NO. 12-88

In the
Supreme Court of the United States

PROSKAUER ROSE LLP,

PETITIONER,

v.

SAMUEL TROICE, HORATIO MENDEZ, ANNALISA MENDEZ, PUNGA PUNGA FINANCIAL, LTD., individually and on behalf of a class of all others similarly situated,

RESPONDENTS.

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

BRIEF FOR PETITIONER

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QUESTION PRESENTED

Does the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), 15 U.S.C. §§ 77p(b), 78bb(f)(1), prohibit private class actions based on state law only where the alleged purchase or sale of a covered security is "more than tangentially related" to the "heart, crux or gravamen" of the alleged fraud?

STATEMENT PURSUANT TO RULE 29.6

Petitioner's corporate disclosure statement, set forth at page ii of its Petition for a Writ of Certiorari, is still accurate.

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The opinion of the United States Court of Appeals for the Fifth Circuit (Appendix to the Petition for Certiorari ("Pet. App.") 1a-44a) is reported at 675 F.3d 503. The orders of the district court (Pet. App. 45a-46a, 47a-75a) are unreported.

JURISDICTION

The Fifth Circuit entered its opinion and order on March 19, 2012, Pet. App. 1a, and denied a timely petition for rehearing on April 19, 2012, with three judges recused, Pet. App. 76a. A petition for a writ of certiorari was filed on July 18, 2012 and granted on January 18, 2013. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The pertinent provisions of the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), Pub. L. No. 105-353, 112 Stat. 3227, which are codified in § 16 of the Securities Act of 1933 (the "Securities Act"), 15 U.S.C. § 77p(b), and § 28 of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § 78bb(f), are reproduced in full at Pet. App. 80a-93a. Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), is reproduced in full at Pet. App. 94a-96a.

STATEMENT OF THE CASE

This case is governed by the broad preclusive language in SLUSA, which prohibits state law class actions alleging a purchase or sale of a covered (*i.e.*, nationally traded) security "in connection with" an untrue statement or omission of material fact. This Court has said that the "in connection with" requirement should be given the same broad construction in SLUSA as in § 10(b) of the Exchange Act.

The complaint in this case alleges that petitioner aided and abetted R. Allen Stanford, the mastermind of a Ponzi scheme. As part of the fraudulent scheme, Stanford allegedly paid above-market commissions to stockbrokers so that they would liquidate their clients' portfolios of stocks and bonds and invest the proceeds in worthless certificates of deposit (the "CDs"). Stanford also allegedly induced investors to buy the CDs by promising them, *inter alia*, that their money would be invested in a portfolio of highly liquid, marketable securities—securities that necessarily trade on a national exchange.

Contrary to the plain language of the "in connection with" requirement and this Court's interpretation of SLUSA, the court below held that the foregoing allegations did not trigger SLUSA preclusion because the alleged purchases and sales were "not more than tangentially related" to the "'heart,' 'crux,' or 'gravamen'" of the alleged fraud. The court of appeals adopted an incorrect legal standard for assessing whether SLUSA precludes a state law class action, thereby allowing litigation of state law claims that Congress has prohibited. In applying this erroneous standard, the court of appeals compounded its error by assessing improper factors, such as the layers of separation between the alleged fraud and a covered securities transaction, as well as a plaintiff's purpose in making the investment giving rise to the claim. The Fifth Circuit's test, and the factors it considered in applying that test, conflict with both the plain statutory language and the decisions of this Court regarding SLUSA. Accordingly, the decision of the court of appeals should be reversed.

I. Statutory Background

Congress enacted SLUSA to prevent private plaintiffs from frustrating the purposes of the Private Securities Litigation Reform Act of 1995 ("PSLRA"), Pub. L. No. 104-67, 109 Stat. 737. *Merrill Lynch, Pierce, Fenner & Smith v. Dabit*, 547 U.S. 71, 81-82 (2006). The PSLRA was passed in part to curb abuses of the class action device in federal securities cases. *Id.* The PSLRA imposed certain restrictions on such cases, including heightened pleading requirements, a discovery stay pending resolution of any motion to dismiss and limitations on recoverable damages. *Id.*

The enactment of the PSLRA had the "unintended consequence" of channeling some securities class actions into state court, as plaintiffs circumvented the restrictions imposed by the statute. *Dabit*, 547 U.S. at 82. Recognizing that these lawsuits threatened to undermine the purpose of the PSLRA, in 1998 Congress closed that loophole by enacting SLUSA to "prevent certain State private securities class action lawsuits alleging fraud from being used to frustrate the objectives" of the PSLRA. SLUSA § 2(2), (5); 112 Stat. 3227. SLUSA's "core provision" prohibits any "covered class action based upon the statutory or common law of any State or subdivision thereof . . . alleging . . . a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security.[1] *Dabit*, 547 U.S. at 82-83 (quoting 15 U.S.C. § 78bb(f)(1)). "[T]he evident purpose of [this provision] is to limit the availability of remedies under state law." *Id*. at 88 n.13.

