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Securities Litigation

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I. Introduction

The federal securities laws are vast and intricate. To complicate things further, congressional, regulatory, and judicial actions all combine to make this area of law prone to quick and dramatic change. Although securities litigation occurs most frequently in specific federal districts, cases are brought throughout the country, resulting in frequent case-law differences among the circuits.

The stakes of such cases can be quite high, and not only for the parties involved. Lawyers, compliance officers, traders, and other industry workers are very finely attuned to even small pronouncements on the nature of the securities laws. Judges should not be surprised if market participants well beyond their own districts pore over their decisions on issues of first impression.

That is not to say that securities cases are not without their rewards. Judges interviewed for this guide appreciate the intellectual challenge of such cases, and they agree that the lawyers involved tend to be experienced and smart, which makes the cases demanding, but structured.

This pocket guide is designed to offer judges an introduction to the law and practice of securities litigation. It provides an overview of the types of legal and practical issues judges may confront in litigation arising under the securities laws, and, where possible, offers suggestions. This guide also identifies the areas of securities law most prone to circuit splits or frequent change, so that judges know where to be particularly vigilant about looking at up-to-date case law and legislation.

Because of the sheer number and particularity of possible securities actions, this pocket guide cannot be exhaustive. Rather, it provides a lay of the land and highlights the issues that are most commonly litigated or most complex.[1] While the guide does provide descriptions of specific causes of action, details concerning each particular section are omitted in favor of common themes and parallels like pleading requirements and secondary liability assessments. The guide devotes particular attention to securities class actions because judges interviewed for the guide identified those cases as the ones that can be the most difficult to manage without prior experience, and for which it is possible to lay out helpful guidelines.

Finally, the guide points out the ways in which securities litigation is similar to or differs from other actions a judge may encounter. For example, the most common securities suits are those alleging fraud, which are usually brought under section 10(b) of the Securities and Exchange Act of 1934 and SEC Rule 10b-5 promulgated thereunder. Although these causes of action have specific elements and case law attached to them, in broad strokes, they are similar enough to suits brought under common-law fraud that judges can take some comfort applying their general knowledge from that area of law. In contrast, many suits brought under more obscure provisions of the securities laws are highly technical. For these cases, judges will not be able to rely on their general knowledge and must be

1. See Thomas Lee Hazen, Federal Securities Law (Federal Judicial Center, 3d ed. 2011) for a more thorough review of federal securities law issues litigated in the federal courts.

prepared to immerse themselves in the relevant statutes and rules to resolve the issues before them.

II. Sources of Securities Law

A. Statutes

The principal causes of action for securities suits, whether public or private, criminal or civil, are found in the Securities Act of 1933 ("the Securities Act") and the Securities and Exchange Act of 1934 ("the Exchange Act").[2] The Securities Act treats the distribution of securities, whether by issuers, underwriters, or sellers. The Exchange Act is broader: It regulates day-to-day trading and includes a number of requirements for securities markets, market professionals, and issuers. In other words, the Securities Act regulates sellers (broadly defined), whereas the Exchange Act regulates both sellers and purchasers. The Exchange Act also created the Securities and Exchange Commission (SEC), which administers the securities laws in three basic ways: (1) it promulgates rules and orders to regulate the securities industry; (2) it supervises an elaborate system of industry self-regulation; and (3) it brings enforcement actions, either as administrative proceedings or in federal court.

The past few decades have seen further developments in securities law in the passage of the Private Securities Litigation Reform Act of 1995 (PSLRA), the Securities Litigation Uniform Standards Act of 1998 (SLUSA), the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank").[3] While these statutes generally do not create new causes of action, they have had a profound effect on how securities actions are brought, particularly class actions. By and large, these acts amended the Securities Act and the Exchange Act, meaning that most of the relevant law remained in the same places in the U.S. Code.

The PSLRA included a wide array of reforms targeted at eliminating frivolous and unmeritorious securities class actions. It made substantial changes to pleading, discovery, liability, and fee provisions in the federal securities laws, and it placed additional requirements on those looking to serve as lead plaintiffs. The passage of the PSLRA caused many plaintiffs to flock to state courts in the hope of avoiding its terms. These lawsuits brought in state court were nominally predi-

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2. 15 U.S.C. §§ 77a–77aa (2012); 15 U.S.C. §§ 78a–78pp (2012).

3. Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 and 18 U.S.C.); Pub. L. No. 105-353, 112 Stat. 3227 (codified as amended in scattered sections of 15 U.S.C.); Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in scattered sections of 11, 15, 18, and 28 U.S.C.); Pub. L. No. 111-203, 124 Stat. 1376 (codified as amended in scattered sections of 7, 12, and 15 U.S.C.). Other statutes that govern the securities industry include the Trust Indenture Act of 1939, 15 U.S.C. §§ 77aaa–77bbbb (2012); the Investment Company Act of 1940, 15 U.S.C. §§ 80a-1 to 80a-64 (2012); the Investment Advisers Act of 1940, 15 U.S.C. §§ 80b-1 to 80b-21 (2012); and the Securities Investor Protection Act of 1970, 15 U.S.C. §§ 78aaa–78*lll* (2012). These last four statutes will not be treated in this guide.

cated on state law, but made the same sorts of arguments previously made under the federal securities laws.

Consequently, Congress passed SLUSA, which essentially provided that class actions that could be brought under the federal securities laws must be brought in federal court. However, it provided exemptions for certain actions brought by agents of the state and the like.

Sarbanes-Oxley was passed in the wake of fraud and corruption scandals that included companies like Enron and WorldCom. It included reforms in securities law to enhance the accountability of corporate officers, as well as requirements for more outside oversight and more detailed disclosure.[4]

Similarly, Dodd-Frank was passed in response to the financial crisis of 2008, and it contained an array of reforms in securities law as well as areas far beyond securities. Securities-related provisions included making certain disclosure requirements applicable to a broader range of organizations and instructing the SEC to conduct a host of studies and rule-making endeavors in areas like consumer protection, corporate governance, and credit ratings.

This quick overview of the more recent legislation offers a helpful window into congressional priorities. Amendments to the securities laws are generally designed to curb abusive private actions, to create accountability for corporate officers, and to render capital markets more efficient by encouraging voluntary disclosure of financial information.

B. SEC Rules and Regulations

In its role as regulator for the securities industry, the SEC has promulgated hundreds of rules, orders, policy statements, interpretive releases, and other materials that enforce or explicate the securities laws. The most well-known of these is Rule 10b-5, which was enacted in 1948 and is discussed at length later in this guide.[5]

In the past twenty years in particular, Congress has often passed securities legislation that contains broad objectives and then tasks the SEC with promulgating rules and regulations that fill in the details. This makes SEC materials increasingly important in litigation. Congress gave SEC rules and regulations statutory force, so they are among the most compelling laws the agency can generate. Other materials the SEC promulgates, including policy statements (clarifying the SEC's position on particular matters) and interpretive releases (providing guidance on topics of general interest to the business and investment communities), are advisory. Still, these materials can be extremely helpful in clarifying the agency's positions, particularly regarding the rules and regulations the agency itself has promulgated. Some judges, particularly court of appeals judges, have been successful in asking the SEC to submit briefings regarding the interpretation of particular regulations, including regulations cited in private litigation that might have a broader effect.

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4. Some of Sarbanes-Oxley's requirements were lifted for small businesses in the Jumpstart Our Business Startups Act of 2012 (JOBS Act), Pub. L. No. 112-106, 126 Stat. 306 (codified as amended in scattered sections of 15 U.S.C.).

5. *See* Part VII.A, *infra*.

C. Case Law

Some areas of securities law are significantly shaped by judges' opinions. In particular, the law of securities fraud, which was promulgated under section 10(b) of the Exchange Act, SEC Rule 10b-5, and other provisions, is among the most heavily judicially shaped areas of federal law. Chief Justice Rehnquist called the law of Rule 10b-5 "a judicial oak which has grown from little more than a legislative acorn."[6]

Judges frequently analogize different provisions of the securities acts to one another when trying to determine the particular contours of whichever provision is under consideration. They do so based on provisions with similar language, structural roles, or purposes.

III. What Is a Security?

In many cases, there will be no question whether the instrument at issue is a security; the extremely broad statutory definition of *security* appears to encompass "virtually any instrument that might be sold as an investment."[7] Examples of securities include stocks, futures, bonds, and trust certificates.

In some cases, whether something qualifies as a security will be the *only* real issue to decide. The question of what qualifies as a security under the securities laws has been the subject of an extensive body of case law, and the challenge of providing a succinct definition is well-known. For example, one of the leading Supreme Court cases on this issue, *SEC v. W.J. Howey Co.*,[8] has a test for whether an investment contract falls under the securities laws. The test includes the existence of a "common enterprise" for investment. There have been numerous circuit splits regarding that case's definition of *enterprise* and its application to other investment instruments. This is an area of securities law that does not lend itself well to generalities; when the existence of a security is at issue, judges will most likely have to make an extremely particularized inquiry.

IV. Types of Securities Actions

There are several types of securities actions. In addition to securities actions brought by private parties, the SEC and Department of Justice (DOJ) can bring civil enforcement actions and criminal proceedings, respectively.

A. Private Parties and Class Actions

Many of the most complicated securities suits are filed as class actions. The Second Circuit and the Ninth Circuit have the largest number of securities class action filings. The Third Circuit and the Fifth Circuit have the third and fourth larg-

6. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 737 (1975).

7. Reves v. Ernst & Young, 494 U.S. 56, 61 (1990). The definition is at 15 U.S.C. § 77b(a)(1) (2012).

8. 328 U.S. 293 (1946).

est number of these filings. Every circuit has had at least one potential securities class action filed in it yearly for the past five years.[9]

The vast majority of securities class actions allege violations of section 10(b) of the Exchange Act (and SEC Rule 10b-5) or section 11 or 12 of the Securities Act. In the past five years, there has also been a significant number of merger objection cases under sections 13 and 14 of the Exchange Act.[10] These sections are all discussed in further detail in Part VII, *infra*, and particular guidance for class action case management appears in Part V.B.

B. SEC Civil Enforcement Actions

SEC-brought actions often arise under the same sections of the securities laws as private actions, but have features particular to them. Sometimes the SEC needs to prove different elements than private parties do, or has alternative options available for proving those elements; some of these differences are discussed in Parts VII and VIII, *infra*. Judges interviewed for this guide also said that by and large, the cases brought by the SEC have more straightforward facts than private actions do. That is not to say, however, that these cases are easier to adjudicate. Judges caution that in SEC proceedings, there is sometimes a disconnect between the investigation and litigation of a case. For instance, investigative testimony, often used by the government to build its case, may constitute inadmissible hearsay and therefore cannot be relied on at summary judgment or trial. There may also be delays if SEC counsel needs to check with those higher up in the commission on certain policy implications.

A growing area of securities litigation in federal court is the set of cases challenging the SEC's use of administrative law judges (ALJs). The SEC has the option of using internal administrative proceedings, rather than the federal courts, to enforce the securities laws, and it frequently does so. Increasingly, defendants in those actions are challenging their constitutionality. Arguments are based on due process, equal protection, or separation-of-powers grounds, and recent cases have focused particular attention on jurisdictional and constitutional arguments relating to the setup of the regulatory system.

This area of law is fast moving and hard to predict. The Seventh Circuit recently rejected a set of jurisdictional arguments and held that the SEC's administrative review structure is constitutional.[11] The Second Circuit and D.C. Circuit have similarly held that federal courts lack jurisdiction to hear such claims until there is a final agency decision.[12] While it is difficult to offer judges guidance at this point, fortunately, these cases tend to be relatively isolated and should not affect the other types of cases discussed in this guide.

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9. Svetlana Starykh & Stefan Boettrich, NERA, Recent Trends in Securities Class Action Litigation: 2015 Full-Year Review 10 (2016).

10. *Id.* at 5.

11. *See* Bebo v. S.E.C., 799 F.3d 765 (7th Cir. 2015).

12. *See* Tilton v. S.E.C., 824 F.3d 276, 291 (2d Cir. 2016); Jarkesy v. S.E.C., 803 F.3d 9, 30 (D.C. Cir. 2015).

One noteworthy remedy available to the SEC under the securities laws is to seek a permanent or temporary injunction "whenever it shall appear to the Commission that any person is engaged or about to be engaged in acts or practices constituting a violation of any provision" of the securities laws or related rules.[13] These injunctions, popularly referred to as "obey-the-law" or "sin-no-more" injunctions, usually seek to prevent ongoing and future violations of the securities laws. One prime benefit is that violators may be held in contempt of court and assessed for related penalties.

Judges who encounter requests for such injunctions should scrutinize the proposed injunctions' specificity and scope. These injunctions "must be framed so that those enjoined know exactly what conduct the court has prohibited and what steps they must take to conform their conduct to the law" in order to be enforceable.[14] Judges should be wary of injunctions that are vague as to which laws and conduct are included as well as ones in which time frames of applicability do not seem commensurate with the conduct alleged.

