue were not securities and instead resembled loans issued by banks for commercial purposes. The four *Reves* factors are (i) "the motivations that would prompt a reasonable seller and buyer to enter into" the transaction, (ii) "the plan of distribution of the instrument," (iii) "the reasonable expectations of the investing public" and (iv) "whether some factor such as the existence of another regulatory scheme significantly reduces the risk of the instrument, thereby rendering application of the Securities Act unnecessary."

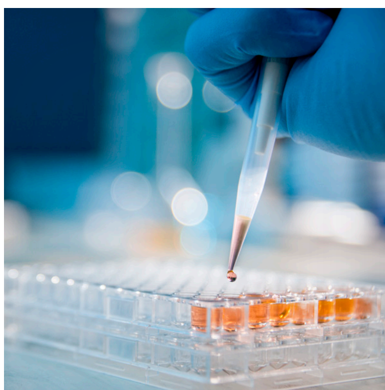
The court first reasoned that the alleged facts suggested that the motivations of the parties to the Notes were mixed, and therefore the first factor leaned in favor of finding the Notes to be securities. The lenders were motivated by the expected profits they would receive from their purchase of the Notes in the form of quarterly interest payments. The company who issued the Notes was not motivated by investment because it was using the funds to primarily pay debt and expenses.

The court next reasoned that the alleged facts did not plausibly suggest that the Notes were offered and sold broadly to the public for speculation or investment, but rather were only offered to limited, sophisticated institutional entities. The fact that the Notes were available on a secondary market did not affect this conclusion because the Notes were subject to certain assignment restrictions that largely prevented them from being broadly sold to the general public.

The court then reasoned that the alleged facts did not plausibly suggest that the lenders perceived the Notes as securities, as they were given clear notice that the Notes were loans and not investments in a business enterprise, and the lenders had certified that they had independently conducted due diligence before deciding to participate in the loan syndication. Isolated references of "investors" in the loan documents alone could not have plausibly created the reasonable expectation that the buyers were investing in securities.

Finally, the court reasoned that the alleged facts did not plausibly suggest that application of the securities laws was necessary. The Notes were secured by the company's collateral, which reduced the risk associated with the Notes. In addition, federal regulators had issued specific policy guidelines addressing syndicated loans, which further reduced the risk of the Notes.

Health Care and Life Sciences



SDNY Dismisses Claims Alleging Health Care Company, Officers Made False and Misleading Statements Following Merger

In re Teladoc Health, Inc. Sec. Litig. (S.D.N.Y. July 5, 2023)

What to know: The Southern District of New York dismissed securities fraud claims against a virtual health care company and five of its officers, holding that the company's statements about its merger with a virtual chronic disease management provider were statements of nonactionable corporate optimism.

Judge Denise Cote of the U.S. District Court for the Southern District of New York dismissed a putative class action against a virtual health care company and certain of its officers under Sections 10(b) and 20(a) of the Exchange Act, and Rule 10b-5 thereunder. The complaint alleged that the defendants made misleading statements following a merger with a virtual chronic disease management provider to inflate the defendants' stock price.

The court found that the plaintiffs failed to adequately allege that the challenged statements were false and materially misleading. It concluded that the statements regarding the company's post-merger integration of the virtual chronic disease management company were "largely non-actionable statements of opinion and/or expressions of corporate optimism." For example, the court noted that although the defendants stated that the companies were "fully integrated" and allegations attributed to one of the plaintiffs' confidential witnesses were to the contrary, "[t]his difference of opinion is insufficient to plead a claim of falsity."

The court also rejected the plaintiffs' argument that the company's "general statements of optimism about the integration of the two companies" were "actionable because they created the false impression that the integration 'was completed or progressing successfully.'" The court noted that a reasonable investor could not have been misled in light of the company's "contemporaneous robust disclosures of the challenges and risks it was facing." The court further determined that the company's contemporaneous disclosures "made clear to any reasonable investor that the integration process was complex and that different components of the integration effort might progress at different rates."

M&A

Fourth Circuit Affirms Summary Judgment in Favor of Corporation and Directors on Materiality and Loss Causation

Karp v. First Conn. Bancorp, Inc. (4th Cir. June 1, 2023)

What to know: The Fourth Circuit affirmed summary judgment in favor of a bank holding company and its individual directors in a suit alleging they misled shareholders by issuing a misleading proxy statement in connection with the bank's merger.

The Fourth Circuit affirmed summary judgment in favor of First Connecticut Bancorp., Inc. and its individual directors in a suit alleging that they misled shareholders by issuing a misleading proxy statement in connection with the bank's merger with People's United Financial, Inc. The court determined, among other things, that (i) the plaintiff had not identified material omissions in the proxy statement, (ii) the challenged disclosures in the proxy statement had not caused the plaintiff's alleged losses and (iii) the defendants had not acted negligently in issuing the proxy statement.