Congress endowed SLUSA, as remedial legislation, with an expansive preclusive effect. Congress intended SLUSA to have a "broad construction" that is fully coextensive with the scope of the authority of the Securities and Exchange Commission (the "SEC") to bring cases under § 10(b) of the Exchange Act. *Id*. at 85-86. The scope of SLUSA preclusion thus extends beyond the class of cases that private plaintiffs can bring under § 10(b), because SLUSA's "in connection with" requirement is not limited by the prudential standing and other requirements applicable to private § 10(b) actions. For example, while private plaintiffs cannot pursue

[1] A "covered class action" is defined as a lawsuit in which damages are sought on behalf of more than 50 people, and a "covered security" includes one traded nationally and listed on a regulated national exchange. *Dabit*, 547 U.S. at 83, nn. 8 & 9.

"holder" actions under the federal securities laws because holders do not themselves buy or sell any securities, such actions can be brought by the SEC (which does not need to satisfy the purchaser-seller standing requirement) and therefore are precluded by SLUSA, so long as they satisfy the statute's other requirements. *See id.* at 88-89.

By using the phrase "in connection with" in SLUSA, Congress intended to incorporate this Court's judicial interpretation of § 10(b)'s identical requirement. *Id.* at 85-86. This Court's decisions interpreting that requirement establish that a misrepresentation and a securities transaction are sufficiently connected even if they merely "touch[]," *Superintendent of Ins. of N.Y. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 12 (1971), or if they "coincide," *SEC v. Zandford*, 535 U.S. 813, 825 (2002).

As the terms "touching" and "coincide" connote, the requisite connection between the alleged fraud and the securities transaction need not be close. For example, this Court's decisions have "rejected th[e] view" that "an alleged fraud is 'in connection with' a purchase or sale of securities only when the plaintiff himself was defrauded into purchasing or selling particular securities." *Dabit*, 547 U.S. at 85. Under both § 10(b) and SLUSA, "it is enough that the fraud alleged 'coincide' with a securities transaction—whether by the plaintiff or by someone else." *Id.* (citing *United States v. O'Hagan*, 521 U.S. 642, 651 (1997)). "The identity of the plaintiffs does not determine whether the complaint alleges fraud 'in connection with the purchase or sale' of securities."

Id. at 89. Indeed, the "in connection with" requirement can be satisfied even if "the person or entity defrauded is not [a] party to [any] trade." *O'Hagan*, 521 U.S. at 656. In addition, the "in connection with" requirement does not turn on whether the misrepresentation concerns the value of a security or even whether the fraud concerns a particular security. *Zandford*, 535 U.S. at 821. Nor does it matter whether the fraud occurs in any particular securities transaction, or contemporaneously with any such transaction, so long as the practices alleged, taken as a whole, are deceptive and involve the purchase or sale of a security. *See Bankers Life & Cas. Co.*, 404 U.S. at 8-10. Where a securities transaction is "made to further . . . a fraudulent scheme," the "in connection with" requirement will be satisfied. *Zandford*, 535 U.S. at 820-21, 825.

II. Respondents' Allegations

Respondents are purchasers of certificates of deposit issued by the Stanford International Bank ("SIB"). Pet. App. 48a-49a. In their second amended complaint, respondents alleged that the CDs were part of a Ponzi scheme run by R. Allen Stanford and the Stanford Financial Group (collectively, "Stanford"). Stanford is not named as a defendant in this action.

The complaint alleges that Stanford induced respondents and a class of similarly situated investors to buy CDs through false representations that the CDs were "safe[] and secur[e]" and paid "high return rates." J.A. 449 [Record ("R.") 183].

According to the complaint, Stanford attributed these features to SIB's investment of the CD proceeds in "stocks" and "bonds" and a diversified portfolio of highly liquid, marketable securities "issued by stable governments, strong multinational companies and major international banks." J.A. 444, 445, 449, 458, 469-470. Stanford allegedly emphasized the "liquidity/marketability of SIB's invested assets" as "the '*most important factor* to provide security to SIB clients . . . .'" J.A. 444 (emphasis added).

To grow the Ponzi scheme, Stanford allegedly "'head hunt[ed]' for U.S. brokers and financial advisers" by paying them large bonuses and commissions to "transfer their book of clients over to Stanford Financial" and to "'push' the SIB CDs on investors like Plaintiffs." J.A. 440-41. As a result, by 2009, Stanford had allegedly sold over $7 billion in CDs. J.A. 449. To generate this volume of sales, at least some CD purchasers, many of whom were small investors allegedly lacking discretionary funds, *see* J.A. 472-74, necessarily liquidated their holdings of covered securities to reinvest the proceeds in the CDs when their brokerage accounts were transferred to Stanford. As the SEC confirmed through a forensic review of sample brokerage accounts, it is undisputed that some investors sold covered securities to buy CDs. J.A. 221. The district court took judicial notice of this fact below, J.A. 771; Pet. App. 70a n. 14, and the court of appeals expressly approved that determination, finding that "covered securities were in fact traded as part of the fraud," Pet. App. 40a-41a.