C. DOJ Criminal Enforcement Actions

The government has the authority to bring criminal charges against a person who violates the securities laws willfully. Different courts of appeals define *willfully* in different ways, but they all generally agree that a defendant need not know of a particular rule or regulation in order to act willfully; rather, a defendant acting "with a bad purpose: either to disobey or disregard the law" is acting willfully.[15]

Although much of the same substantive law is used in criminal securities cases and civil securities cases, proceedings in the two types of cases tend to be quite different. Criminal securities cases are high stakes for both sides and are hard fought as a consequence. Criminal defendants also often need to pay their own lawyers, as opposed to being covered by the company that employs them.

Determining intent in a criminal case is usually the most difficult task facing a judge, and judges interviewed for this guide said issues concerning a finding of conscious avoidance can be particularly challenging. Conscious avoidance, also called "willful blindness" or "deliberate ignorance," provides that in situations in which a defendant's knowledge of a fact is required to prove guilt, that knowledge "may be found when the jury is persuaded that the defendant consciously avoided learning that fact while aware of a high probability of its existence."[16] In other words, defendants cannot escape culpability simply by burying their heads in the sand.

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13. 15 U.S.C. § 78u(d)(1) (2012 & Supp. III 2015); *see also* 15 U.S.C. § 77t(b) (2012).

14. S.E.C. v. Smyth, 420 F.3d 1225, 1233 n.14 (11th Cir. 2005); *see also* S.E.C. v. Goble, 682 F.3d 934, 949–53 (11th Cir. 2012) (containing extended discussion of vagueness concerns in obey-the-law injunctions).

15. United States v. Peltz, 433 F.2d 48, 54 (2d Cir. 1970); *see also* 3B Fed. Jury Prac. & Instr. § 161:53 (6th ed.) (2013).

16. United States v. Svoboda, 347 F.3d 471, 477 (2d Cir. 2003) (internal quotation marks and citations omitted).

Judges must determine whether a factual predicate exists that makes a conscious avoidance jury instruction appropriate, as well as how to phrase such an instruction. Both of these issues have been addressed in circuit-specific case law, but have been most fully developed in the Second Circuit. A factual predicate exists when there is evidence that allows a rational juror to reach the conclusion, beyond a reasonable doubt, "that the defendant was aware of a high probability of the fact in dispute and consciously avoided confirming that fact."[17] Several different phrasings of the instruction have been upheld by courts of appeals.[18]

Conviction under the securities laws can lead to fine, imprisonment, or both, but the maximum penalties under the Securities Act are much less severe than those under the Exchange Act.[19] In addition, section 32(a) of the Exchange Act prohibits imprisonment if the defendant "proves that he had no knowledge of [a] rule or regulation."[20] The Second Circuit has held that the statute's specific inclusion of the phrase "rule or regulation" means that the defense is unavailable for violations of a statute; the Eighth Circuit has disagreed.[21]

Under the federal sentencing guidelines, sentence length for securities-related crimes is heavily correlated with the amount of loss. Judges caution that dramatically different losses can be calculated using equally reasonable methods, particularly in situations involving the backdating of stocks. Judges should exercise care when reviewing loss calculations in any setting, but particularly when they are being used to determine a criminal sentence. There is a six-year statute of limitations on criminal securities fraud violations.[22]

D. Parallel Proceedings

When the SEC and the DOJ file parallel civil and criminal actions, most judges will stay the civil action until the criminal action is resolved. Oftentimes, the civil action will be withdrawn or settled before a judge needs to pick it back up. If the defendants in the two types of actions do not overlap exactly, however, stays can be a little more difficult. In such circumstances, judges often opt to stay only the cases of those civil defendants who also have criminal charges brought against them, and they schedule discovery such that these defendants are deposed at the end.

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17. United States v. Ferrarini, 219 F.3d 145, 154 (2d Cir. 2000) (internal quotation marks and citation omitted); *see also* United States v. Heredia, 483 F.3d 913, 922 (9th Cir. 2007) (offering a different standard); United States v. Stone, 987 F.2d 469, 471 (7th Cir. 1993) (offering a similar test for an "ostrich instruction").

18. *See, e.g.*, U.S. S.E.C. v. Big Apple Consulting USA, Inc., 783 F.3d 786, 803–04 (11th Cir. 2015); United States v. Svoboda, 347 F.3d 471, 476 n.5 (2d Cir. 2003); United States v. Stone, 987 F.2d 469, 470 (7th Cir. 1993).

19. *See* section 24 of the Securities Act, 15 U.S.C. § 77x (2012); section 32(a) of the Exchange Act, 15 U.S.C. § 78ff(a) (2012).

20. 15 U.S.C. § 78ff(a) (2012).

21. *See* United States v. Eucker, 532 F.2d 249, 256 (2d Cir. 1976); United States v. Knueppel, 293 F. Supp. 2d 199, 204 (E.D.N.Y. 2003); *but see* United States v. Behrens, 644 F.3d 754, 756 (8th Cir. 2011).

22. 18 U.S.C. § 3301(b) (2012).

Judges may find themselves presiding over SEC or DOJ proceedings when a private suit has also been filed that is premised on the same facts. In such situations, judges need to be aware of the ways in which their decisions in either type of proceeding might affect the other. Some of these challenges are discussed in Part XII, *infra*.

V. Preliminary Requirements and Procedures

Preliminary procedures under the securities laws are not significantly different from those for other commercial suits, apart from the specific requirements under the PSLRA, discussed in Part V.B, *infra*. This part discusses a selection of issues that judges have frequently encountered in the preliminary stages of securities cases.

A. Requests for Temporary Restraining Orders and Preliminary Injunctions

Some types of securities actions begin with a request for a temporary restraining order (TRO) or preliminary injunction. Proxy litigation and Williams Act actions under sections 13–14 of the Exchange Act are common examples (discussed in Part VII.C.5 & 6, *infra*).

Motions for preliminary injunctions are reviewed under the traditional standard: Movants must demonstrate the prospect of irreparable harm and show that legal remedies are inadequate. Judges who receive a request for an injunction or TRO will have to move quickly, particularly when there is a melting asset involved or a corporate restructuring at stake. Judges interviewed for this guide were in agreement that there is no substitute for getting the parties talking, ideally in person, and that ex parte orders should be avoided whenever possible.[23]

Some judges suggest setting up a fast briefing schedule and instructing the parties to be ready with joint proposals as soon as possible. They also suggest that where possible, direct testimony be submitted by affidavit so that it can be sworn to and then tendered for cross-examination. Other judges call the parties into court the same day or the day after the TRO request is filed, arrange for a reporter, and set a schedule at that point. Judges also sometimes come to the hearing with a draft opinion so that they can decide the issue as soon as possible afterward.

When the SEC commences a case, it will sometimes seek an order to freeze or seize assets and to have a receiver appointed to help preserve the assets. In some such instances, the assets seized will be the only source of income a defendant has, so the defendant will petition the court not to stop the flow of funds entirely, but to provide enough to cover living expenses and legal fees. Judges confronting such situations should consider how to negotiate the request so as to be fair to both sides and preserve the assets at issue, while also acknowledging that no formal adjudication has yet occurred for the defendant.

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23. Judges did say they are more likely to grant ex parte requests from the SEC, since these usually appear in cases in which assets are in immediate danger of disappearing.

B. Class Action Management

Federal Judicial Center publications have devoted considerable attention to class action management, particularly Chapter 31 of the *Manual for Complex Litigation, Fourth*,[24] and *Managing Class Action Litigation: A Pocket Guide for Judges*.[25] This section highlights aspects of class action management common in or particular to securities cases, but those other sources contain further details and suggestions.

1. Preliminary Case Management

Plaintiffs seeking to file class actions under the securities laws must satisfy not only the traditional requirements under Federal Rule of Civil Procedure 23, but also certain prerequisites under the PSLRA. Like many complex cases, securities class actions are usually best handled with immediate and assertive case management.[26] Judges should endeavor to create a structure in which issues are resolved quickly and, to the extent possible, once. Putting thought into case management at the start and continuing to pay attention to it as the action proceeds can help keep the case moving and narrow the issues under consideration.

Judges interviewed for this guide suggest setting up an initial conference under Federal Rule of Civil Procedure 16 quickly in order to get the parties talking to each other and to begin working through the requirements of the PSLRA. Chief among these requirements are notice procedures and the selection of lead plaintiff and lead counsel.

The PSLRA is designed in part to prevent lawyer-driven suits and expedite selection of a lead plaintiff. It includes a sixty-day deadline from the filing of a complaint for additional complaints from anyone seeking to serve as lead plaintiff. Prospective lead plaintiffs must file with their complaint a signed statement that confirms that the plaintiff did not purchase the security at issue at the direction of counsel or in order to participate in the suit. The statement must also identify any other actions in the previous three years in which that plaintiff served or sought to serve as a representative party. Additionally, such plaintiffs must provide notice to members of the purported class no later than twenty days after the filing of the initial complaint that an action is pending and that any member of the purported class may move to serve as lead plaintiff.[27]

At the initial conference, judges usually set a schedule for these proceedings as well as a conference at which to hear from candidates for lead plaintiff and render a decision. Other provisions of the PSLRA outline Congress's expectation about

24. Manual for Complex Litigation, Fourth ch. 31 (Federal Judicial Center 2004) [hereinafter MCL, Fourth].

25. Barbara J. Rothstein & Thomas E. Willging, Managing Class Action Litigation: A Pocket Guide for Judges (Federal Judicial Center, 3d ed. 2010).

26. Many courts have local rules that apply to securities class actions, and judges are encouraged to consult those rules along with the suggestions offered in this section and other FJC resources.

27. See 15 U.S.C. § 78u-4 (2012) for additional requirements.

how long certain steps of the litigation should take: for instance, that a lead plaintiff will be appointed within ninety days of the date the notice is published. Such time lines are often subject to revision, so judges should not feel constrained by them. There will be instances in which modifications to the periods set out in the statute will better suit the action, particularly when there are consolidation issues to consider.

Judges usually schedule the lead plaintiff conference between two and six weeks after all lead plaintiff petitions are due, and many wait until all petitions are received before reviewing the case. Judges report that frequently plaintiffs scramble to line up the lead plaintiff and lead counsel, and often, candidates fall by the wayside, leaving a shorter roster for a judge to consider closer to the conference date. The PSLRA mandates that the action be consolidated before a lead plaintiff is appointed.

The decision of which plaintiff is most appropriate for the role of lead plaintiff is left largely to the judge's discretion. The PSLRA states that the "most adequate plaintiff" should be appointed, and it offers a rebuttable presumption that this would be the plaintiff who (a) filed the complaint; (b) has the largest financial interest; and (c) otherwise satisfies Rule 23's requirements.[28] The PSRLA strives to help judges to be fair to parties in selecting a lead plaintiff, but also to pick one that has the interest and resources to pursue the case vigorously on behalf of the class.

Judges suggest setting aside about a week to get familiar with the complaint, class period, nature of the claims, and other factors that will help determine an appropriate lead plaintiff and lead counsel. Judges suggest that when reviewing the applications, a judge pay particular attention to how the class is defined, particularly the time period. A plaintiff will often define a class in such a way as to maximize the plaintiff's apparent loss, increasing the likelihood of him or her being appointed lead plaintiff. Judges caution that it can be extremely difficult to identify inappropriate manipulation at this early stage, so the judge should keep a watchful eye for parameters that are inappropriate. For instance, if a case involves alleged misstatements and a consequent stock drop and has a class period that extends well beyond such events, it may be worth questioning why.

Prospective lead plaintiffs almost always apply with attached counsel. However, a judge need not automatically select the lead plaintiff's originally chosen representative as lead counsel. The PSLRA directs that the lead plaintiff shall select counsel "subject to the approval of the court."[29] The judge may decide to examine how experienced the lead counsel candidate is in the subject and how many similar cases he or she has pending, to ensure the counsel has both the experience and time to adequately handle the case. Some judges, after appointing a lead plaintiff, require the plaintiff to conduct due diligence and reexamine potential lead counsel. These judges reason that the lead plaintiff has a fiduciary duty to the

28. *See* 15 U.S.C. § 78u-4 (a)(3)(B)(iii) (2012).

29. *Id.* § 78u-4(a)(3)(B)(v) (2012).

class and is in a position to negotiate better representation and more attractive fee proposals.

Having two or more firms as co-lead counsel is an option, though an unusual one. If one lead counsel is from a relatively small firm and would benefit from the resources of a second, for instance, judges have allowed a second to join. In extremely large cases, judges have also found it helpful to appoint a liaison counsel, who facilitates communication between the court and other counsel (for instance, if there are individual defendants with separate counsel).