The suit alleged that in 2017, First Connecticut's financial advisor, Piper Jaffray & Co., presented a set of cash-flow projections to the board regarding a prospective merger with People's United. However, when First Connecticut and People's United proposed the merger in question to their shareholders in June 2018, the proxy statement did not include the 2017 projections — instead, it provided a less optimistic discounted cash flow analysis, leading shareholders to "undervalue their shares and approve the merger."

Selwyn Karp, a First Connecticut shareholder, asserted, among other arguments, that First Connecticut and its directors violated Section 14(a) of the Exchange Act, and SEC Rule 14a-9 thereunder, by not including in the proxy statement the cash-flow figures that Piper used in its analysis, leading shareholders to undervalue their shares and approve the 2018 merger at an unfairly low price. The U.S. District Court for the District of Maryland granted First Connecticut's motion for summary judgment, holding that Mr. Karp failed to show that (i) the cash-flow projections were material, (ii) their omission caused him any economic loss or (iii) the directors acted negligently in approving the proxy statement.

The Fourth Circuit affirmed. The panel held that as long as the merger proxy gave "a thorough and accurate summary" of the financial advisor's work, it was not sufficient to speculate that shareholders might have found different projections helpful to their deliberations. The panel found that the proxy statement "contained a bevy of information," and "[g]iven the array of metrics in the proxy statement, [the court found] it unlikely that the [2017] cash-flow projections would have 'significantly altered the total mix of information,'" rendering the alleged omission of the cash flow projections immaterial.

Further, even if the proxy statement was considered misleading, the panel held that First Connecticut would still be entitled to summary judgment because there was no genuine issue of material fact that the omission of the 2017 cash-flow projections caused shareholder losses. Specifically, the panel found that it was speculative as to whether inclusion of the 2017 projections would have led shareholders to reject the proposed merger, much less obtain more value for their shares. Finally, the panel affirmed the district court's determination that Mr. Karp failed to establish that First Connecticut or any of the directors acted negligently in issuing the proxy statement.

Court of Chancery Holds Officers and Acquirer Liable in Deal Litigation, Sets Rebuttable Presumption of Reliance for Disclosure Claims When Requesting Stockholder Action

In re Columbia Pipeline Grp. Merger Litig. (Del. Ch. June 30, 2023)

What to know: The Court of Chancery found two energy company executives breached their duties of loyalty by favoring a bidder during their company's sale process. The court also held the bidder, and ultimate buyer, liable for aiding and abetting the executives' breaches of fiduciary duty.

The Delaware Court of Chancery found Columbia Pipeline Group (CPG) chairman and CEO Robert Skaggs, Jr. and executive vice president and CFO Stephen Smith breached their duties of loyalty by favoring TC Energy Corp. (TransCanada), CPG's ultimate buyer, during CPG's sale process. The court also held TransCanada liable for aiding and abetting the executives' breaches of fiduciary duty.

The Delaware Court of Chancery found, after trial, that Mr. Skaggs and Mr. Smith were officers of NiSource Inc. With their sights set on retiring near-term and earning change-in-control benefits upon a sale, Mr. Skaggs and Mr. Smith helped to orchestrate a sale of CPG shortly after it became an independent publicly traded entity.

During the sale process, the officers' "ardor for a transaction" was on full display, and Mr. Skaggs and Mr. Smith "showed extraordinary solicitude" toward the ultimate buyer, TransCanada. The court found that Mr. Skaggs and Mr. Smith demonstrated their TransCanada favoritism by, among other things, ignoring TransCanada's breaches of its standstill agreement and disclosing to TransCanada critical sell-side information about the sale process. TransCanada ultimately used this information to "re-trade" on an all-cash deal at $26 per share, and the "haphazard sale process" concluded with the CPG board's acceptance of TransCanada's revised cash-and-stock offer valued at the signing at $25.50 per share.

The plaintiffs filed suit, alleging that Mr. Skaggs and Mr. Smith breached their fiduciary duties as CPG officers by conducting an unreasonable sales process under a conflict of interest and by authorizing a false and misleading proxy statement. The plaintiffs also alleged that TransCanada aided and abetted the actionable breaches of duty by Mr. Skaggs and Mr. Smith, as well as exculpated breaches of the duty of care by the CPG board. Mr. Skaggs and Mr. Smith settled, and trial proceeded only against TransCanada.