Petitioner Proskauer is an international law firm that was hired as outside counsel to represent Stanford in an SEC investigation. J.A. 424-25, 488. Respondents do not allege that petitioner made misrepresentations to them or was involved in selling the CDs or perpetuating the Ponzi scheme. Instead, they assert that petitioner aided and abetted Stanford's violations of the Texas Securities Act and common law by allegedly stalling an SEC investigation into Stanford's operations. J.A. 488-89.

III. The Proceedings Below

Petitioner moved to dismiss respondents' second amended complaint on SLUSA and other grounds. J.A. 3. Petitioner in No. 12-79 joined in and adopted the arguments made under SLUSA. J.A. 3. The district court (Godbey, J.) granted petitioner's motion to dismiss the complaint, holding that SLUSA precludes respondents' state law class action claims. Pet. App. 45a-46a.

The district court determined that respondents alleged fraud "in connection with" a covered securities transaction in two ways: (1) the plaintiffs' purchases of SIB CDs were allegedly "induced" by the misrepresentation that SIB invested plaintiffs' funds in a portfolio that included SLUSA-covered securities; and (2) "at least one of the [plaintiffs] acquired SIB CDs with the proceeds of selling SLUSA-covered securities in their IRA portfolios." Pet. App. 66a, 70a (internal quotation marks omitted). In interpreting SLUSA's "in connection with" requirement, the district court adopted the test employed by the Eleventh Circuit, which asks whether the complaint alleges "fraud that induced [the plaintiffs] to invest with [the defendants] . . . or a fraudulent scheme . . . that coincided and depended upon the purchase or sale of securities." Pet. App. 64a (alteration in original) (*citing Instituto de Prevision Militar v. Merrill Lynch*, 546 F.3d 1340, 1349 (11th Cir. 2008) ("*IPM*")). Concluding that respondents' allegations satisfied this standard, the district court dismissed the complaint. Pet. App. 75a.

IV. The Court of Appeals' Decision

Respondents timely appealed the dismissal of this action to the Fifth Circuit, where this action was consolidated with *Roland v. Green*, 11-10932 and *Troice v. Willis of Colorado*, No. 11-11048.

The Fifth Circuit reversed the district court's orders dismissing all three cases. Identifying the scope of SLUSA's "in connection with" requirement as one of "first impression" within the circuit, the Fifth Circuit complained that guidance from this Court that a fraud must "coincide" with a securities transaction was "not particularly descriptive." Pet. App. 14a, 17a. In attempting to interpret what it means for a fraud and a securities transaction to "coincide," the court of appeals did not examine this Court's decisions construing § 10(b).

Instead, the Fifth Circuit surveyed decisions from six other circuits interpreting SLUSA's scope. The Fifth Circuit rejected the tests used by the Sixth, Seventh and Eighth Circuits, concluding that they did not sufficiently define what it means for a securities transaction and a fraud to "coincide," and eliminated too many state law claims. Pet. App. 18a. The Fifth Circuit also rejected the standards of the Eleventh and Second Circuits. The Fifth Circuit held that insofar as the Eleventh Circuit considers whether a complaint alleges a fraud that "induced" the plaintiff's securities transaction, that test analyzes the "in connection with" requirement from the plaintiff's point of view, which the Fifth Circuit believed was the "wrong" perspective. Pet. App. 32a-33a. The Fifth Circuit disapproved, as "too stringent a standard," the portion of the Eleventh Circuit's test that considers whether an alleged fraudulent scheme "depends on" a securities transaction. Pet. App. 33a. For the same reason, the Fifth Circuit rejected the Second Circuit's test, which asks whether the plaintiff's claims "necessarily" allege, involve or rest on a securities transaction. *Id.* Ultimately, the Fifth Circuit announced that it was adopting the Ninth Circuit's test: whether "there is a relationship in which the fraud and the stock sale . . . are *more than tangentially related* . . . ." Pet. App. 34a (quoting *Madden v. Cowen & Co.*, 576 F.3d 957, 965-66 (9th Cir. 2009)).

The Fifth Circuit applied a test considerably more restrictive than the Ninth Circuit's, however. Relying primarily on a series of district court decisions from the Southern District of New York, the Fifth Circuit held that the purchase or sale of a covered security must also be more than tangentially related "to the '*heart,' 'crux,' or 'gravamen*' *of the defendants' fraud*." Pet. App. 38a (emphasis added). Although the Fifth Circuit agreed with the district court that the complaints in *Roland* and *Willis* alleged that purchases and sales of covered securities occurred as "part of the fraud," Pet. App. 41a, the court of appeals nonetheless concluded that this connection was insufficient because the plaintiffs did not invest in the CDs for the "purpose of purchasing covered securities" and because "there are 'multiple layers of separation' between the CDs and any security purchased by SIB," Pet. App. 40a (citations omitted).