One of the unintended effects of the PSLRA's notice provisions has been a tendency for attorneys to use them to increase their chances of being appointed lead counsel. For instance, as one court noted, some attorneys will file notices that solicit additional clients, and will file suit "not once but over and again, all in an effort to compile the largest portfolio of investor names."[30] Judges who encounter tactics like these need not give credence to an artificially created group, but can instead choose a lead plaintiff with a smaller financial stake but greater ability and incentive to manage the litigation effectively. This position is in line with guidance the SEC has offered on this point.[31]

Judges suggest that once the lead plaintiff has been selected, the judge set a motion schedule as early as possible. Under the PSLRA, discovery is stayed during the pendency of the motion to dismiss, but the judge will still need to set the schedule for a consolidated amended complaint and briefing for the motion to dismiss. Some judges set the schedule at the lead plaintiff conference. Other judges have the parties come to a second conference within a month after the lead plaintiff conference to set the schedule, and they have the parties provide a proposed schedule a week prior to this second conference. Reasonable extensions should be granted, but by and large, the case should be kept moving. Because the selected lead counsel often has experience in this area, judges report that the parties often have a good sense of a plan they want to follow and that things run smoothly.

Judges have different approaches to class action case management after the preliminary issues are taken care of. Some schedule regular conferences to keep parties on track and dispose of issues that arise. Others eschew such conferences, preferring instead to direct parties to meet and confer and draft short briefing papers before the parties meet before the judge. Judges who follow the latter course believe this prevents issues from festering longer than they need to and limits letter writing campaigns and other transaction costs.[32]

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30. *In re* Network Assocs., Inc. Sec. Litig., 76 F. Supp. 2d 1017, 1021 (N.D. Cal. 1999).

31. *See, e.g., In re* Baan Co. Sec. Litig., 186 F.R.D 214, 218–35 (D.D.C. 1999) (appending an amicus brief from the SEC with its position on appointing lead counsel in such circumstances).

32. See Parts VI and XII, *infra*, on the motion to dismiss and discovery, for more information on class action management at these stages of litigation.

2. Class Certification

Federal Rule of Civil Procedure 23(c)(1) counsels that a judge should decide whether to certify an action as a class action "[a]t an early practicable time." Judges choose to schedule the motion for class certification at various points in litigation, but there has been a trend in recent years to make the decision earlier in securities cases. Most judges set this date at the Rule 26 discovery conference, and most set a time between the middle and end of fact discovery. This time line balances the need for sufficient discovery to draft a complete class certification motion against the desire for early clarity regarding the existence and scope of the class.

Class certification is usually the first point in the case where a judge can make factual findings, as well as take a preliminary position on the merits. Judges interviewed for this guide agree that the hardest questions they face at the certification stage usually involve issues of predominance, that is, Rule 23(b)(3)'s requirement that "questions of law or fact common to class members predominate over any questions affecting only individual members." Looking at how a purported class intends to prove the merits of its case is often necessary for this determination. In addition, in *Halliburton Co. v. Erica P. John Fund, Inc.*, the Supreme Court clarified that defendants can present evidence at the class certification stage to rebut a presumption of reliance in a securities fraud case.[33] That decision means that this will be an area of heavy attention in the upcoming years.[34]

Parties have sometimes asked judges to bifurcate cases between common "liability" issues (e.g., falsity, materiality, scienter) and specialized "damages" issues (causation and damages). The request is for the class only to be certified with regard to the first set of issues, or for the case to be tried initially only on the first set of issues, or both. Judges will sometimes grant such requests in particularly complex cases in which the division can be done precisely in terms of the discovery sought. More frequently, judges deny such requests, because the judges find that they cause unnecessary complication of the class certification decision, as well as time delays, without providing much benefit in the way of procedural simplification or cost reduction.

The FJC has developed illustrative notices of proposed class action certification, which are available on its website.

3. Opt-out Plaintiffs

A regular feature in class action cases is the presence of opt-out plaintiffs: individual plaintiffs who choose not to participate in the class and who therefore have the option to pursue their own litigation. In the securities class action context, plain-

33. 134 S. Ct. 2398 (2014) ("*Halliburton II*")

34. *See, e.g.,* IBEW Local 98 Pension Fund v. Best Buy Co., 818 F.3d 775 (8th Cir. 2016) (applying *Halliburton II* and holding that defendant successfully rebutted the fraud-on-the-market presumption).

tiffs who opt out are often institutional investors represented by established law firms[35] and allege claims virtually identical to those of the class action.

Plaintiffs may opt out at various points in a litigation. Some opt out quite late, after a settlement has been announced, presumably because they hope to gain more money than they would have received as class members or because they otherwise object to the terms of the settlement. Some judges insist that fee petitions be filed prior to the opt-out deadline precisely so that potential opt-out plaintiffs can look to them as a factor in their decision. Plaintiffs may also opt out earlier in the litigation in the interest of retaining more control over the litigation of their claims.[36]

A judge who encounters opt-out plaintiffs must consider a few factors. First and most important, when opt-out plaintiffs want to pursue their own litigation, the judge must decide whether those cases should be coordinated with the main class action, and if so, how. Judges tend to put such cases on the same track, reasoning that it prevents prolonged and redundant litigation and is not significantly more expensive for the opt-out plaintiffs. Of course, there are exceptions to every rule, and plaintiffs who opt out late in the litigation may not be able to catch up. Opt-out plaintiffs may also resist being aligned with the class action calendar for other reasons. For example, courts traditionally have a broad reading of SLUSA's definition of a "covered class action," which includes actions "joined, consolidated, or otherwise proceed[ing] as a single action for any purpose."[37] An opt-out plaintiff who might otherwise not be subject to SLUSA preclusion, then, may become precluded because the plaintiff has the same calendar as the class action.[38]

Another point to consider is how statutes of limitations and repose (and relevant tolling) apply to opt-out plaintiffs. As discussed in Part IX, *infra*, case law on tolling is complex and quick to change, and this is equally true in the opt-out context. For instance, courts have grappled with whether plaintiffs who opt out of a class action after a statute of repose has run may nonetheless bring suit.[39]

4. Third-Party Litigation Financing

Litigation financing, in which third-party investors help finance a lawsuit in exchange for an interest in the proceeds, is a relatively recent phenomenon in the United States. It first rose to prominence in the personal injury context, but since 2010 it has expanded rapidly to other causes of action.

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35. It has become increasingly common to see the same group of law firms representing both classes and opt-out plaintiffs in securities class actions.

36. *See* Jeffrey Paul Mahoney, *Navigating Alternatives to Securities Fraud Class Actions: State Law and Opt-Out Litigation,* 46 Loyola U. Chi. L.J. 459, 463–65 (Spring 2015).

37. 15 U.S.C. § 77p(f)(2)(A)(ii) (2012).

38. *See, e.g.*, *In re* Fannie Mae 2008 Sec. Litig., 891 F. Supp. 2d 458, 480 (S.D.N.Y. 2012) (finding individuals' state law claims precluded under SLUSA because their suit was a covered class action).

39. *See, e.g.,* Franklin U.S. Rising Dividends Fund v. American Intern. Grp., 605 F. App'x 32 (2d Cir. 2015) (discussing such questions in the context of changed law and a transfer between circuits).

Litigation financing is controversial. In many instances, parties need not even disclose that they are being financed by third parties. The practice has been criticized for, among other things,

- increasing the volume of cases brought, particularly weak ones;
- prolonging litigation and discouraging settlement or alternative dispute resolution (ADR);
- undercutting plaintiff and lawyer control over litigation;
- directing money away from the injured;
- constituting champerty; and
- creating various ethical conflicts.[40]

Proponents of the practice point to its many benefits, including

- addressing the staggering costs of litigation that could bar even meritorious claimants from bringing suit;
- providing funding to improve the quality of litigation;
- off-loading risk because the litigation is non-recourse, meaning parties owe nothing for unfavorable outcomes;
- allowing companies to focus on their core business and leave the pursuit of their claim to others; and
- evening the playing field with resource-laden defendants.[41]

Both supporters and opponents of litigation financing have called for regulation and rule making to provide clarity to lawyers and investors and protection to claim holders.

The impact of litigation financing on individual securities suits is difficult to gauge. But as increasing numbers of securities class actions receive third-party funding the third-party players are becoming more visible, and judges are paying more attention to potential conflicts of interest. Judges report that in the lead plaintiff and lead counsel selection process, some parties have pointed to the fact that they secured the third-party funding as the reason why they must be selected as lead plaintiff and lead counsel. Funders may not agree to come through with the funding without their preferred counsel or plaintiff making the decisions. Judges also report that plaintiffs claim privilege over communications between them and their funders, or file motions to enforce collection. Some judges now ask

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40. *See generally* U.S. Chamber Institute for Legal Reform, Stopping the Sale on Lawsuits: A Proposal to Regulate Third-Party Investments in Litigation 1–6 (Oct. 2012), *available at* http://web.archive.org/web/20160219202403/http://www.instituteforlegalreform.com/uploads/sites/1/TPLF_Solutions.pdf; New York City Bar Association Formal Opinion 2011-2, *available at* http://www.nycbar.org/ethics/ethics-opinions-local/2011-opinions/1159-formal-opinion-2011-02.

41. *See generally* David Lat, *6 Virtues of Litigation Finance*, Above the Law, Nov. 24, 2015, http://web.archive.org/web/20160606211438/http://abovethelaw.com/2015/11/6-virtues-of-litigation-finance/?rf=1; Sylvan Seidel & Sandra Sherman, *"Corporate Governance" Rules Are Coming to Third Party Financing of International Arbitration (and in General)*, *in* ICC, Doosier X: Third-Party Funding in International Arbitration 32–49; 35–36 (Bernardo M. Cremades & Antonias Dimolitsa eds., 2013).

parties if there is any outside financing so that proper fiduciary duties can be ascertained.[42]

C. Jurisdiction

Both the Securities Act and the Exchange Act confer subject-matter jurisdiction on federal courts for all cases brought under them.[43] This means that plaintiffs need not aver diversity of citizenship or amount in controversy to satisfy jurisdictional requirements, so long as they aver that some instrumentality of interstate commerce (such as the mail, telephone, or Internet) was used as part of the alleged violation. The type of instrumentality and degree of use required differ somewhat from circuit to circuit, though the general trend is toward broadening what satisfies this standard.

The law of extraterritorial jurisdiction in securities actions has been in flux in recent years. Dodd-Frank extended jurisdiction to actions brought by the government that involve "conduct occurring outside the United States that has a foreseeable substantial effect within the United States."[44] Many commentators see this as a response to *Morrison v. National Australia Bank*,[45] a case in which the Supreme Court rejected a "conduct and effects" test that the Second Circuit had previously used to determine jurisdiction under the securities laws in favor of a "transactional" test that focused on the location of the transactions at issue. Whether the "conduct and effects" test of Dodd-Frank reinstates the one that existed before *Morrison* is a difficult question, and one that courts are still working through.[46]

The supplemental jurisdiction provisions in 28 U.S.C. § 1367 allow federal courts to adjudicate causes of action under state securities laws if they are brought alongside federal securities law actions. Although subject-matter jurisdiction under the Exchange Act is exclusive to the federal courts, jurisdiction under the Securities Act is not, so non–class actions brought under the Securities Act in state court usually may not be removed to federal court. Individual circuits do have certain exceptions to the rule of non-removal of Securities Act cases; notably, the Second Circuit allows removal for Securities Act cases brought in state court during a pending federal bankruptcy proceeding.[47] In addition, as mentioned earlier in the context of securities class actions, SLUSA preempts state courts from hearing most such cases, and the Supreme Court has given SLUSA preemption broad interpretation.[48]

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42. *See generally* Bert I. Huang, *Litigation Finance: What Do Judges Need to Know?* 45 Colum. J.L. & Soc. Probs. 525 (2012).

43. 15 U.S.C. §§ 77v, 78aa (2012).

44. 15 U.S.C. §§ 77v(c), 78aa(b) (2012).

45. 561 U.S. 247 (2010).

46. *See, e.g.,* S.E.C. v. Chicago Convention Ctr., LLC, 961 F. Supp. 2d 905, 908 (N.D. Ill. 2013) (calling the issue "a complicated question" and determining that the court need not answer it "because the SEC has stated a claim under either inquiry").

47. *See* Cal. Pub. Employees' Ret. Sys. v. Worldcom, Inc., 368 F.3d 86, 104 (2d Cir. 2004).

48. *See* Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit, 547 U.S. 71, 85–86 (2006).

Provided that subject-matter jurisdiction and venue are established, federal courts have personal jurisdiction over a defendant anywhere in the United States under the Securities Act and the Exchange Act, so process may be served nationwide. Personal jurisdiction over foreigners is subject to a minimum contacts test.[49]

D. Forum and Venue

The forum and venue provisions of the securities laws are extremely broad. The most likely disputes involving forum will be ones in which (a) plaintiffs contest the validity of a mandatory arbitration provision, or (b) the SEC opts to use administrative proceedings rather than a civil action, an option the SEC has exercised with increasing frequency since the passage of Dodd-Frank. The SEC has issued guidance explaining its choice of forum,[50] but judges will most likely still encounter suits from defendants who are unhappy with having their cases heard by an administrative law judge. See the discussion of SEC actions in Part IV.B, *supra*, for more information on the types of arguments found in these suits.