Because the claim for aiding and abetting against TransCanada depended on an underlying breach of fiduciary duty, the court analyzed the conduct of Mr. Skaggs, Mr. Smith and the CPG board during the sale process. The court found that Mr. Skaggs and Mr. Smith "acted like executives who were thirsty for a sale," and that the plaintiffs proved that they had "breached their fiduciary duties as officers during the sale process because they pursued a transaction that would enable them to retire in 2016 with their full change-in-control benefits and, under the influence of that conflict of interest, took actions that fell outside the range of reasonableness."

For the outside directors, the court indicated that the conduct required to find a breach of the duty of care varied depending on the standard of review applied by the court. Where, as here, the transaction was subject to enhanced scrutiny under *Revlon*, the court only needed to find that the directors' actions fell "outside the range of reasonableness." The court found that the outside directors' failure to monitor Mr. Skaggs and Mr. Smith more closely in the face of warning signs about their interactions with TransCanada fell outside the range of reasonableness, resulting in a breach of the duty of care. However, monetary liability could not attach to the directors themselves because the court found that their actions did not rise to the level of gross negligence. Nevertheless, the underlying breach was a sufficient predicate for an aiding and abetting claim.

With respect to the plaintiffs' claim for aiding and abetting the sale process breaches, the court found that TransCanada had "constructive knowledge" that Mr. Skaggs and Mr. Smith were breaching their duty of loyalty, and that the outside directors of CPG were breaching their duty of care by failing to adequately oversee them. The court found that TransCanada exploited these breaches through its "persistent and opportunistic violations of the [s]tandstill" and capitalized on its ability to co-opt Mr. Smith based on his longstanding relationship with TransCanada's dealmaker and his own position as "a neophyte dealmaker on his first and only assignment." These actions, coupled with TransCanada's reneging on an oral agreement for $26 per share and threatening to publicly disclose that deal talks had ended if CPG did not accept a new offer of $25.50 within 72 hours, "crossed the line" from hard-nosed bargaining to exploitation. The court awarded $1 per share in damages — representing the difference between the $26 all-cash offer and the $25.50 mixed cash/stock offer that was ultimately accepted — after accounting for the rise in TransCanada's stock between signing and closing.

The court also found that Mr. Skaggs and Mr. Smith had breached their duty of loyalty, and the outside directors had breached their duty of care, because the proxy statement issued in connection with the acquisition was materially misleading in

describing the sale process. The court found TransCanada liable for aiding and abetting these breaches because the company knew that the proxy statement omitted material information about its contacts with CPG management and chose not to correct the material misstatements despite an obligation under the merger agreement to do so.

When addressing issues of reliance on the disclosures to establish damages for the disclosure-related breach of duty, the court articulated a new "rule of law": "If corporate fiduciaries [1] distribute a disclosure document, [2] to diffuse stockholders, [3] in connection with a request for stockholder action, and [4] the disclosure document contains a material misstatement or omission, then there is a presumption that the stockholders relied on the disclosures such that individualized proof of reliance is not required." The court said that such a presumption would have been "outcome-determinative" in this case, but the court did not apply it here because the parties had not litigated the case with the knowledge that this presumption would apply. Because the presumption did not apply here, the court denied the plaintiffs' request for rescissory damages. The court awarded $0.50 per share damages for the disclosure breach, but those damages overlapped with the $1 per share awarded for the sale process breaches.

Court of Chancery Rejects Stockholder Challenge to Controller Squeeze-Out Transaction

City of Dearborn Police & Fire Revised Ret. Sys. v. Brookfield Asset Mgmt. Inc. (Del. Ch. June 9, 2023)

What to know: The Court of Chancery rejected plaintiff stockholders' allegations that a software company's directors and controlling stockholder breached their fiduciary duties in the controller's acquisition of all of the software company's outstanding shares.

The Delaware Court of Chancery rejected plaintiff stockholders' allegations that Brookfield Asset Management, Inc., a controlling stockholder of TerraForm Power, Inc., and Terraform's directors breached their fiduciary duties in connection with Brookfield's acquisition of all of Terraform's outstanding shares. Brookfield conditioned its proposal to acquire Terraform on the approval of an independent board committee and a majority of the non-Brookfield-affiliated stockholders. Upon receipt of the proposal, the board established a special committee consisting of the company's three independent directors.

The plaintiffs sued, alleging that certain Terraform directors and Brookfield breached their fiduciary duties in connection with the acquisition. The defendants moved to dismiss, arguing that the business judgment rule applied under Delaware's *MFW* doctrine. The plaintiffs argued that *MFW* did not apply because (i) the special committee was not fully empowered, (ii) the special committee did not meet its duty of care and (iii) the stockholder vote was not fully informed.