The Fifth Circuit likewise concluded that the connection alleged in the complaint between the alleged fraud and the covered securities transaction was "not more than tangential[]." Pet. App. 44a. In making this determination, the Fifth Circuit did not evaluate the connection between the alleged fraud by Stanford and the covered securities transactions, which was the only connection petitioner had discussed in its motion to dismiss and on appeal, and the connection upon which the district court relied in granting the motion to dismiss. Instead, the Fifth Circuit reasoned that because petitioner was sued solely for aiding and abetting Stanford and had not made any misrepresentations to respondents, the court should focus its analysis on petitioner's purported communications with the SEC. Pet. App. 43a-44a. Finding that these were "one level removed" from the representations made to respondents and the transactions in covered securities, the Fifth Circuit held, as a result, that SLUSA does not preclude respondents' claims. Pet. App. 43a-44a.

This Court granted certiorari and consolidated this case with *Chadbourne & Parke LLP v. Troice, et al.*, No. 12-79, and *Willis of Colorado Incorporated, et al. v. Troice, et al.*, No. 12-86.

SUMMARY OF ARGUMENT

The court of appeals erred in holding that SLUSA did not preclude this action. The court below specifically determined that respondents' complaint alleged misrepresentations concerning SIB's investments in a portfolio of covered securities, and that these misrepresentations, in part, induced respondents and other investors to purchase CDs from Stanford. The court of appeals also determined that covered securities were, in fact, traded as part of Stanford's fraudulent scheme. Nevertheless, the Fifth Circuit held that SLUSA did not preclude this action because the allegations concerning covered securities transactions were not "more than tangentially related" to the "heart, crux or gravamen" of the alleged fraud. This holding was legally incorrect. It finds no support in SLUSA's text or in this Court's decisions, and it frustrates Congress's intent to preclude state law class actions involving allegations of fraud relating to nationally traded securities.

I. As an initial matter, the court of appeals failed to analyze properly whether the complaint's allegations met the statutory standard for preclusion: whether a misrepresentation and a transaction in a covered security are "in connection with" one another. Instead, the Fifth Circuit adopted a test that is not based upon, and directly conflicts with, the language of SLUSA and § 10(b) of the Exchange Act as interpreted by this Court. The court of appeals thus committed three errors.

A. *First*, the court of appeals disregarded SLUSA's statutory text, which specifies that the "in connection with" requirement is the controlling standard for preclusion under SLUSA. In *Merrill Lynch, Pierce, Fenner & Smith v. Dabit*, 547 U.S. 71 (2006), this Court explained that Congress intended to incorporate judicial interpretations of § 10(b)'s identical "in connection with" requirement into SLUSA, and that the two statutory provisions are meant to have the same broad construction. Instead of applying those interpretations to this case, the Fifth Circuit created a different test that is substantially more restrictive.

B. *Second*, the Fifth Circuit's "more than tangentially" related test either would narrow the breadth of § 10(b) or cause its scope to diverge from SLUSA's—an untenable result under *Dabit*. The Fifth Circuit applied its restrictive test in a manner that is analytically incompatible with § 10(b). Specifically, the court of appeals developed additional criteria intended to assess how central a covered securities transaction is to the "heart, crux or gravamen" of the alleged fraud. These factors make it unlikely that complex and multi-layered frauds could ever satisfy the "in connection with" requirement, even though those are precisely the frauds § 10(b) was designed to address. Indeed, under the Fifth Circuit's approach, some of the securities transactions upon which the SEC relied to bring its related enforcement action against Stanford under § 10(b) would be too "tangentially related" to the fraud to satisfy that statute's "in connection with" requirement.

C. *Third*, the factors that the Fifth Circuit used to ensure that a fraud and a covered securities transaction are "more than tangentially related" to each other find no support in SLUSA's text and conflict with this Court's prior decisions. These four factors—(1) the defendants' "perspective" on the alleged fraud; (2) the centrality of a covered securities transaction to the fraud; (3) the plaintiff's investment purpose and (4) the layers of separation between the fraud and the purchase or sale—have been rejected by this Court as invalid considerations under § 10(b), and they are equally incompatible with SLUSA. These factors also conflict with the express intent of Congress in enacting SLUSA because they preserve the very state law class claims that Congress foreclosed. Several of the factors, moreover, conflict with each other, producing incoherent results that counsel strongly against adopting the Fifth Circuit's statutory construction.

II. The state law class claims in this case fit easily within the broad scope of SLUSA's preclusion provision. Respondents' complaint alleged fraud "in connection with" the purchase or sale of covered securities in at least two respects. First, the complaint alleged that Stanford falsely represented that SIB would invest CD proceeds in a portfolio of covered securities, and that these investments endowed the CDs with features that, at least in part, induced respondents and other investors to purchase them. In short, the complaint alleged that Stanford made a false promise to purchase covered securities while intending never to fulfill that promise. This Court and the SEC have long held that such a deceptive practice satisfies the "in connection with" requirement. Second, the complaint alleged that some investors sold covered securities to reinvest the proceeds in the SIB CDs. These allegations also satisfy the "in connection with" requirement under this Court's precedents because they involve securities transactions made in furtherance of a fraudulent scheme, which injured investors who were duped into believing that they would receive the proceeds of the sales. Because the sales and the fraud were not independent events, they "touch" and "coincide," and, therefore, are "in connection with" each other within the meaning of SLUSA.