E. Standing

Standing under the securities laws varies widely depending on which section of the laws the suit is brought under. For instance, some actions, like those brought under section 12 of the Securities Act, require a showing of privity, that is, a specific relationship between the parties. Defendants will often probe the contours of the requisite relationship to show that it does not exist.

Standing issues can also arise in the class action context when the commonality of standing is disputed. For instance, defendants have argued that named plaintiffs who have purchased some tranches of a security, but not all, should not be allowed to pursue claims on behalf of purchasers of the other tranches; courts have disagreed on this issue.[51]

VI. General Pleading Requirements and Standards, and the Motion to Dismiss

Most securities lawsuits are resolved early in litigation, and the motion to dismiss in particular is a critical step. A case is often reconfigured or shut down entirely at this point. For instance, NERA Economic Consulting examined potential class action lawsuits brought under SEC Rule 10b-5 or section 11 of the Securities Act (which together constitute the vast majority of securities class actions), and it found that consistently over fifteen years, about half of them were dismissed completely at the motion-to-dismiss stage. In addition, less than 9% of such lawsuits

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49. *See* Helicopteros Nacionales de Colombia, S.A. v. Hall, 466 U.S. 408, 414 (1984).

50. SEC, Division of Enforcement Approach to Forum Selection in Contested Actions, *available at* http://web.archive.org/web/20160605002331/https://www.sec.gov/divisions/enforce/enforcement-approach-forum-selection-contested-actions.pdf.

51. *See, e.g.*, NECA-IBEW Health & Welfare Fund v. Goldman Sachs & Co., 693 F.3d 145, 157–58 (2d Cir. 2012); *In re* Countrywide Fin. Corp. Mortgage-Backed Sec. Litig., 860 F. Supp. 2d 1062, 1068–69 (C.D. Cal. 2012).

had motions for summary judgment filed; this means that 91% of such suits were dismissed (by the court or the parties) or settled before then.[52] As a consequence, any changes to pleading requirements or to defenses allowed at the pleading stage (rather than at class certification, summary judgment, or trial) can have profound effects on caseloads and settlement amounts. Not surprisingly, then, the pleading stage is an area of intense focus for practitioners and policy makers alike.

The judges we interviewed suggested that when a judge is assessing motions to dismiss in a securities case, the judge use the opportunity to draw the boundaries of the case. They suggest paying particular attention to the subordinate components of the claims in order to see what can be done to narrow the case into something triable. Often, judges scrutinize the individual statements or omissions at issue, arguments relating to causation, and, in class actions, time periods. Given the specialized knowledge often needed by the judge and the sophistication of many of the lawyers involved in securities litigation, judges often find oral argument on the motion to dismiss helpful.

Some judges hold a pre-motion conference and instruct parties to draft a short summary of the arguments they plan to make in their motions. This process can sometimes help narrow or resolve certain open issues, and plaintiffs can address defendants' arguments in their initial brief rather than at reply. Judges will sometimes also allow plaintiffs to amend the complaint before they decide the motion based on arguments raised at the pre-motion conference. Note, however, that the Second Circuit has specifically held that the holding of such a conference cannot be grounds to deny leave to amend under Rule 15 if the motion is ultimately granted.[53] In the Second Circuit and throughout the country, liberal leave to amend means that judges usually dismiss these complaints without prejudice.

Elements of different causes of action under the securities laws have significant overlap. As a result, one difficulty judges frequently face is how to interpret case law addressing one cause of action when litigants argue that it should (or should not) apply to another. It may be helpful for the judge to consider securities suits as falling into two main groups: those that include allegations of fraud and those that do not. Issues like specificity of pleadings and mental element requirements tend to be more similar within these groups.

Cases brought under the securities laws that sound in fraud, for instance, must satisfy the heightened pleading requirements of Federal Rule of Civil Procedure 9(b). Courts have generally interpreted this rule to require that allegations be sufficiently particular as to put defendants on notice of the alleged wrong so that they can formulate an effective response. For example, courts have required that complaints specify the statements that the plaintiff contends were fraudulent, identify

52. Starykh & Boettrich, *supra* note 9, at 18.

53. *See* Loreley Financing (Jersey) No. 3 Ltd. v. Wells Fargo Sec., LLC, 797 F.3d 160, 189–91 (2d Cir. 2015).

their speaker and where and when they were made, and explain why the statements were fraudulent.[54]

Other securities actions are premised on negligence, and therefore generally have the lower pleading standard of Rule 8. However, this division between fraud and non-fraud securities suits is complicated by two issues. First, some courts that have held that sections of the acts that do not *require* that fraud be pleaded to state an action (notably, sections 11 and 12 of the Securities Act) still need to satisfy Rule 9(b) if the claims are "grounded in fraud."[55] Many circuits have yet to consider this question in the wake of the Supreme Court's revisions to general pleading standards in *Bell Atlantic Corp. v. Twombly*[56] and *Ashcroft v. Iqbal*.[57] Second, the PSLRA has certain heightened pleading requirements for "securities fraud actions," and its definition of what qualifies as such an action appears to encompass claims brought under sections 11 and 12(a)(2) of the Securities Act.[58] So while these actions might otherwise need to satisfy Rule 8, in the class action context, the standard is higher.

If all or part of a case survives the motion to dismiss, the case proceeds to discovery (see Part XII, *infra*, for a discussion of discovery).

VII. Selected Causes of Action Under the Securities Laws

This part offers discussion of the elements and other noteworthy features of several specific causes of action brought under the securities laws. Many of the issues that arise under certain provisions also appear in others; this part points out such parallels as they appear. Because of the high proportion of securities actions that do not reach summary judgment, this part pays particular attention to issues arising during the pleading and earlier stages of litigation.

A. Section 10(b) of the Exchange Act and SEC Rule 10b-5

Section 10(b) of the Exchange Act and SEC Rule 10b-5 promulgated thereunder[59] are the most common bases for private securities litigation: in 2015, 84% of class actions filed in federal court included such claims.[60] One principal reason for these instruments' popularity is their breadth. Section 10(b) prohibits using "manipulative or deceptive" practices "in connection with" the purchase or sale of securities, and it applies to both secondary market trading and initial offerings.[61]

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54. *See* ATSI Commc'ns, Inc. v. Saar Fund, Ltd., 493 F.3d 87, 99 (2d Cir. 2007) (citing Novak v. Kasaks, 216 F.3d 300, 306 (2d Cir. 2000)). In multidefendant cases, these criteria must be satisfied for each defendant. *See* Swartz v. KPMG LLP, 476 F.3d 756, 764–65 (9th Cir. 2007).

55. *See, e.g.*, *In re* NationsMart Corp. Sec. Litig., 130 F.3d 309, 315 (8th Cir. 1997); Lone Star Ladies Inv. Club v. Schlotzsky's Inc., 238 F.3d 363, 368 (5th Cir. 2001).

56. 550 U.S. 544 (2007).

57. 556 U.S. 662 (2009).

58. *See* 15 U.S.C. § 78u-4(b)(1) (2012).

59. 15 U.S.C. § 78j(b) (2012); 17 C.F.R. § 240.10b-5 (2012).

60. Cornerstone Research, Securities Class Action Filings: 2015 Year in Review 8 (2016).

61. It should be noted that there is another section of the Exchange Act, section 9(e), that establishes a cause of action against those who engage in manipulative practices with regard to trad-

SEC Rule 10b-5 is similarly broadly worded and far-reaching, and is often pleaded interchangeably. This guide refers to claims brought under either section 10(b) or SEC Rule 10b-5 as "10(b)" claims or actions. Even when plaintiffs base their allegations on other provisions in the securities laws, they will often include a 10(b) claim for good measure.

Because 10(b) claims are so common, because many of the issues they raise are also found in other securities suits, and because the case law itself often looks at other causes of action through a 10(b) lens, this guide offers an expanded treatment of 10(b) claims here, before discussing other causes of action.

Different circuits parse the elements of a 10(b) claim slightly differently, but essentially those bringing the suit must allege and prove that a defendant, in connection with the purchase or sale of securities,

1. made a misrepresentation or omission
2. of a material fact,
3. with scienter,
4. that the plaintiff relied on and
5. that caused injury to the plaintiff.

1. Misrepresentations or Omissions

A 10(b) claim must be premised on a false statement, often called a misstatement or misrepresentation in the case law, or an omission. Courts and the SEC have spent much time assessing the actionability of statements about the future, known as forward-looking statements. Frequently, if a company's prediction does not come true, a lawsuit follows. The law recognizes that a statement about the future implies that the speaker has a good-faith belief that it will be accurate, and if this is not true, 10(b) liability may attach. However, lawmakers are also sensitive to the fact that companies should not be held liable for a twist of fate they had no means of predicting and no duty to warn investors of.

The PSLRA partially addressed these concerns by providing a safe harbor for forward-looking statements when either (a) the statement is "accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement" or (b) the plaintiff fails to prove the statement "was made with actual knowledge by [the speaker] that the statement was false or misleading."[62] Courts have used the PSLRA safe harbor to find that certain forward-looking statements are not actionable as a matter of law, allowing for claims to be adjudicated at the motion to dismiss or summary judgment stage.

Most circuits have read the first prong of the PSLRA safe harbor provision to mean that forward-looking statements with the requisite cautionary language are not actionable regardless of the state of mind of the speaker, the Fifth Circuit be-

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ing of exchange-listed securities. However, because manipulation is defined narrowly, and because a showing of willfulness is required, plaintiffs prefer to bring such claims under Rule 10b-5.

62. 15 U.S.C. § 78u-5(c) (2012).

ing the notable exception.[63] Congress's inclusion of the phrase "actual knowledge" in the second prong of the safe harbor provision has been understood to mean that forward-looking statements made recklessly are still included in the safe harbor, making the mental element required for forward-looking statements higher than the general scienter requirement for statements about current matters (discussed in Part VII.A.3, *infra*).[64]

The safe harbor developed in part from aspects of previously promulgated SEC rules that carved out exceptions for certain forward-looking statements so long as it was not shown that the statements were made lacking "a reasonable basis or w[ere] disclosed other than in good faith."[65] The safe harbor was also informed by the "bespeaks caution" doctrine first applied to the securities laws in *Luce v. Edelstein*.[66] The PSLRA safe harbor does not eliminate these other defenses, and courts still do look to them, particularly in non–class action cases. Judges should bear in mind, however, that the SEC rules require a deeper factual inquiry than the PSLRA safe harbor provision, making them difficult to apply before discovery. Additionally, judicial treatment of the "bespeaks caution" doctrine in particular varies widely between circuits, making the PSLRA safe harbor provision much easier to apply consistently.

As for omissions, a defendant cannot be found liable for omitting information unless there is a duty to disclose the information.[67] Judges interviewed for this guide stated that assessing what gives rise to a duty to disclose is often one of the most difficult issues they encounter. A duty can result from specific reporting requirements, as well as instances in which disclosure of certain facts is required to make a statement complete and not misleading. A disclosure duty can also arise after the fact: If a defendant later finds out that his or her statement was false or misleading, or subsequent events render it so, the defendant must correct or update the original statement if not doing so renders it materially misleading.

2. Materiality

Only misrepresentations and omissions of *material* facts are actionable under section 10(b) or SEC Rule 10b-5. A fact is material "if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding" whether to purchase a security, or if inclusion of the omitted fact would have altered the "total mix" of information available to investors.[68] Materiality is an objective measure, not specific to the particular plaintiff, and is a mixed question of law and fact.

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63. *See* Lormand v. US Unwired, Inc., 565 F.3d 228, 244 (5th Cir. 2009).

64. *See, e.g.,* Inst. Investors Grp. v. Avaya, Inc., 564 F.3d 242, 274 (3d Cir. 2009).

65. Two rules containing the same language offered the safe harbor under both the Securities Act and the Exchange Act: 17 C.F.R. § 230.175(a) (2011) and 17 C.F.R. § 240.3b-6(a) (2011).

66. 802 F.2d 49, 56 (2d Cir. 1986). The "bespeaks caution" doctrine provides that sufficient cautionary language renders alleged misrepresentations or omissions immaterial.

67. *See* Basic, Inc. v. Levinson, 485 U.S. 224, 239 n.17 (1988).

68. *See id.* at 231–32 (internal quotation marks and citations omitted).

At the motion to dismiss stage, judges have the option of deferring the issue of materiality, but they may also use it as grounds for dismissal, particularly for those classes of information that have been held to be immaterial as a matter of law. These classes include (a) puffing, or vague statements of optimism, and (b) opinions, if honestly held.[69] Furthermore, in assessing materiality, judges must consider not only the type of information being communicated, but also the degree; alleged misrepresentations or omissions that are relatively small quantitatively are probably not material.[70]

The materiality of a misrepresentation or omission often depends heavily on specific industry standards. Judges may need to acquire information in the relevant field through outside research or use of expert witnesses to resolve such issues.