After oral argument, the court dismissed the case, rejecting the plaintiffs' following allegations:

- The plaintiffs argued that the special committee was coerced and not able to "say no definitively" because a financial model Brookfield provided during diligence that "did not include growth for TerraForm" was an "implicit threat" that Brookfield would let Terraform "wither on the vine" if the special committee said no. The court rejected this argument as an "unreasonable inference[]."
- The plaintiffs argued that the special committee failed to meet its duty of care by (i) failing to conduct a market check, (ii) selecting conflicted advisers and failing to manage those conflicts and (iii) assigning *de minimis* value to pending derivative claims that would be extinguished as a result of the transaction.

  The court held that "[a] failure to conduct a presigning market check is not a *per se* violation of the duty of care." While the court did not "love the … level of financial ties" between the special committee's advisers and Brookfield, those ties were not enough to state a claim for breach of fiduciary duty. Finally, the court found no breach by the special committee in holding only one 35-minute meeting to consider the value of a pending derivative litigation because the committee members were not named as defendants, received advice on the value of the litigation and were already familiar with its facts.
- The court rejected most of the plaintiffs' disclosure claims due to their overlap with the rejected duty of care allegations. It also rejected the plaintiffs' claims that the proxy failed to disclose nonratable benefits Brookfield received from the acquisition and the likely dilutive effect of the merger on dividend yields for TerraForm, finding that the disclosures surrounding this information were adequate.

Media and Entertainment

Court of Chancery Rejects Stockholder Books and Records Demand Related to Company Opposition to Florida House Bill 1557

Simeone v. Walt Disney Co. (Del. Ch. June 27, 2023)

What to know: The Delaware Court of Chancery held that a stockholder was not entitled to further inspection of a multinational media and entertainment conglomerate's books and records related to the company's opposition to Florida House Bill 1557. The stockholder's disagreement with the company's business decision did not provide a credible basis to suspect wrongdoing or entitle the stockholder to inspect the company's books and records.

The Delaware Court of Chancery held that a stockholder of The Walt Disney Company was not entitled to inspect additional books and records of Disney related to its board's decision to have the company publicly oppose Florida House Bill 1557. Disney had produced certain board minutes and corporate policies in response to the stockholder's demand letter seeking to inspect Disney's records, despite maintaining that the stockholder had not stated a proper purpose under Delaware law to review them. The stockholder sued when Disney would not provide additional records, asking the court to order Disney to produce records that included emails going back three years.

The Court of Chancery rejected the stockholder's claim for three reasons. First, the court found that the demand's stated purposes belonged to the stockholder's counsel, not the stockholder himself. The court found that (i) the stockholder was "solicited by counsel" to serve the demand letter seeking records, (ii) the stockholder's litigation fees were being advanced by a third party, (iii) the stockholder did not recall reading the demand letter before it was sent and (iv) the purpose expressed by the stockholder at his deposition differed from the purpose articulated in the demand letter. The court stated that a lawsuit seeking books and records must be "designed to address the plaintiff's interest as a stockholder" and "not a vehicle to advance" counsel's, or a financial backer's, interests.

Second, the demand's stated purposes, all of which involved potential wrongdoing related to the Disney board's decision to publicly oppose the bill, were not proper because they offered no credible basis to suspect wrongdoing. The court stated that "Delaware law vests directors with significant discretion to guide corporate strategy — including on social and political issues." The court found that the stockholder was critiquing a business decision by Disney's board and nothing more, which is not enough to demonstrate a credible basis to suspect wrongdoing by the directors.

Finally, even if the stockholder had stated a proper purpose, the court held that the stockholder was not entitled to additional documents because Disney had already produced all of the necessary and essential information, including the "formal Board documents" on the bill's consideration and any potential ramifications. The court concluded that the stockholder's demand of nearly three years of emails and other records was '"vastly overbroad,"' especially since the bill was introduced in 2022.

SEC

Ninth Circuit Clarifies Summary Judgment Burden for Civil Penalties in SEC Enforcement Action

SEC v. Husain (9th Cir. June 13, 2023)

What to know: The Ninth Circuit reversed a lower court's imposition of a civil penalty on summary judgment against an alleged stock promoter, holding that there were genuine disputes of material fact as to the proper amount of the penalty.

The Ninth Circuit reversed a district court's grant of summary judgment in a civil enforcement action accusing entrepreneur Imran Husain and his attorney, Gregg Evan Jaclin, of making false and misleading statements regarding various shell companies they created and sold.

The SEC brought the civil enforcement action against Mr. Husain and Mr. Jaclin in 2016 and moved for summary judgment, seeking to impose a $1.76 million penalty on Mr. Husain under the theory that those were the funds Mr. Husain received in connection with his scheme.