ARGUMENT

I. The Fifth Circuit's Test Conflicts With This Court's Precedents and the Plain Meaning of "In Connection With" In § 10(b) and SLUSA

The Fifth Circuit applied the wrong standard for determining when a covered securities transaction and a fraud are "in connection with" one another as that phrase is used in SLUSA. The court of appeals held that SLUSA does not preclude claims that are only "tangentially related" to the "'heart,' 'crux,' or 'gravamen'" of the alleged fraud. Pet. App. 34a, 38a (footnotes omitted). This test is substantially narrower than the expansive language of the "in connection with" requirement in both SLUSA and § 10(b) of the Exchange Act, as interpreted by this Court and as intended by Congress.

A. SLUSA's Statutory Text Specifies That the Standard For Preclusion Is "In Connection With," Not "More Than Tangentially Related"

The court of appeals committed a fundamental error by disregarding the statutory standard for SLUSA preclusion. The Fifth Circuit explained that SLUSA precludes state law claims only where the alleged fraud and the securities transaction "coincide." Pet. App. 17a-21a (repeatedly discussing the scope of the purported "coincide requirement"). Observing that this purported "test" is "not particularly descriptive," the court of appeals reviewed the divergent tests adopted by other circuits "to give dimension to the 'coincide' requirement" before ultimately finding the Ninth Circuit's "more than tangentially related" standard "to be the best articulation" of that "requirement." Pet. App. 17a, 34a. The initial error in the Fifth Circuit's approach, however, is that "coincide" is not a "requirement" or test for SLUSA preclusion under the statute or this Court's precedents. Moreover, the "more than tangentially related" standard the Fifth Circuit used to further narrow this supposed requirement or test finds no support in either source.

The "starting point" for interpreting the federal securities laws—as with every other statute—is the statutory language itself. *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511

U.S. 164, 173 (1994) (quoting *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 197 (1976) (internal quotation marks omitted)); *accord CSX Transp., Inc. v. Alabama Dep't of Revenue*, 131 S.Ct. 1101, 1107 (2011). SLUSA provides that:

> [n]o covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging . . . a misrepresentation or omission of a material fact *in connection with* the purchase or sale of a covered security . . . .

15 U.S.C § 78bb(f)(1)(a) (emphasis added). In *Dabit*, this Court unanimously held that by "import[ing] the key phrase—'in connection with the purchase or sale'—into SLUSA's core provision," Congress intended SLUSA to have the same "broad construction adopted by both this Court and the SEC" in interpreting the identical words that appear in § 10(b) of the Exchange Act. 547 U.S. at 85.

Contrary to the Fifth Circuit's view, this Court has never "announced" that a fraud can only be "in connection with" a securities transaction if the two "coincide." Pet. App. 17a. Neither *Dabit* nor this Court's decisions concerning § 10(b) have adopted such a requirement. To the contrary, *Dabit* confirmed that under both SLUSA and § 10(b), and consistent with the text of both statutory provisions, "[t]he requisite showing . . . is 'deception *in connection with* the purchase or sale of any security . . . .'" *Dabit*, 547 U.S. at 85 (quoting *United States v. O'Hagan*, 521 U.S. 642, 651 (1997)) (emphasis added and internal quotation marks omitted). Allegations of a securities transaction in "further[ance] [of a] fraudulent scheme" will satisfy this standard. *Zandford*, 535 U.S. at 820-21.

To be sure, "this Court *has* sought to give meaning to the phrase ["in connection with"] in the context of § 10(b) and Rule 10b-5," *Dabit*, 547 U.S. at 85, and in doing so, it has, at times, used the word "coincide"—but never as a requirement. For example, in *O'Hagan,* this Court used that term in holding that § 10(b) covered the misappropriation theory of insider trading. But the Court in *O'Hagan* did not purport to adopt a "coincide" requirement; rather it interpreted the standard that the statutory text already supplied: "the § 10(b) requirement that the misappropriator's deceptive use of information be 'in connection with the purchase or sale of [a] security.'" *O'Hagan*, 521 U.S. at 655-56. The Court held that the misappropriation theory satisfied "[t]his element" of a § 10(b) prosecution because "the securities transaction and the breach of duty . . . coincide." *Id.* at 656. "Coincide" was a sufficient—but not necessary—condition for satisfying the statutory "in connection with" requirement. That, in fact, is precisely what this Court unanimously said in *SEC v. Zandford*, 535 U.S. 813 (2002), when it again used the term "coincide" in the context of § 10(b). In holding that a broker with discretionary authority over his clients' accounts violated § 10(b) merely by selling their securities without disclosure, the Court stated that "*[i]t is enough* that the scheme to defraud and the sale of securities coincide." *Id.* at 822 (emphasis added). Under the particular facts of

Zandford, where the securities sales and the deceptive breach of fiduciary duty occurred together, they were "not independent events," *id.* at 820, and nothing further—such as the broker's misappropriation of the proceeds—was required to satisfy § 10(b)'s "in connection with" element, *id.* at 822.