3. Scienter

Section 10(b) claims require a showing that the defendant acted with scienter. Scienter connotes "intentional or willful conduct," a more serious mental element than mere negligence.[71]

While Federal Rule of Civil Procedure 9(b) allows conditions of a person's mind to be alleged generally, a showing of scienter is subject to heightened pleading requirements under the PSLRA; plaintiffs must plead "with particularity facts giving rise to a strong inference" of scienter.[72] The legislation does not define "strong inference," so in 2007 the Supreme Court clarified that in the face of competing possible inferences, "[a] complaint will survive . . . only if a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged."[73] The Court advised lower courts to conduct a "holistic[]" assessment of all the relevant facts alleged, including those not necessarily in the complaint itself.[74]

Unfortunately, there is very little consistency between the circuits regarding precisely what scienter entails and what pleadings satisfy the required level of specificity. In particular, courts have grappled with to what extent reckless behavior constitutes scienter, a question renewed in the wake of the PSLRA's passage. Every court of appeals to consider the issue has concluded that recklessness can satisfy a scienter showing, but each one has also developed its own formulation. The Third Circuit, for instance, has held that recklessness "for purposes of a Rule 10b-5 claim . . . involve[es] . . . an extreme departure from the standards of ordinary care."[75] The Second Circuit has required "conscious recklessness—i.e., a

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69. See the discussion of section 11 claims in Part VII.C.1, *infra*, for additional information on the actionability of opinions.

70. *See, e.g.,* Parnes v. Gateway 2000, Inc., 122 F.3d 539, 546–47 (8th Cir. 1997).

71. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199 (1976).

72. 15 U.S.C. § 78u-4(b)(2) (2012).

73. Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 324 (2007).

74. *Id.* at 326.

75. Belmont v. MB Inv. Partners, Inc., 708 F.3d 470, 493 (3d Cir. 2013) (internal quotation marks and citations omitted).

state of mind approximating actual intent."[76] The Ninth Circuit has held that "mere recklessness" is not sufficient, but "deliberate recklessness" that "reflects some degree of intentional or conscious misconduct" is.[77] Judges should therefore be cautious about looking beyond their own circuits for guidance when confronting issues of scienter and should pay particular attention to whether holdings within their circuit qualify the type of recklessness necessary to state a 10(b) claim.

The scienter requirement also raises some thorny issues when there are multiple defendants. Courts are currently divided on whether group pleading (the presumption that officers and directors are collectively responsible for certain types of alleged misstatements) is allowed in light of the PSLRA's heightened pleading standards, particularly its requirement that statements or omissions be pled "with particularity" against each defendant.[78] Courts also disagree on whether they will allow a "collective scienter" theory at the pleading stage. Under certain factual circumstances, courts have allowed a complaint to survive a motion to dismiss even when it does not identify a specific person with the requisite fraudulent intent, but only a corporate defendant.[79]

4. Reliance and Loss Causation

The final elements of a 10(b) claim are (a) a showing that plaintiffs relied on the material misrepresentation or omission and (b) a showing that they were damaged as a result. Reliance and loss causation are separate showings, but terminology in the case law can make this confusing. First, plaintiffs must show that the defendants' fraud caused them to buy or sell securities; this is referred to as *reliance* or *transaction causation*. Second, plaintiffs must show that the fraud (and not some other factor) caused their loss or damage; this is referred to as *causation* or *loss causation*.

a. Reliance

One extremely popular way to plead reliance is based on what is called the "fraud-on-the-market" theory. It is a presumption based on the idea that in an efficient market, a security's price accurately reflects all material information publicly available. Someone who purchases or sells a security relies on the accuracy of the security's price as reflecting all available material information. By extension, any public material misrepresentation or omission that may exist will affect the secu-

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76. Novak v. Kasaks, 216 F.3d 300, 312 (2d Cir. 2000) (internal quotation marks and citations omitted).

77. WPP Luxembourg Gamma Three Sarl v. Spot Runner, Inc., 655 F.3d 1039, 1051 (9th Cir. 2011) (internal quotation marks and citations omitted).

78. Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 326 n.6 (2007) (noting circuits' disagreement).

79. *See, e.g.,* Teamsters Local 445 Freight Div. Pension Fund v. Dynex Cap. Inc., 531 F.3d 190, 195–96 (2d Cir. 2008).

rity's price; therefore, by trading in the security, the plaintiff has effectively relied on the fraud. The Supreme Court articulated the theory in *Basic Inc. v. Levinson.*[80]

The fraud-on-the-market theory is a rebuttable presumption. If a defendant can show that the security's price was not causally linked to the misrepresentation or omission, or that the plaintiffs were somehow aware of the truth and traded in the security anyway, the causal chain will be broken and the plaintiffs will not have proven their case.

The fraud-on-the-market theory has been the subject of some criticism in the economic community, particularly in the wake of the 2008 financial crisis. In 2014, the Supreme Court had the opportunity to revisit the theory in *Halliburton Co. v. Erica P. John Fund, Inc.*,[81] but did not significantly modify its precedent. The Court did hold, however, that in class action suits, defendants would be allowed to offer evidence against the presumption at the class certification stage, rather than waiting until summary judgment or trial.

b. Loss causation

Loss causation, the second causal element of a 10(b) claim that must be shown, is a simple concept: The harm plaintiffs suffer must have a causal connection to the defendant's culpable actions. Successfully pleading and proving loss causation, however, can be challenging. Judges interviewed for this guide stated that most 10(b) actions they encounter rise or fall on either scienter or loss causation.

Most courts of appeals have held that it is not sufficient for plaintiffs simply to allege a disparity between the price paid for a security and its true value. Instead, plaintiffs must plead and offer evidence showing that disclosure of the information the defendants allegedly omitted or misstated caused a drop in the security's value once disclosed.[82] This requirement ensures that 10(b) actions aren't used to help investors recover *any* decline in market value; instead, they compensate only those who suffered an actual loss as a result of fraud. Proving loss causation in the class action context almost always involves the plaintiffs enlisting an expert to conduct an event study, a statistical analysis assessing how the alleged misrepresentations and corrective disclosures affected price changes.

B. Insider Trading Actions

Insider trading actions are among the most prominent brought under the securities laws today. Consequently, they are likely to have more governmental focus and to receive more public scrutiny than other cases. Because they involve individuals rather than companies, they are also more likely to go to trial.

Insider trading is understood to be a type of securities fraud proscribed by section 10(b) and SEC Rule 10b-5. Insider trading liability in the securities laws is

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80. 485 U.S. 224 (1988). The Supreme Court expressed a corollary presumption for omissions in *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972), which is known as the *Affiliated Ute* presumption.

81. 134 S. Ct. 2398 (2014).

82. *See* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 344–45 (2005).

premised on two main theories. The first is the traditional or "classical theory," which focuses on a "corporate insider [who] trades in the securities of his corporation on the basis of material, nonpublic information."[83] This theory is based on a fiduciary duty the insider has to the corporation's shareholders that information be used for the corporation's benefit, and not the individual's. Insiders with such information must either disclose it at the point of trade or abstain from trading.

The second theory, the "misappropriation theory" of insider trading, targets those outside the company who are provided with information in a position of trust and who then use it for personal gain. These outsiders owe a duty to the source of the information, and individuals in such a position are expected to either disclose the information at the point of trade or abstain from trading.[84] This theory, which is newer than the classical theory, has gained widespread acceptance in the last two decades.

One important developing area of law in the insider trading context is tipper/tippee liability. Courts are examining when someone who provides confidential nonpublic information (a "tipper") to someone else who then trades on it (a "tippee") can be found liable. In *United States v. Newman*,[85] the Second Circuit interpreted a series of Supreme Court cases to conclude that certain showings are necessary for tipper/tippee liability, including that tippees either must have known or should have known that the tipper received a consequential personal benefit from sharing the information. The Ninth Circuit, in the recent case *United States v. Salman*,[86] disagreed, holding instead that if the tippee was a close friend or family member of the insider, no proof of other personal benefit was necessary. The Supreme Court granted certiorari in *Salman* and heard the case in its October 2016 term.[87]

In addition to insider trading allegations brought as 10(b) claims, section 20A of the Exchange Act establishes a distinct private cause of action. Investors who traded contemporaneously with traders "in possession of material, nonpublic information," where the trades occurred in the opposite direction in the same class of securities (i.e., the insiders bought and the investors sold, or vice versa) can bring suit.[88] "Contemporaneous" is not defined, and the assessment is generally left to the district courts. Section 20A requires that a predicate violation of the Exchange Act be pleaded, and most often plaintiffs plead a section 10(b) violation as the predicate. Courts are in disagreement regarding whether plaintiffs may pursue section 10(b) and section 20A insider trading claims simultaneously; some have held that doing so would undermine section 20A's damages limitations.[89]

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83. *See* United States v. O'Hagan, 521 U.S. 642, 651–52 (1997).

84. *See id.* at 652–53.

85. 773 F.3d 438 (2d Cir. 2014).

86. 792 F.3d 1087 (9th Cir. 2015).

87. Salman v. United States, 136 S. Ct. 899 (mem.) (Jan. 19, 2016). At the time of this publication, a decision is still pending.

88. 15 U.S.C. § 78t-1 (2012).

89. *See, e.g.,* Gordon v. Sonar Capital Mgmt. LLC, 962 F. Supp. 2d 525, 532 (S.D.N.Y. 2013) (allowing alternative pleading); T. Rowe Price New Horizon Fund, Inc. v. Preletz, 749 F. Supp. 705,

C. *Other Specific Causes of Action*

This section outlines other commonly used or otherwise noteworthy causes of action under the securities laws. Causes of action are referred to by their popular names and arranged in the order in which they appear in the securities laws. Like other sections of the guide, this section is not meant to be exhaustive. Its purpose, rather, is to provide a basic lay of the land of securities litigation, which can provide judges with context for whatever specific issues they may encounter.

1. Section 11 of the Securities Act

Section 5 of the Securities Act outlines registration requirements for securities.[90] Section 11 of the Securities Act establishes a private cause of action for registration statements that contain false or misleading information.[91] Registration statements actionable under section 11 must contain, at the time they became effective, (a) an untrue statement of a material fact or (b) an omission of a material fact required under law or necessary to make the statement not misleading. Section 11 does not include reliance or loss causation as elements; in this, it is broader than other so-called antifraud provisions of the securities laws. Scienter is not an element of a section 11 claim, though information about a defendant's mental state may be relevant for certain affirmative defenses, as discussed below.

The materiality standard for section 11 claims is essentially the same as that for 10(b) claims, and as they do in the 10(b) setting, judges have the option of deferring the question of materiality at the motion to dismiss stage or granting the motion if materiality is not present as a matter of law. For example, courts frequently have found that a statement was not material under the "bespeaks caution" doctrine. There is also a statutory good-faith defense, which is the most popular defense for such actions; if defendants can show they had reasonable grounds for believing, and did in fact believe, that there was no omission or material misstatement, they are not liable.[92] In addition, the SEC, in line with its policy to encourage broad disclosure about future plans, promulgated SEC Rule 175, which provides an additional safe harbor for forward-looking statements.[93]

There had been a circuit split on the question of what plaintiffs needed to allege in connection with statements of opinion in section 11 actions. In 2015, the Supreme Court shed some light on how statements of opinion might be actionable under section 11 in *Omnicare, Inc. v. Laborers District Council Construction Industry Pension Fund*.[94] The Court held that if an opinion is stated and honestly held, if it contains no embedded facts that are shown to be false, and if it includes enough facts to prevent the opinion from being misleading, then there is probably

709–10 (D. Md. 1990) (prohibiting alternative pleading). Section 20A claim damages are statutorily capped at the defendant's gain (or avoided loss).

90. 15 U.S.C. § 77e (2012).

91. 15 U.S.C. § 77k (2012).

92. 15 U.S.C. § 77k(b)(3) (2012). SEC Rule 176, 17 C.F.R. § 230.176 (2011), offers some factors to consider.

93. 17 C.F.R. § 230.175 (2011).

94. 135 S. Ct. 1318 (2015).

no basis for liability, even if the opinion is later proved wrong. The Court left to the district court the task of analyzing these issues in the context of a motion to dismiss, making it likely that different approaches will continue to be used as case law develops.

As outlined in Part VI, *supra*, judges may also encounter some disagreement over whether section 11 claims sounding in fraud are subject to the heightened pleading standards of Federal Rule of Civil Procedure 9.

2. Section 12(a)(1) of the Securities Act

Section 12(a)(1) of the Securities Act creates a private cause of action for the offer or sale of unregistered securities.[95] "The registration requirements are the heart of the Act, and [section] 12[(a)](1) imposes strict liability for violating those requirements."[96] Unlike many other causes of action under the securities laws, section 12(a)(1) liability does not require a finding of materiality, nor of scienter, nor even of negligence. The purchaser can either recover damages or have the purchases rescinded, depending on whether the purchaser still owns the securities at issue. There are three elements that must be shown:

1. the defendant offered to sell or sold a security to the plaintiff;
2. the defendant used the mails or an instrument of interstate commerce; and
3. the defendant did not comply with the registration or prospectus requirements of section 5.