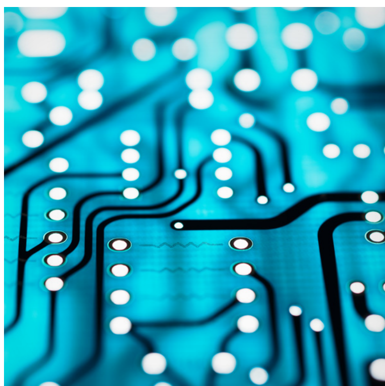
The district court granted the motion, but the Ninth Circuit reversed. The panel held that the district court erred in granting summary judgment in two ways.

First, while the district court found that it was undisputed that Mr. Husain had received $1.76 million in connection with his scheme, the Ninth Circuit held that there was a dispute of fact as to whether he actually received that amount. Specifically, the panel focused on Mr. Husain's declaration, which it found created a genuine issue of material fact as to whether Mr. Husain received $287,500 of the alleged gross pecuniary gain or whether those funds had been paid or diverted elsewhere.

Second, the Ninth Circuit held that the district court misapplied the so-called *Murphy* factors, a four-factor test used to determine the amount of a civil penalty "in light of the facts and circumstances" presented by the case. Under the *Murphy* factors, courts evaluate whether the defendant (i) acted with a high degree of scienter, (ii) engaged in a repeated pattern of wrongdoing, (iii) failed to recognize the wrongful nature of his conduct and (iv) only ceased wrongdoing upon being caught. Here, the district court found that the factors justified imposing the penalty's full allowable amount.

The Ninth Circuit disagreed with the district court's analysis as to two of the factors — the first and fourth — holding that material disputes of fact precluded summary judgment. Specifically, the panel concluded that Mr. Husain's actions may not have supported imposing the full penalty because (i) Mr. Husain introduced evidence that he lacked the requisite scienter because he simply followed his attorney's advice on certain alleged violations and (ii) Mr. Husain's signed declaration raised a dispute of fact as to the fourth factor because it evidenced remorse for his actions.

Technology



District of Massachusetts Denies in Part Motion To Dismiss Claims Alleging Code of Conduct Compliance Misstatements in Trade Secret Case

City of Fort Lauderdale Police & Firefighters' Ret. Sys. v. Pegasystems Inc.
(D. Mass. July 24, 2023)

What to know: The District of Massachusetts denied in part a motion to dismiss securities fraud claims against a software company based on alleged misstatements regarding the company's compliance with its code of conduct following a damages award in a separate civil trade secret lawsuit, in which the company was found to have engaged in unlawful corporate espionage against a competitor.

Judge William G. Young of the District of Massachusetts denied in part a motion to dismiss investors' claims against a software company alleging violations of Sections 10(b) and 20(a) of the Exchange Act based on alleged misstatements about a trade secret lawsuit filed against the company by a competitor. That lawsuit resulted in a damages award of more than $2 billion after the court found that the company willfully and maliciously misappropriated trade secrets. The plaintiffs alleged that the defendants' statements that the claims in the trade secret lawsuit were "without merit" were misleading, and that statements in the company's code of conduct regarding not engaging in misappropriation activity were also false and misleading. In its SEC disclosures, the company had stated that the trade secret lawsuit was "without merit," that it had "strong defenses" and that "any alleged damages claimed by [the competitor] are not supported by the necessary legal standard."

The court rejected the company's argument that the plaintiffs had not adequately pled false or misleading statements or a strong inference of scienter. It reasoned that the company's code of conduct, which stated that the company would "[n]ever use illegal or questionable means to acquire a competitor's trade secrets," was objectively false in light of the $2 billion damages verdict in the trade secrets case and based on the finding that the company's espionage activity was directed by senior executives. The court further reasoned that the statement in the company's disclosures that the trade secret lawsuit was "without merit" was sufficiently alleged as misleading because the CEO was allegedly aware of and directed the company's trade secret misappropriation, and "a reasonable investor could justifiably have understood [the CEO's] message that [the] claims were 'without merit' as a denial of the facts underlying [the] claims — as opposed to a mere statement that [the company] had legal defenses against those claims." The court reasoned that, while the company may have believed it had viable defenses to the claims, "an issuer may not ... make misleading substantive declarations regarding its beliefs about the merits of the litigation."

The court also held that the plaintiffs alleged a strong inference of scienter. It found that the complaint sufficiently alleged a detailed scheme to misappropriate trade secrets and that the CEO was aware of and personally involved in the scheme. The court, however, held that the scienter allegations against the CFO were insufficient — allegations that a senior executive "must have known" about the alleged fraud based on the person's status at the company are uniformly rejected.