In those cases, moreover, this Court used the "coincide" analysis in the course of "espous[ing] a broad interpretation" of the statutory "in connection with" requirement. *Dabit*, 547 U.S. at 85. Indeed, in each case, the Court held that the scope of SLUSA or § 10(b), as applicable, was *more expansive* than the lower courts believed. *See Zandford*, 535 U.S. at 820-21 (reversing Fourth Circuit's determination that § 10(b) applies only where there is "a misrepresentation about the value of a particular security"); *O'Hagan*, 521 U.S. at 656 (adopting misappropriation theory that Eighth Circuit had rejected). In *Dabit*, this Court explicitly applied the "broad interpretation" of the statutory phrase from both *Zandford* and *O'Hagan* to SLUSA and once again gave the "in connection with" requirement a broader construction than the lower court had. *Dabit*, 547 U.S. at 88-89 (reversing Second Circuit's determination that SLUSA does not apply to holder class actions).

The Fifth Circuit erred not only by substituting a "coincide" requirement for the "in connection with" requirement as the governing standard for preclusion, but also by using a "coincide" analysis in precisely the *opposite* way in which this Court has used it. Instead of adopting a broad construction of the phrase "in connection with" consistent with the holding of *Dabit*, the Fifth Circuit used the "coincide" analysis as a jumping-off point for narrowing SLUSA (and preserving state law claims that Congress meant to preclude) by creating a test unmoored from either this Court's prior decisions or the statutory text.[2]

Specifically, the Fifth Circuit held that the only connection that will satisfy SLUSA's requirements is one where a covered securities transaction is "more than tangentially related" to the "'heart,' 'crux,' or 'gravamen'" of the alleged fraud. Pet. App. 34a, 38a.

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[2] To the extent that the tests adopted by some of the other courts of appeals under SLUSA impose requirements beyond an allegation of fraud "in connection with" the purchase or sale of a covered security, they, too, are not consistent with the statutory text or this Court's decision in *Dabit*. *See, e.g.*, *Romano v. Kazacos*, 609 F.3d 512, 522 (2d Cir. 2010) ("necessarily allege, necessarily involve, or rest on"); *Madden v. Cowen & Co.*, 576 F.3d 957, 965-66 (9th Cir. 2009) ("more than tangentially related"); *LaSala v. Bordier et Cie*, 519 F.3d 121, 141 (3d Cir. 2008) (misrepresentation must be a "necessary fact[]"); *Gavin v. AT&T Corp.*, 464 F.3d 634, 639 (7th Cir. 2006) ("involving," meaning more than "but for"). The Sixth and Eighth Circuits, hewing closer to SLUSA's text, have declined to specify how strong the alleged "connection" must be to trigger preclusion. *See Segal v. Fifth Third Bank, N.A.*, 581 F.3d 305, 310-11 (6th Cir. 2009); *Siepel v. Bank of Am., N.A.*, 526 F.3d 1122, 1127 (8th Cir. 2008). The Fifth Circuit rejected these decisions as unpersuasive because they "do not attempt to define [SLUSA's] 'coincide requirement." Pet. App. 18a. But, as discussed above, the Fifth Circuit misapprehended what SLUSA requires.

These requirements go beyond SLUSA's statutory text, and courts should resist adding words or elements to a statute. *See Bates v. United States*, 522 U.S. 23, 29 (1997) ("[W]e ordinarily resist reading words or elements into a statute that do not appear on its face."); s*ee also Burlington No. R.R. Co. v. Oklahoma Tax Comm'n*, 481 U.S. 454, 461, 463 (1987) (finding statute's language clear and noting that respondent's argument "would require the addition of words to a statutory provision which is complete as it stands [and] [a]doption of [this] view would require amendment rather than construction of the statute, and…must be rejected"). The effect of adding these requirements to the statute is that a court, after finding a "connection" between a fraud and a covered securities transaction, must find additional factors in order for SLUSA preclusion to apply. That analysis is contrary to the statutory language and should therefore be rejected.

B. The Fifth Circuit's Test Improperly Narrows the "In Connection With" Requirement Under Both SLUSA & § 10(b)

The test adopted by the Fifth Circuit substantially narrows the "in connection with" requirement of SLUSA and § 10(b) as this Court has interpreted it. As a result, the Fifth Circuit's test risks either limiting the scope of conduct that is covered by § 10(b), or forcing the meaning of the "in connection with" requirement in SLUSA to diverge from its meaning under § 10(b), notwithstanding this Court's conclusive determination in *Dabit* that it means the same thing in both statutes. *See* 547 U.S. at 85-86. Neither result is consistent with this Court's prior decisions, the language of the statutes or the intent of Congress.