Once the prima facie case is shown by the plaintiff, the burden of proof shifts to the defendant to show that the elements of the violation do not exist or that an exemption or exception applies. These arguments will rely heavily on the statutory definitions of terms like *person*, *offer*, and *sold*, which appear in section 2 of the Securities Act, as well as on the safe harbor provisions and other statutory exemptions to section 5, which appear in sections 3 and 4.[97] Defendants may also point to the statute's privity requirements, which the Supreme Court addressed in *Pinter v. Dahl*,[98] or make an *in pari delicto* defense, that is, that the plaintiffs' wrongdoing outweighs their own.[99]

There is some case-law inconsistency concerning the limitations provisions that govern section 12(a)(1) claims. Actions under section 12(a)(1) must be brought within one year of the purported violation, and the Securities Act bars actions brought more than three years after the security is offered bona fide to the

95. 15 U.S.C. § 77l(a)(1) (2012). This was originally section 12(1) of the Securities Act and will be so labeled in cases predating the PSLRA.

96. Pinter v. Dahl, 486 U.S. 622, 638 (1988).

97. Sections 2–5 of the Securities Act are codified at 15 U.S.C. §§ 77b-e (2012 & Supp. III 2015).

98. 486 U.S. 622 (1988).

99. While there once were courts that held that the *in pari delicto* defense was not available for section 12(a)(1) violations because of their strict liability nature, the Supreme Court has held that the defense is available for all private actions brought under the federal securities laws. *See Pinter*, 486 U.S. at 633–35. That being said, because of the restricted nature of the defense allowed under *Pinter*, it is not used frequently.

public. Courts have disagreed on whether equitable tolling can be applied to the limitations provisions, and if so, how, as well as when the bona fide offer occurs in the non-registration context. For more information on time limitations provisions, see Part IX, *infra*.

3. Section 12(a)(2) of the Securities Act

Section 12(a)(2) of the Securities Act creates a cause of action against those who have offered or sold securities by means of a prospectus or oral communication that contains material misrepresentations or omissions.[100] This cause of action is similar to a section 12(a)(1) claim, but more complicated because of the requirement to show materiality. The elements are as follows:

1. the defendant offered to sell or sold a security to the plaintiff;
2. the defendant used the mails or an instrument of interstate commerce;
3. the defendant used a prospectus or oral communication; and
4. the prospectus or oral communication contained an untrue statement or omission of material fact of which the purchaser was not aware.

The materiality element, absent from section 12(a)(1)'s elements, is similar to the section 11 requirement and involves similar issues regarding statutory scope. Although the Supreme Court has not weighed in on whether claims sounding in fraud are subject to the heightened pleading standards of Federal Rule of Civil Procedure 9, every court of appeals to address the issue in a section 12(a)(2) claim has held that Rule 9 applies.

As in section 12(a)(1) cases, in section 12(a)(2) cases, once the prima facie case is shown by the plaintiff, the burden of proof shifts to the defendant. And again, many of the available defenses focus on how various terms are defined by statute and interpreted by courts. In addition, section 12(a)(2) offers a defense for those who "did not know, and in the exercise of reasonable care could not have known, of [the] untruth or omission."[101] In other words, if defendants can prove an absence of negligence, they avoid liability.

Reliance and loss causation are not elements of a section 12(a)(2) claim; instead, they are statutory affirmative defenses. Courts have dismissed claims when defendants proved that the plaintiff knew of the misrepresentation or omission before the purchase. The statute also states that losses not caused by the misrepresentation or omission are not recoverable.[102] Some courts have taken this further, requiring that the pleading include some causal connection between the defective communication and the purchaser's loss. Finally, as with section 12(a)(1), with section 12(a)(2), there is some case-law inconsistency concerning the time limitations provisions that attach to the action.

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100. 15 U.S.C. § 77l(a)(2) (2012). Again, this was originally section 12(2) of the Securities Act and will be so labeled in cases predating the PSLRA.

101. 15 U.S.C. § 77l(a)(2) (2012).

102. 15 U.S.C. § 77l(b) (2012).

4. Section 17(a) of the Securities Act

Section 17(a) of the Securities Act prohibits fraud, material misstatements, or omissions in connection with the offer or sale of securities.[103] In a sense, it is the Securities Act's equivalent of section 10(b), and similarly broad. Most courts have held that there is no private right of action under this section and the Supreme Court has reserved the issue several times, so judges will most likely see this section in actions brought by the SEC. The main advantage that section 17(a) has over section 10(b) from the SEC's perspective is that many section 17(a) claims can be premised on negligent conduct rather than requiring a showing of scienter.[104]

5. Proxy Litigation—Section 14(a) of the Exchange Act

Prior to an annual meeting, a corporation is required to provide shareholders with a proxy statement that contains information about the issues that will be voted on at the meeting. Corporations also frequently solicit proxies (essentially absentee votes) from shareholders on specific items on the agenda. Section 14(a) of the Exchange Act governs the form of the proxy statement, as well as solicitation of proxy votes from shareholders, so as to safeguard fair corporate suffrage.[105]

Proxy litigation has increasingly been used in struggles for control over publicly traded corporations, as well as to contest the elections of boards of directors and to recommend changes to articles of incorporation. Actions under section 14(a) often request not only damages, but also an injunction to bar further action using the proxies at issue. Since proxy litigation most often occurs in the context of mergers or change of control transactions, section 14(a) cases are the ones most likely to be time sensitive. See Part V.A, *supra*, on temporary restraining orders and preliminary injunctions, for suggestions on how to manage these cases when they are first filed.

Section 14(a) authorizes the SEC to adopt rules for the solicitation of proxies, consents, and authorizations. These rules detail the type of information shareholders can expect to receive and prohibit false or misleading statements in the solicitation of proxies. Rule 14a-9 prohibits the making of any false or misleading statement in the solicitation of proxies.[106] To state a claim, a plaintiff must allege

1. a misrepresentation or omission of a material fact;
2. that the misrepresentation was negligent or willful; and
3. that the proxy solicitation itself (not the specific representation) was an "essential link" in accomplishing the proposed corporate transaction.[107]

The pleading requirements concerning misrepresentation are similar to those for section 11 claims. However, proxy statements are essentially arguments in

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103. 15 U.S.C. § 77q(a) (2012).
104. *See* Aaron v. SEC, 446 U.S. 680, 695–97 (1980).
105. 15 U.S.C. § 78n(a) (2012).
106. 17 C.F.R. § 240.14a-9 (2011).
107. Mills v. Elec. Auto-Lite Co., 396 U.S. 375, 385 (1970).

furtherance of a specific position, and therefore, by nature, they have a complicated combination of facts, opinions, and conclusions. Judges will often be tasked with determining which statements are sufficiently factual to be actionable and whether they rise to the level of materiality.[108] Section 14(a)'s "essential link" requirement is unique among causes of action under the securities laws.

The law is somewhat muddy concerning the mental element of section 14(a) claims. For example, although there is nearly unanimous authority in lower courts that negligence is the standard of liability for section 14 claims, the Supreme Court has never ruled on the issue.[109] This leaves open the possibility that for certain types of proxy fraud claims, a higher standard is required. For instance, the Sixth and Eighth Circuits have held that scienter should be the standard of liability for section 14(a) defendants who are outside advisors to a company's board; the Third Circuit has disagreed.[110] Similarly, there is disagreement among the circuits regarding whether the PSLRA's particularity requirements apply to a negligence pleading.

Because the right to sue under section 14(a) is an implied right, there is no explicit statute of limitations. Courts have held that the time to sue under section 14(a) generally should be the same as that under section 10(b) before its modification by the Sarbanes-Oxley Act, that is, within one year of discovering the facts constituting the violation and no more than three years after the violation.

6. The Williams Act—Sections 13–14 of the Exchange Act

The Williams Act, passed by Congress in 1968, inserted additional subsections into sections 13 and 14 of the Exchange Act. The Williams Act was a response to the increasing use of cash tender offers—where an offeror publicly requests shares at a fixed price—to achieve control of unwilling companies. Before the Act, a cash tender offer was an effective way to avoid the Exchange Act's usual requirements for mergers, which included a shareholder vote.

The Williams Act is decidedly neutral on whether cash tender offers are "bad" or "good" as a policy matter, but it makes such offers subject to disclosure requirements. Because the Williams Act is not meant to benefit or protect incumbent management, suits are usually brought by the target company on behalf of its shareholders, purportedly asserting the shareholders' rights.[111]

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108. *See, e.g.,* Va. Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1090–91 (1991).

109. Some courts have read the Supreme Court's holding in *Aaron v. SEC*, 446 U.S. 680, 697–700 (1980), which discusses actions brought under section 17(a) of the Securities Act, to apply analogously to section 14.

110. *See* Adams v. Standard Knitting Mills, Inc., 623 F.2d 422, 428–31 (6th Cir. 1980); SEC v. Shanahan, 646 F.3d 536, 546–47 (8th Cir. 2011); Herskowitz v. Nutri/Sys., Inc., 857 F.2d 179, 189–90 (3d Cir. 1988).

111. *See* Daniel J. Kramer et al., Federal Securities Litigation: A Deskbook for the Practitioner 7-1 to 7-2 (3d ed. 2014).

a. Section 13(d) litigation

There are two main types of litigation under the Williams Act. The first type is brought under section 13(d) of the Exchange Act,[112] which requires anyone acquiring beneficial ownership of more than 5% of certain securities to file with the SEC and send a schedule to the issuer with specified information. This requirement serves as an early warning to investors and company management that a takeover attempt may be under way. Section 13(d) suits allege that the disclosure information provided is false, misleading, or otherwise defective. There are no reliance or materiality requirements in such a claim. Though purportedly section 13(d) litigation is brought with shareholders' interests in mind, as a practical matter, managers often use section 13(d) to stall or block tender offers regardless of whether they would benefit shareholders.

It should be no surprise that most section 13(d) claims request injunctive relief to halt further tender offer activities. See Part V.A, *supra*, on temporary restraining orders and preliminary injunctions, for guidance on the initial management of such requests. The Supreme Court has made it clear that a technical violation of section 13(d) is not sufficient to justify an injunction,[113] so judges should be wary of arguments that point to the policy concerns of the Williams Act to justify findings of per se irreparable harm. Judges should also consider whether additional disclosure that brings the schedule in line with section 13's requirements and alerts shareholders to the nature of the dispute (for instance, by annexing the complaint) would be sufficient relief; Second Circuit courts have been particularly open to this option.[114]

b. Section 14(d) litigation

The second main type of Williams Act litigation comes under section 14(d) of the Exchange Act,[115] which prohibits anyone from making a tender offer that would result in their owning more than 5% of the issuer's shares without first filing the offer with the SEC, as well as a statement with information similar to that required under section 13(d). Section 14(d) also regulates the substance of tender offers and sets certain time limits for withdrawal.

"Tender offer" is not defined by statute or by the SEC, so one issue courts often confront in section 14(d) actions is whether a tender offer has occurred. *Wellman v. Dickinson*[116] lays out eight factors the SEC has listed as characteristic of a tender offer, but courts have consistently declined to declare those factors mandatory for finding that a tender offer has occurred.

Typically, section 14(d) actions are brought by the target company, which alleges that the raider (the company seeking to acquire the target, also referred to as a bidder) has made a tender offer without the requisite filings or that the filings

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112. 15 U.S.C. § 78m(d) (2012).
113. *See* Rondeau v. Mosinee Paper Corp., 422 U.S. 49, 60–61 (1975).
114. *See* Kramer et al., *supra* note 111, at 7-16 to 7-19.
115. 15 U.S.C. § 78n(d) (2012).
116. 475 F. Supp. 783, 823–24 (S.D.N.Y. 1979).

are faulty. Raiders have also been known to file suit under section 14(d) when there are competing tender offers, using the lawsuit to attack other bidders' statements as faulty or inadequate and insisting on additional disclosure. Suits by shareholders themselves are rare, but not unheard of. As with section 13(d) actions, with section 14(d) actions, injunctions are often the relief requested.

7. Section 16—Short Swing Profits

Section 16 of the Exchange Act includes a cause of action intended to prevent "short swing" trading, in which corporate insiders use access to nonpublic information to engage in short-term trading for profit.[117] The section enables issuers of securities to recover such profits from "insiders" (defined by statute) who both purchase and sell (or sell and purchase) equity securities within a six-month period. Unlike insider trading actions (discussed in Part VII.B, *supra*), which require an inquiry into the insider's knowledge or intent, section 16 is strict liability, with no mental element requirement.

Section 16 does not share many issues with other sections of the securities laws. Note also that there cannot be double recovery for the same transaction if a defendant is found liable under both section 16 and another provision of the securities laws. Finally, section 16's case law, like that of other sections, has been prone to frequent change with regard to the tolling of the applicable limitations provisions.