Other Notable Cases

Third Circuit Vacates Dismissal of Section 10(b) Claim Predicated on Confidential Witness Allegations

City of Warren Police & Fire Ret. Sys. v. Prudential Fin., Inc. (3d Cir. June 13, 2023)

What to know: The Third Circuit vacated in part the dismissal of claims brought under Section 10(b) of the Exchange Act, holding that investors plausibly alleged that statements by an insurance company's CFO regarding the purported stability of the company's reserves were false or misleading at the time they were made.

The Third Circuit vacated in part the dismissal of claims alleging Prudential Financial, Inc.'s CFO made false and misleading statements about the company's reserve increases based on updated mortality rate assumptions.

In January 2013, Prudential paid $615 million to acquire 700,000 life insurance policies that were underwritten by *Fortune 500* insurance and investment company The Hartford. These policies, referred to as the "Hartford Block," were cashed out sooner than anticipated because the policyholders were not living as long as predicted.

In mid-2018, Prudential announced a $65 million reserve increase, which it attributed in part to its updated mortality rate assumptions from the Hartford Block. Over the next six months, the company made various statements to investors assuring them that there were no problems with the company's reserves. The last such statement came in June 2019, when Prudential's CFO stated that the company's recent numbers with respect to its mortality expectations were "in between [the] range of what we'd expect[,] normal volatility, but net it has been below our experience" and "very quarter-to-quarter, both positive and negative," or, at worst, only "slightly negative." Just two months later, however, Prudential issued a press release announcing a $208 million increase in reserves, which the company attributed to its mortality rates. Prudential also disclosed that its life insurance earnings would be reduced by "about $25 million a quarter ... for the foreseeable future." The company's common stock dropped 13% after this announcement.

Shareholders filed suit under Section 10(b) of the Exchange Act, alleging in part that the CFO's statements were false or misleading because he must have known in June 2019 that the company's reserve situation was not in a normal range given the size of the increase in reserves the company had to book just two months later.

The district court dismissed the claims, but the Third Circuit vacated the dismissal with respect to the CFO's statements in particular. Citing allegations from a confidential witness claiming to be a former employee, the court held that the plaintiffs plausibly alleged that Prudential's CFO knew that the company's reserves would need to be significantly increased at the time he stated — during a conference call with investors — that Prudential's rates were within the range of "normal volatility" or, at worst, "slightly negative." The court reasoned that the timing of the CFO's statements and their temporal proximity to the later reserve increase supported an inference that the executive knew the company's rates could not have been within a normal or slightly negative range at the time of the conference call.

Northern District of Illinois Denies in Part Motion To Dismiss Securities Fraud Action Over Alleged Market Manipulation

Kessev Tov, LLC v. John Doe(s)
Pajoje Development v. John Doe(s)
(N.D. Ill. July 27, 2023)

What to know: The Northern District of Illinois granted in part and denied in part a motion to dismiss securities fraud claims against Chicago Board Options Exchange market participants for artificially inflating the price of put options during a stock market "flash crash" in August 2015.

Judge LaShonda A. Hunt of the U.S. District Court for the Northern District of Illinois granted in part and denied in part a motion to dismiss securities fraud claims against Chicago Board Options Exchange market participants for artificially inflating the price of put options during a stock market "flash crash" in August 2015. The plaintiff hedge funds alleged that the defendants engaged in market manipulation in violation of Section 10(b) of the Exchange Act and Section 12 of the Illinois Securities Law of 1953 (ISL). The defendants moved to dismiss, and the court granted the motion as to the plaintiffs' ISL claim and denied the motion as to the plaintiffs' Exchange Act claim.

On August 24, 2015, the stock market opened down sharply in a "flash crash." That morning, many S&P 500 index stock options had no bid or ask information for approximately the first twenty minutes of trading. The plaintiffs alleged that the defendants took advantage of this vacuum by simultaneously placing bids and asks that they never intended to execute and cancelling them within milliseconds, thus artificially inflating the market price of the relevant index options. The defendants' "spoofing," according to the plaintiffs, created a false market midpoint for the index options, and the plaintiffs alleged that they lost millions of dollars because the defendants' actions caused them to close out their positions at these artificially inflated market midpoints.

In June 2022, the court granted the defendants' motion to dismiss the original complaint without prejudice, finding that the plaintiffs failed to explain (i) how the cancelled orders demonstrated a plan to deceive and (ii) how the midpoint prices resulting from the defendants' actions were fundamentally irrational in a period of extreme market volatility. The plaintiffs then filed an amended complaint, supplementing their allegations with charts, tables and a declaration from a market-making expert who applied option theory and analyzed bidding data to show that the defendants' bids were irrational. The defendants again moved to dismiss, arguing that the plaintiffs failed to state a claim under the Exchange Act or ISL, and in the alternative, that the ISL claim must be dismissed because the plaintiffs failed to allege a remedy available under the ISL.