As a definitional matter, the "more than tangentially related" test ignores the statutory text and departs from this Court's interpretation of it. A "connection" is an "association," "relationship," or "link." *See* The Random House Unabridged Dictionary 431-32 (2d ed. 1993); The American Heritage Dictionary of the English Language 390 (5th ed. 2011). While this Court has recognized that the statutory phrase "in connection with" may be ambiguous, *Zandford*, 535 U.S. at 819, nothing in the statutory text itself invites an assessment of the strength of the alleged connection, as the Fifth Circuit's "more than tangentially related" test does. Rather, this Court has repeatedly emphasized that the statutory language of § 10(b) should not be interpreted in a "technical[] and restrictive[]" manner, *Zandford*, 535 U.S. at 819, and that no especially close connection between the fraud and the securities transaction is required. As this Court has explained, § 10(b)'s "in connection with" requirement is satisfied where a plaintiff has "suffered an injury as a result of deceptive practices *touching* [the purchase or] sale of securities." *Superintendent of Ins. of N.Y. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 12-13 (1971) (emphasis added); *see also Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 476

(1977) (same).[3] The Fifth Circuit held below that SLUSA does not apply unless the complaint's "allegations regarding the fraud are more than tangentially related to (real or purported) transactions in covered securities." Pet. App. 34a-35a. The word "tangential" means "touching lightly." Webster's Third New International Dictionary 2337 (1993).[4] By definition, the Fifth Circuit's "more than tangential" standard requires something *more* than "touching," *see Bankers Life*, 404 U.S. at 12-13, and thus, a relationship more substantial than what this Court held in *Bankers Life* would satisfy the "in connection with" requirement.

The Fifth Circuit's error is not purely semantic. As discussed further *infra*, the court of appeals considered several factors in applying its test that are analytically inappropriate to SLUSA or § 10(b). For example, the Fifth Circuit held that the alleged fraud in this case was not "more than tangentially related" to a covered securities transaction because there were "multiple layers of separation" between

[3] Although the Court has used the term "coincide" in its more recent cases, there is no indication that this was intended to limit the "touch" analysis of *Bankers Life*. To the contrary, in *Zandford*, this Court explained that the complaint in that case, "[a]s in *Bankers Life* . . . describes a fraudulent scheme in which the securities transactions and breaches of fiduciary duty coincide." 535 U.S. at 825.

[4] The root of "tangent" is the Latin "tangere," meaning "to touch." *The Concise Oxford Dictionary of English Etymology* 482 (1993).

respondents' investments and a misrepresentation concerning a covered securities transaction. Pet. App. 40a, 43a. Having multiple layers of separation, however, frequently will be a hallmark of any complex fraud. That is precisely the kind of fraud that § 10(b) was aimed at; the drafters intended it as a "catchall" clause "to enable the Commission 'to deal with new manipulative [or cunning] devices.'" *Hochfelder*, 425 U.S. at 202-203 (quoting testimony by Thomas G. Corcoran, a spokesman for the drafters of Section 10(b) during Hearings on H.R. 7851 and H.R. 8720 before the House Committee on Interstate and Foreign Commerce, 73d Cong., 2d Sess., 115 (1934); *see also Chiarella v. United States*, 445 U.S. 222, 234-35 (1980) ("Section 10(b) is aptly described as a catchall provision."). A ruling that SLUSA does not apply to highly complex multi-layered frauds simply cannot be squared with the scope of § 10(b)'s "in connection with" requirement as this Court has interpreted it. *See infra* at 30-31 (discussing *Bankers Life*). Nor can such a ruling be squared with Congress's intent in passing SLUSA "to limit the availability of remedies under state law." *Dabit*, 547 U.S. at 88 n.13.

The clearest indication that the Fifth Circuit's interpretation of SLUSA will circumscribe the scope of § 10(b) is provided by the SEC itself. In its related action against Stanford, the SEC took the position that § 10(b) covered the *same* alleged fraud based on one of the *same* theories that petitioner advances here. Specifically, in seeking a preliminary injunction and the appointment of a receiver, the SEC argued that it could satisfy § 10(b)'s "in connection with" requirement, in part, by showing that Stanford had duped investors into liquidating their existing portfolios of stocks and bonds to re-invest the proceeds in the SIB CDs. J.A. 190. The SEC supported this contention through the results of a forensic audit of several investor accounts, J.A. 211-221, of which the district court took judicial notice in granting the motion to dismiss in *this* action, Pet. App. 69a-70a. Although the Fifth Circuit specifically found that through these sales, "covered securities were in fact traded as a part of the fraud," Pet. App. 41a, it nonetheless held that these *same* sales were too tangentially related to the alleged fraud in this action to satisfy SLUSA's "in connection with" requirement. Pet. App. 42a. If the Fifth Circuit were correct, then those securities sales could not satisfy § 10(b)'s requirements, and the SEC would not have been able to rely on them to bring the § 10(b) claim it asserted against Stanford. The scope of § 10(b) would thus be narrowed as a direct result of the court of appeals' incorrect SLUSA decision below.