8. Section 18—Liability for False Filings

Section 18 of the Exchange Act establishes a cause of action for investors who are injured by false or misleading statements in documents filed with the SEC or another national securities exchange.[118] Section 18 claims are relatively rare compared with 10(b) claims, in part because unlike 10(b) claims, section 18 claims cannot be premised on a fraud-on-the-market theory, and therefore reliance must be pleaded with particularity.[119]

VIII. Secondary Liability

One of the fastest moving areas of law in securities litigation is secondary liability: whether and how individuals and corporations not principally or directly involved in the alleged violation can be held responsible. Private plaintiffs and government entities alike regularly conceive new theories of secondary liability, which are met with varying degrees of acceptance by different courts. In addition, congressional amendments to the securities laws frequently involve issues of secondary liability. This part offers an overview of how traditional theories of secondary liability have been used in securities litigation, with the caveat that judges should be sensitive to the current laws in their particular court.

117. 15 U.S.C. § 78p (2012).
118. 15 U.S.C. § 78r (2012).
119. *See* Kramer et al., *supra* note 111, at 9-1 to 9-2.

An important case that does not fall into a single theory of secondary liability is *Janus Capital Group, Inc. v. First Derivative Traders.*[120] In that case, the Supreme Court held that only "the person or entity with ultimate authority over [a] statement" could be held primarily liable for securities fraud based on that statement.[121] *Janus* has proven to be important in assessing not only individuals' liability (including that of corporate officers to whom statements are not implicitly attributed), but also liability in situations in which statements are issued by multiple entities.

A. Aiding and Abetting Liability

Congress authorized the use of aiding and abetting liability in SEC-brought actions under both the Securities Act and the Exchange Act. Dodd-Frank confirmed that the SEC has the power to bring claims against "any person that knowingly or recklessly provides substantial assistance to another person in violation of a provision."[122] Courts generally agree that to establish aiding and abetting liability, there must be (a) a primary violation of the securities laws, (b) some general awareness on the part of the aider or abettor that his or her role was part of an overall plan of wrongdoing, and (c) knowing and substantial assistance.

The Supreme Court, in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, held that private parties cannot maintain an aiding and abetting lawsuit under section 10(b) of the Exchange Act.[123] Courts have read this decision as foreclosing aiding and abetting suits by private parties under other sections of the securities laws as well.

B. Control Person Liability

Both the Securities Act and the Exchange Act contain language providing for control person liability for violations of the federal securities laws.[124] Liability is derivative, meaning there must be a primary violation and a control relationship for liability to attach, but the primary violator need not be made a party to the action. The primary violator can be either a natural person or a legal entity (like a corporation). A control person defendant's liability is joint and several with the primary violator's. Depending on the underlying offense, a control person found liable might be able to sue for contribution even if the primary violator is not named in the suit.

Because *control* is not defined anywhere in the statutes,[125] there is a great deal of disagreement concerning the pleading and proof requirements for control person liability. Some courts, for instance, require proof that the control person was a

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120. 1565 U.S. 135 (2011).

121. *Id.* at 142.

122. 15 U.S.C. § 77o(b) (2012); 15 U.S.C. § 78t(e) (2012).

123. 511 U.S. 164 (1994).

124. *See* 15 U.S.C. § 77o(a) (2012); 15 U.S.C. § 78t(a) (2012).

125. SEC Rule 405, 17 C.F.R. § 230.405 (2016), does offer a definition of *control* as "the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person."

"culpable participant" in the alleged illegal activity for liability to attach. Others hold that this showing is not part of a plaintiff's primary case, but that good faith is available to the defendant as an affirmative defense.[126] When construing the control person statutes, courts generally focus on both the actual exercise of control in the specific instance and the general power to control.

There are a number of statutory affirmative defenses offered for control person defendants, most significantly the Exchange Act's good faith defense.[127] The language of the good faith defense is absent from the Securities Act provision (which instead has a defense for lack of knowledge), making case law of each Act harder to analogize to that of the other. Other sections of the securities laws may also have relevant affirmative defenses in the control person setting. For instance, the Exchange Act precludes imposing liability for insider trading on someone solely because he or she employed an individual who engaged in it.[128]

C. Respondeat Superior

The common law doctrine of *respondeat superior* is similar, but not identical, to the control person liability appearing in the securities statutes. The courts of appeals are split on whether common law theories of vicarious liability can also be pleaded under the securities laws (and to which underlying offenses they might attach).

Proponents of concurrent liability point to the securities statutes' silence on being the exclusive means for finding vicarious liability and the presence of saving clauses in each statute providing that "[t]he rights and remedies provided by this [law] shall be in addition to any and all other rights and remedies that may exist at law or in equity."[129] Proponents of exclusive liability focus on statutory purpose, noting that the securities statutes generally impose liability only on persons who are to some degree culpable, an issue that common law *respondeat superior* does not address.

IX. Time Limitations Provisions

Time limitations provisions in the securities laws are usually two-fold: A shorter limitations period is linked to the violation or its discovery, and a longer one runs from the underlying transaction. These provisions are sometimes referred to as a "statute of limitations" and a "statute of repose," respectively, but that terminology remains a point of contention in many instances.

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126. *See, e.g.,* Ganino v. Citizens Utils. Co., 228 F.3d 154, 170 (2d Cir. 2000) (requiring culpable participant as part of prima facie case); Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1574–75 (9th Cir. 1990) (en banc) (once a plaintiff establishes control, burden shifts to the defendant to establish good faith).

127. 15 U.S.C. § 78t(a)(2012).

128. 15 U.S.C. § 78t-1(b)(3) (2012).

129. 15 U.S.C. § 77p (2012); 15 U.S.C. § 78bb(a) (2012).

The Securities Act's limitations provisions appear in section 13.[130] Actions under section 12(a)(1) must be brought within one year of the purported violation. Actions under sections 11 and 12(a)(2) must be brought within one year after the misstatement or omission was discovered or should have been discovered. Section 13 adds that "[i]n no event shall any such action be brought to enforce a liability" created under the Act more than three years after the security was bona fide offered to the public or sold. The Exchange Act does not contain a specific section devoted to limitations periods. Such provisions appear either next to specific causes of action or in other legislation, notably section 804 of the Sarbanes-Oxley Act, which provides limitations periods of two years from discovery or five years from violation for bringing "a private right of action that involves a claim of fraud, deceit, manipulation, or contrivance in contravention of a regulatory requirement concerning the securities laws, as defined in [the Exchange Act]."[131]

Because the limitations provisions affect whether a suit can be brought, they are featured prominently in the case law. Particularly in recent years, this case law has changed quickly, so judges should be vigilant in ensuring that they base their decisions on up-to-date information. For instance, in 2010, the Supreme Court offered a new discovery rule for when the statute of limitations begins to run for section 10(b) claims.[132] Although most district courts that have addressed the issue have agreed that this ruling applies to section 11 claims as well, courts of appeals have yet to rule.[133]

Much of the recent case law regarding limitations provisions centers on class actions. Traditionally, courts have allowed the statutes of limitations for individual class members to be tolled during the pendency of a class action, under principles articulated in *American Pipe v. Utah*.[134] Courts have disagreed, however, over whether those who opt out of a class action can still have their limitations periods tolled.[135] In addition, the applicability of *American Pipe* tolling to securities laws' statutes of repose has been inconsistent in some circuits and unresolved in others. In 2014, the Supreme Court granted certiorari on the question whether the

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130. 15 U.S.C. § 77m (2012).

131. 28 U.S.C. § 1658(b) (2012). By and large, courts have read this provision to apply only to private actions alleging fraud under the Exchange Act, and not as a replacement for section 13 of the Securities Act. *See* Thomas Lee Hazen, Federal Securities Law § 7.10 (Federal Judicial Center, 3d ed. 2011); *see also In re* Exxon Mobil Corp. Sec. Litig., 500 F.3d 189, 197 (3d Cir. 2007) (concluding that Congress intended that the provision only apply to fraud claims within the Exchange Act).

132. Merck & Co. v. Reynolds, 559 U.S. 633, 644–48 (2010).

133. *See, e.g.*, *In re* Bear Stearns Mortgage Pass-Through Certificates Litig., 851 F. Supp. 2d 746, 762 (S.D.N.Y. 2012) (collecting S.D.N.Y. cases); F.D.I.C. v. Countrywide Fin. Corp., No. 2:12-CV-4354 MRP, 2012 WL 5900973, at *3 (C.D. Cal. Nov. 21, 2012) (accepting S.D.N.Y. position). *But see In re* IndyMac Mortgage-Backed Sec. Litig., 793 F. Supp. 2d 637, 648 (S.D.N.Y. 2011) (rejecting the extension of *Merck* to Securities Act claims).

134. 414 U.S. 538 (1974).

135. *See* Renee Choy Ohlendorf, *Growing Divide over Class Action Tolling Under American Pipe*, ABA Litigation News, Feb. 4, 2015, http://web.archive.org/web/20151113162132/ http://apps.americanbar.org/litigation/litigationnews/top_stories/020415-class-action-tolling.html.

section 13 three-year limitations period can be tolled under certain circumstances relating to class action filing,[136] but the Court ultimately concluded that certiorari was improvidently granted and dismissed the case.[137]

X. Damages

Generally, actions under the securities laws are limited to actual damages.[138] However, damages calculations can be quite complex, so they often require considerable judicial attention. In addition, limiting damages to actual damages does not preclude courts from imposing ancillary remedies, such as restitution, rescission, disgorgement, sanctions, and various forms of injunctive relief.

When possible, judges try to avoid nullifying large transactions that have already been completed and instead assign damages to make plaintiffs whole. For instance, if a merger were induced by material misrepresentations or omissions in the proxy materials, a judge might award plaintiff-sellers benefit-of-the-bargain damages rather than undoing the merger itself.

Joint and several liability traditionally governs damages awards, but the PSLRA introduced a rule of comparative fault as a way to counter the practice of plaintiffs including in securities class actions deep-pocketed defendants of questionable blameworthiness. Under this rule, a defendant is only liable according to his or her percentage of responsibility for the wrongdoing, unless "the trier of fact specifically determines that such covered person knowingly committed a violation of the securities laws."[139] This rule applies to contribution actions as well. Also, as explained in the next part, the PSLRA bars contribution claims against parties with whom plaintiffs have settled prior to final verdict or judgment.[140]

XI. Settlement

If a securities suit survives a motion to dismiss, there is a high likelihood that it will settle before summary judgment briefing. Parties face extraordinarily high discovery costs, and particularly in class actions, most litigants prefer the security of a settlement to the risk of protracted litigation and trial.

Settlements in securities suits follow patterns similar to those in other cases. As in other cases, when all litigants are present and involved in the litigation, the judge's role in approving a settlement agreement is relatively straightforward. Judges have a much greater responsibility when assessing settlement agreements for securities class actions, so it is on this set of cases that this part focuses. Part IV

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136. Public Employees' Retirement Sys. of Miss. v. IndyMac MBS, Inc., 134 S. Ct. 1515 (mem.) (2014).

137. Public Employees' Retirement Sys. of Miss. v. IndyMac MBS, Inc., 135 S. Ct. 42 (mem.) (2014).

138. 15 U.S.C. § 78bb(a) (2012).

139. 15 U.S.C. § 78u-4(f)(2)(A) (2012). This rule is subject to some limited exceptions.

140. 15 U.S.C. § 78u-4(f)(7)(A) (2012).

of the FJC's pocket guide *Managing Class Action Litigation*[141] provides most of the fundamental information and guidance. This part is meant to supplement that source, highlighting some securities-specific issues and challenges judges may face.

A. Rulings Earlier in the Case

The knowledge that a case is likely to settle rather than go to trial may factor into certain decisions judges make in earlier phases of litigation. For instance, some judges suggest instructing the parties to discuss the possibility of settlement before the initial Rule 16 conference. Because some parties regard bringing up settlement as a show of weakness, having the judge step in eliminates this concern. Other judges feel strongly that the issue of settlement should not be raised by a judge until after a claim has survived a motion to dismiss. Until a judge has determined that a legal claim has been stated, there is no reason to suggest that parties should settle—though judges can encourage parties to make use of court mediation programs if appropriate or required under local rules.

As mentioned in Part V.B.2, *supra*, on class certification, judges are also sometimes confronted with requests to bifurcate liability and damages issues. If one party's damages case is significantly stronger than its liability case, agreeing to such a bifurcation may put that party into an inferior position for settlement negotiations later on.

B. Notice and Preliminary Approval

Whenever possible, judges suggest raising any potential concerns about the fairness of a settlement agreement before granting preliminary approval, as waiting until the fairness hearing can raise costs tremendously. Judges also suggest scrutinizing the proposed settlement notice that will go to class members. An effective notice should allow an individual with a high school education to read the notice and arrive at an informed decision on the next steps he or she wants to take.

Securities cases often have complicated facts, making a clear and comprehensible notice challenging but essential. The FJC has developed some illustrative notices of proposed class action settlement, which are available on its website.