The court denied the defendants' motion to dismiss the Exchange Act claim, finding that the plaintiffs' exhibits plausibly suggested that the defendants' actions were irrational, and thus the complaint adequately alleged manipulative acts. The court then rejected the defendants' argument that the plaintiffs needed to point to specific orders that the defendants executed and profited from, holding that due to the obstacles posed by the defendants' anonymity, the plaintiffs did not need to meet such a high burden of proof at the pleading stage. The court also found that the plaintiffs adequately pled scienter via an intent to manipulate the market. Finally, the court held that the plaintiffs sufficiently pled loss causation by alleging that (i) the defendants' conduct created higher prices, (ii) the plaintiffs were forced to close their positions shortly thereafter and (iii) prices for options dropped once the spoofing bids were no longer the predominant bids on the market.

The court agreed with the defendants' argument that the plaintiffs failed to allege a remedy under the ISL and granted the motion to dismiss that claim.

SDNY Denies Dismissal of Claims Alleging Food Ordering Company Made Misleading Statements About Restaurant Locations on Platform

Steamship Trade Ass'n of Baltimore-Int'l Longshoreman's Ass'n Pension Fund v. Olo Inc. (S.D.N.Y. July 25, 2023)

What to know: The Southern District of New York denied a motion to dismiss securities fraud claims against a food ordering company based on allegedly misleading statements about the number of restaurant locations using the company's platform, holding that the complaint adequately alleged that the statements were false or misleading.

Judge Jed S. Rakoff of the U.S. District Court for the Southern District of New York denied a restaurant management software company's motion to dismiss claims alleging that it violated Sections 10(b) and 20(a) of the Exchange Act by making misstatements about its relationship with a large customer and the number of active restaurant locations using its software. The court found that the plaintiff did not adequately allege that the company made a material omission by failing to disclose the termination of a relationship with one of its major customers because the company's disclosures concerning future revenue

projections associated with that customer contained adequate forward-looking disclaimers to afford safe harbor protections.

However, the court found that the plaintiffs adequately alleged falsity concerning statements about the number of individual restaurant locations actively using the company's software. The court rejected the company's argument that the alleged 2% inflation of customers using the software was not material. The court determined that a reasonable investor could have relied on the inflated number of customers — in this case, thousands of locations — in deciding whether to transact in the company's stock. It also reasoned that materiality was a question of fact that could not be resolved at the motion to dismiss stage. The court also found that the plaintiffs adequately alleged scienter, finding that the individual defendants had access to specific data about the number of active locations that would have indicated inflation.

District of Minnesota Grants Motion To Dismiss Securities Fraud and Control Person Liability Claims Against Bedding Manufacturer, Executives

Steamfitters Local 449 Pension & Ret. Sec. Funds v. Sleep No. Corp. (D. Minn. July 10, 2023)

What to know: The District of Minnesota granted a motion to dismiss securities fraud and control person liability claims against a bedding designer and manufacturer and its executives because the plaintiffs failed to allege that the defendants made false statements and acted with the requisite scienter.

Judge Patrick Schiltz of the U.S. District Court of the District of Minnesota granted a motion to dismiss securities fraud and control person liability claims against Sleep Number Corporation and two of its executives. The plaintiffs acquired Sleep Number common stock between February and July 2021 and claimed that the defendants failed to inform them that supply chain issues would affect Sleep Number's production. They sued the defendants for securities fraud under Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder, and control person liability under Section 20 of the Exchange Act.

One of the critical components for Sleep Number's mattresses is foam, which is made from petroleum chemicals manufactured along the Gulf Coast. After a severe winter storm hit the Gulf region in February 2021, oil refineries experienced extensive damage and were shut down. As a result of the storm, manufacturers that supplied foam to Sleep Number declared *force majeure*. The plaintiffs alleged that, as a result, the storm significantly disrupted Sleep Number's supply chain, resulting in product shortages that delayed the manufacture of products.

The plaintiffs alleged that Sleep Number failed to inform investors of the supply chain disruption and misled them by making several false statements:

- First, the plaintiffs claimed Sleep Number insinuated it was in a solid financial and supply position to promptly deliver products to its customers.
- Second, the plaintiffs alleged that Sleep Number, in its 2020 10-K, (i) failed to mention the side effects of the storm, (ii) only disclosed future risk instead of the risk that had already materialized and (iii) included Sarbanes-Oxley (SOX) certifications signed by executives that falsely stated the 10-K did not include false or misleading statements.
- Lastly, plaintiffs contended that one of the Sleep Number executives misled the public on an earnings call concerning predictions for the second quarter. According to the plaintiffs, the executive only disclosed Sleep Number's supply restrictions in the first quarter instead of the possible continuing effects in the second quarter.