C. Pending Cases

In assessing whether a settlement amount is reasonable, judges should be aware that pending Supreme Court or court of appeals decisions may affect the parties' calculations. For instance, in 2014, *Halliburton v. Erica P. John Fund*[142] (popularly referred to as "*Halliburton II*") was before the Supreme Court. The case addressed when and how a reliance presumption should be pleaded in section 10(b) class actions, and it had the potential to dramatically alter the class action landscape.

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141. Barbara J. Rothstein & Thomas E. Willging, Managing Class Action Litigation: A Pocket Guide for Judges (Federal Judicial Center, 3d ed. 2010).

142. 134 S. Ct. 2398 (2014).

The opinion was issued in June 2014, and practitioners largely agree that it improved defendants' position in such cases.

The average settlement amount for section 10(b) class actions in the first half of 2014 was $40 million; the average in the second half was $29 million.[143] The change in settlement amounts might be due to a number of factors: to *Halliburton II*'s content, to the greater clarity, to both, or to other circumstances entirely. But it is reasonable to assume that parties that settled in early 2014 did so fully aware of the pendency of *Halliburton II*, and they opted to settle in the contemporaneous legal landscape rather than waiting for an unknown holding. And it would be reasonable for parties to take the case's pendency into account when agreeing to a settlement amount. Plaintiffs may have been willing to settle sooner and for less than they would have otherwise; in this instance, their gamble paid off, since the law turned somewhat against them. A judge looking to approve such a settlement might therefore decide that a settlement number that seems low would still be fair, given the precariousness of the law before a Supreme Court ruling. Because of the infrequency with which the Supreme Court steps in on such matters, cases at the court of appeals level (particularly in the Second and Ninth Circuits) can have a similar effect.

D. Partial Settlements and Scope of Release

The PSLRA has several provisions that affect distribution of damages between defendants and what damages are ultimately awarded. If a settlement only encompasses part of a group of defendants, it may have consequences when calculating damages later on. For example, 15 U.S.C. § 78u-4(f)(7) (2012), titled "Settlement discharge," bars contribution claims against parties with whom plaintiffs have settled prior to the final verdict or judgment, and it imposes a rule of comparative fault, whereby damages awards must be reduced with the settled party's amount in mind.

Judges should review the scope of release for class action settlement agreements to ensure that it is not unreasonably broad. Defendants may push for the incorporation of additional class members or for release from claims that do not necessarily correspond with the case brought, and at this point plaintiffs have less incentive to contest them.

E. Plan of Allocation and Fees

Judges often pay attention to the plan of allocation in private settlements. They check whether the plan is practicable, what happens to unallocated funds, and how attorneys' fees are calculated. Sometimes funds are distributed pro rata once all the claims are in, and sometimes claims are satisfied according to a rubric and anything left over is returned to defendants or donated to a designated charity.[144]

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143. NERA, Recent Trends in Securities Class Action Litigation: 2014 Full-Year Review (2015), at 26.

144. The settlement agreement will often make clear when funds should go to a charity, and which charity or charities. When that is not the case, judges tend to use the *cy pres* doctrine to

When assessing fees, some judges suggest asking for a breakdown of attorney charges by month and type of activity, so that the judge can see which stages of the litigation created the highest costs.

Judges should also be attuned to de minimis provisions or distribution thresholds, as these are often cause for objection. In many instances, the change in a security's price that is due to alleged liable conduct is a matter of pennies, so a de minimis provision of even $10.00 may invalidate the claims of a large number of smaller shareholders. What to do about such provisions is left to the discretion of the district judge, who must weigh the need to encourage the filing of class actions and "preserve the settlement fund from excessive and unnecessary expenses" against the interests of smaller shareholders.[145] In the face of objections, some judges have approved parties' removing the de minimis provision in favor of alternative cost-saving mechanisms; others have allowed the provision to remain.[146]

F. Settlements with the SEC

Traditionally, settlements with the SEC focused on cash payouts rather than admissions of culpability. Defendants were allowed to settle while "neither admitting nor denying" wrongdoing. Some district courts have questioned the appropriateness of such settlements, arguing that without an admission or denial, it is extremely difficult to gauge the fairness of the settlement amount.[147] Most judges still rely on the SEC's status as a public agency as justification for deferring to it to assess what is in the public interest. Judges have fewer reservations about asking that private settlement agreements include information on potential liability and relative merits to help them in their fairness assessment.

Shortly after Mary Jo White assumed her position as chair of the SEC in 2013, she announced that the SEC would demand more admissions of misconduct as part of settlements, particularly in instances of egregious conduct.[148] The policy is still in its early stages, so its effects are unclear. Some commentators have predicted that the policy change will lead to an increase in trials, since defendants will be unwilling to settle if it requires an admission of fault. Others predict that the SEC will turn increasingly to administrative orders (rather than court orders) for

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determine the next best use of remaining funds. In many circuits there is case law that describes the scope of judges' discretion to make such distributions and that outlines what steps must be followed to make an appropriate *cy pres* determination. *See, e.g.*, Masters v. Wilhelmina Model Agency, Inc., 473 F.3d 423 (2d Cir. 2007); *In re* Airline Ticket Comm'n Antitrust Litig., 268 F.3d 619 (8th Cir. 2001).

145. *See In re* Global Crossing Sec. and ERISA Litig., 225 F.R.D. 436, 463 (S.D.N.Y. 2004).

146. *See, e.g.,* Union Asset Mgmt. Holding A.G. v. Dell, Inc., 669 F.3d 632, 640–41 (5th Cir. 2012); Sullivan v. DB Invs., Inc., 667 F.3d 273, 328–29 (3d Cir. 2011).

147. The best-known instance of such a ruling is *SEC v. Citigroup Global Markets, Inc.,* 827 F. Supp. 2d 328 (S.D.N.Y. 2011). The Second Circuit ultimately held that the district court had abused its discretion in withholding approval on the stated grounds. *See* SEC v. Citigroup Global Markets, Inc., 752 F.3d 285 (2d Cir. 2014).

148. James B. Stewart, *S.E.C. Has a Message for Firms Not Used to Admitting Guilt*, N.Y. Times, June 21, 2013, at B1.

settlement approval, which allow the SEC leeway to obtain admissions but to balance them against more concessions to defendants.[149]

SEC settlements may also include an injunction request (see the discussion in Part IV.B, *supra*).

XII. Discovery

For general guidance on discovery issues, judges should consult Chapter 4 of the FJC's *Manual for Complex Litigation, Fourth.*[150] In addition, the FJC has published two pocket guides that address e-discovery: *Managing Discovery of Electronic Information*[151] and *Criminal E-Discovery*.[152]

Under the PSLRA, all discovery in private class actions is supposed to be stayed "during the pendency of any motion to dismiss," absent showings of undue prejudice or a need for particularized discovery.[153] This is an unusual feature of securities class actions, and it covers attached cases as well. Judges frequently opt to extend such stays to earlier than the filing of a motion if a defendant states an intent to file, and through repleadings and reconsiderations of motions after an opinion has been issued.

A. Discovery Scheduling

Judges report that preparing early for discovery scheduling is extremely helpful; otherwise, the cost of discovery can quickly outweigh the value of a case. Many judges request proposed schedules from parties a week before the first discovery conference that list dates, either through to trial or else to summary judgment briefing. Judges often also request materials for any other issues the judge may need to rule on, including proposed confidentiality orders, production issues, and proposed deposition lists. While many judges will rule on all these issues at the initial conference, some judges wait to approve certain discovery requests, particularly the full list of proposed depositions. Judges who follow such practices believe they encourage parties to make better use of early depositions and avoid obstructionist tactics. Such an approach is also in line with the recent amendments to Federal Rule of Civil Procedure 26, which emphasize the need for proportionality in discovery.

Judges have some general recommendations for setting a discovery schedule, but they caution that schedules are very much the product of a case's needs. For

149. *See, e.g.,* James Edward Maloney, *Trends in Enforcement and Recent Developments in Securities Litigation*, *in* Inside the Minds: New Developments in Securities Litigation 19 (2014); Jason E. Siegel, Note, *Admit It! Corporate Admissions of Wrongdoing in SEC Settlements: Evaluating Collateral Estoppel Effects*, 103 Geo. L.J. 433, 455–64 (2015); Gretchen Morgenson, *S.E.C. Wants the Sinners to Own Up*, N.Y. Times, Mar. 15, 2015, at BU1.

150. MCL, Fourth, *supra* note 24.

151. Barbara J. Rothstein, Ronald J. Hedges & Elizabeth C. Wiggins, Managing Discovery of Electronic Information: A Pocket Guide for Judges (Federal Judicial Center, 2d ed. 2012).

152. Sean Broderick et al., Criminal E-Discovery: A Pocket Guide for Judges (Federal Judicial Center 2015).

153. 15 U.S.C. § 77z-1(b)(1) (2012); 15 U.S.C. § 78u-4(b)(3)(B) (2012).

example, most securities cases will require expert discovery, and judges generally suggest setting the date for the end of expert discovery later than that for the end of fact discovery. In certain circumstances, judges have found extending expert discovery beyond summary judgment to be useful.

B. Discovery Disputes

Judges must also put a structure in place for resolving discovery disputes, bearing in mind whatever the local rules say on the matter. Judges interviewed for this guide varied widely in their treatment of discovery disputes, but they agreed that in general their procedures endeavor to create bright lines, promote common sense, and ensure speed where possible.

Judges are divided in their use of magistrate judges to oversee discovery in complex securities actions. Some judges favor using magistrate judges because they believe the magistrate judges give parties "breathing space" to work through disputes while not under the eyes of the trying judge. Others prefer to oversee discovery themselves to keep themselves educated and proceedings timely. Judges who don't use magistrate judges to assist in discovery also state that it tends to encourage parties to resolve disputes themselves rather than come to the judge; they think parties are more likely to "behave" in front of the judge who will try the case. Some point out that in certain districts, magistrate judges would not be available for a single judge's calendar for a case as complex as a securities class action.

Judges also have different approaches for how they instruct parties to raise discovery disputes. Some favor three-page briefing letters and mandatory meet-and-confers before parties approach the judge. Others prefer to get the parties on the phone more quickly so as to minimize briefing and delays. Still others insist on having a record for any discovery proceedings, often making phone calls untenable.

C. Parallel Proceedings

Parallel civil and criminal securities proceedings sometimes raise difficult questions for discovery. If a defendant decides to be cooperative with the government, the defendant risks any disclosures being discoverable by private civil plaintiffs. Courts of appeals have not wholly banned selective waiver arguments, but generally do not accept them under such circumstances (the notable exception is the Eighth Circuit, which does accept selective waiver arguments).[154] Conversely, defendants may also use a criminal proceeding to their advantage, invoking a Fifth Amendment right in a parallel civil proceeding, but waiving it once discovery is closed.[155]

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154. *See In re* Steinhardt Partners, L.P., 9 F.3d 230, 235–36 (2d Cir. 1993) (collecting cases from other circuits); *but see* Diversified Indus., Inc. v. Meredith, 572 F.2d 596, 611 (8th Cir. 1977).

155. Lawrence J. Zweifach & Eric M. Creizman, *Defending Parallel Proceedings: Basic Principles & Tactical Considerations*, *in* Securities Litigation Report vol. 7.2 (2010), at 6–7, *available at* http://web.archive.org/save/_embed/http://www.gibsondunn.com/publications/Documents/DefendingParallelProceedings.pdf.

Federal Rule of Evidence 502(d) allows for court orders that limit the scope of a waiver of privilege, but such orders do not appear to be widely used in securities cases. More often, courts have exercised the option of granting a motion to stay civil proceedings or civil discovery during a pending criminal case, as described in Part IV.D, *supra*.

XIII. Trial

Securities trials that are not class actions have few if any noteworthy differences from other cases. For general information and guidance on trials in the complex commercial context, judges should consult Chapter 12 of the FJC's *Manual for Complex Litigation, Fourth*.[156]

Securities class action trials are exceedingly rare; since the passage of the PSLRA in 1994 only twenty-one federal securities class actions have gone to trial, and only fifteen have reached a verdict or judgment.[157] It is not surprising that the scarcity of such trials has led to an overreliance on those cases that *have* been tried. Jury instructions, verdict forms, and similar materials may be presented for approval with the simple justification that they were used in a previous case. It bears emphasizing that while a previous trial may serve as a valuable resource, in most instances it does not carry precedential weight. In cases in which the parties disagree over such matters, judges should be wary of choosing one side's proposal simply because it has been used before.

XIV. Conclusion

A pocket guide can only scratch the surface of an area of law as vast as securities litigation. Nevertheless, the author's hope is that reading this guide will leave judges with an improved sense of the securities litigation landscape and where the particular issues of cases they encounter may fit in. There is no doubt that handling a securities case for the first time may feel daunting, but understanding the broader context in which the action is brought can help a judge know where to look to render decisions with confidence.

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156. MCL, Fourth, *supra* note 24.
157. Starykh & Boettrich, *supra* note 9, at 38.

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