The court dismissed the plaintiffs' securities fraud claim because it found the complaint was devoid of allegations that Sleep Number's supply plummeted to the point of disruption in its foam supply chain. Instead, the court observed that the plaintiffs' allegations relied on purported facts that predated the storm or its effects and, therefore, these facts would not show that the defendant's statements were untrue when they made them.

Additionally, the court noted that because the plaintiffs did not specifically allege facts showing the storm's impact or that the chemical manufacturers had shut down operations before the company filed its 10-K, their allegations failed to substantiate the securities fraud claim. Similarly, the court noted that the plaintiffs' SOX argument failed to allege that Sleep Number's supply chain situation was dire when the executives signed the SOX certifications. As for the earnings call, the court found the plaintiffs' conclusory allegations failed to show that the company's second-quarter predictions were false at the time the executive made the statement. Similarly, the court noted that the plaintiffs failed to present facts that gave a "strong inference" of scienter because they did not allege that the defendants' statements were false when they made them.

Consequently, having dismissed the underlying securities fraud claims, the court dismissed the plaintiffs' control person liability claim and granted the defendants' motion to dismiss.

Contacts

New York
One Manhattan West
New York, NY 10001
212.735.3000

Alexander C. Drylewski
212.735.2129
alexander.drylewski@skadden.com

Lara A. Flath
212.735.3717
lara.flath@skadden.com

Robert A. Fumerton
212.735.3902
robert.fumerton@skadden.com

Jay B. Kasner
212.735.2628
jay.kasner@skadden.com

David Meister
212.735.2100
david.meister@skadden.com

Daniel Michael
212.735.2200
daniel.michael@skadden.com

Scott D. Musoff*
212.735.7852
scott.musoff@skadden.com

Patrick G. Rideout
212.735.2702
patrick.rideout@skadden.com

Susan L. Saltzstein*
212.735.4132
susan.saltzstein@skadden.com

Tansy Woan
212.735.2472
tansy.woan@skadden.com

George A. Zimmerman
212.735.2047
george.zimmerman@skadden.com

Boston
500 Boylston St.
Boston, MA 02116
617.573.4800

James R. Carroll
617.573.4801
james.carroll@skadden.com

Eben P. Colby
617.573.4855
eben.colby@skadden.com

Michael S. Hines*
617.573.4863
michael.hines@skadden.com

Alisha Q. Nanda
617.573.4804
alisha.nanda@skadden.com

Chicago
155 N. Wacker Drive
Chicago, IL 60606
312.407.0700

Matthew R. Kipp
312.407.0728
matthew.kipp@skadden.com

Marcie Lape (Raia)*
312.407.0954
marcie.lape@skadden.com

Chuck Smith*
312.407.0516
charles.smith@skadden.com

Houston
1000 Louisiana St., Suite 6800
Houston, TX 77002
713.655.5100

Noelle M. Reed
713.655.5122
noelle.reed@skadden.com

Los Angeles
300 S. Grand Ave., Suite 3400
Los Angeles, CA 90071
213.687.5000

Winston P. Hsiao
213.687.5219
winston.hsiao@skadden.com

Virginia Milstead
213.687.5592
virginia.milstead@skadden.com

Peter B. Morrison*
213.687.5304
peter.morrison@skadden.com

Jason D. Russell
213.687.5328
jason.russell@skadden.com

Palo Alto
525 University Ave.
Palo Alto, CA 94301
650.470.4500

Jack P. DiCanio
650.470.4660
jack.dicanio@skadden.com

Mark R.S. Foster*
650.470.4580
mark.foster@skadden.com

Washington, D.C.
1440 New York Ave., N.W.
Washington, D.C. 20005
202.371.7000

Anita B. Bandy
202.371.7570
anita.bandy@skadden.com

Bradley A. Klein*
202.371.7320
bradley.klein@skadden.com

Wilmington
One Rodney Square
920 N. King St.
Wilmington, DE 19801
302.651.3000

Cliff C. Gardner
302.651.3260
cgardner@skadden.com

Joseph O. Larkin
302.651.3124
joseph.larkin@skadden.com

Paul J. Lockwood
302.651.3210
paul.lockwood@skadden.com

Edward B. Micheletti*
302.651.3220
edward.micheletti@skadden.com

Jenness E. Parker
302.651.3183
jenness.parker@skadden.com

Jennifer C. Voss
302.651.3230
jennifer.voss@skadden.com

*Editors

This communication is provided by Skadden, Arps, Slate, Meagher & Flom LLP and its affiliates for educational and informational purposes only and is not intended and should not be construed as legal advice. This communication is considered advertising under applicable state laws.