C. The Fifth Circuit's Test Relies on Extra-Statutory Factors That This Court Has Rejected and That Produce Incoherent Results

In applying its "more than tangentially related" test, the Fifth Circuit looked to factors—(1) the defendant's perspective on the fraud as alleged, (2) the centrality of the purported misstatements to the relevant transaction, (3) the plaintiff's investment purpose and (4) the layers of separation between the fraud and the purchase or sale—that are outside SLUSA's statutory framework and directly contravene this Court's decisions. Moreover, certain of these factors are internally inconsistent with each other and, when applied together, produce incoherent results.

1. The Defendant's Perspective On the Alleged Fraud. The Fifth Circuit improperly concluded that "the defendant-oriented perspective is the proper point of view from which to consider the allegations" for purposes of assessing SLUSA's application. Pet. 32a-33a. It thus rejected any consideration of whether the alleged fraud "induced" the plaintiffs to "invest[] . . . because of (representations about) transactions in covered securities." Pet. App. 32a. The court of appeals believed that this inquiry would "ask[] the wrong question" because it "[v]iew[s] the allegations from the plaintiffs' perspective," and would "unnecessarily import[] causation into [the] test" for SLUSA preclusion. *Id.* Nothing in SLUSA's statutory text, however, suggests that there is any "proper point of view" from which to assess whether an alleged misrepresentation or omission is "in connection with" a covered securities transaction. So long as the complaint alleges a connection between the fraud and the transaction, SLUSA's requirements are satisfied. *See Segal v. Fifth Third Bank, N.A.*, 581 F.3d 305, 311 (6th Cir. 2009) ("The Act does not ask whether the complaint makes 'material' or 'dependent' allegations of misrepresentation in connection with buying or selling securities. It asks whether the complaint includes these types of allegations, pure and simple.").

Moreover, this Court *has* routinely considered the effect of the alleged fraud on the victim or others—what the Fifth Circuit termed the "plaintiffs' perspective." Pet. App. 32a. This Court has held that the "in connection with" requirement is satisfied where the "seller [of the securities] was *duped* into believing that it, the seller, would receive the proceeds" as a result of a fraudulent scheme. *Bankers Life*, 404 U.S. at 9-10 (emphasis added); *see also Zandford*, 535 U.S. at 822 (victims "were injured . . . through . . . deceptions, which deprived them of any compensation for the sale of their valuable securities" because "[t]hey were *duped* into believing respondent would 'conservatively invest' their assets") (emphasis added). Thus, while a fraud need not induce a securities transaction to satisfy the "in connection with" requirement, the Fifth Circuit improperly disregarded allegations in this case that misrepresentations concerning covered securities transactions induced plaintiffs both to purchase SIB CDs and to sell their existing investments in covered securities so that they could reinvest in those CDs. *See infra* at 33-40.

2. The Centrality of the Securities Transaction to the Alleged Fraud. Straying once more from the statutory text, the Fifth Circuit held that the existence of a mere "connection" between a fraud and a securities transaction will not trigger preclusion under SLUSA unless that "connection" also satisfies an additional proximity requirement: specifically, the covered securities transaction must be more than tangentially related to the "'heart,' 'crux' or 'gravamen' of the defendants' fraud." Pet. App. 38a (footnotes omitted); *see also* Pet. App. 37a-40a. The Fifth Circuit thus concluded that Stanford's alleged misrepresentations concerning SIB's investments in covered securities were "merely tangentially related" to the alleged fraud because there were a "host" of other misrepresentations that were also allegedly made to plaintiffs. Pet. App. 37a-38a, 43a-44a. Setting aside that many of these other purported misstatements—such as the liquidity of the SIB CDs and their consistently high rates of return—directly concerned SIB's investments in covered securities,[5] the existence of other, unrelated misrepresentations does not abrogate the "connection" under SLUSA between a covered securities transaction and an alleged fraud. *See IPM*, 546 F.3d at 1350 (11th Cir. 2008) (including additional allegations of negligent handling of client funds did not undo alleged "connection" between purported misrepresentations and securities transactions). Where a securities transaction is alleged "to further . . . the fraudulent scheme," the "in connection with" requirement is satisfied, regardless of what other deceptive conduct the perpetrator may have engaged in unrelated to securities. *Zandford*, 535 U.S. at 820-21.

The Fifth Circuit's requirement that, even after finding a connection between a fraudulent scheme and a covered securities transaction, a court must

[5] *See infra* at 30-32.

weigh the importance of the allegations regarding covered securities in the context of the scheme is entirely unworkable and an invitation to artful pleading. It would permit plaintiffs to load a complaint with allegations of representations or misrepresentations unrelated to a covered securities transaction in the hope of arguing that the link between the allegation about a covered securities transaction and the alleged fraud is too attenuated. That result—permitting plaintiffs to evade federal jurisdiction through artful pleading—is precisely what Congress sought to avoid in "adopting [SLUSA's] pre-emption provision, the evident purpose of which is to limit the availability of remedies under state law." *Dabit*, 547 U.S. at 88 n.13.

3. The Plaintiffs' Investment Purpose. The Fifth Circuit considered it important that the plaintiffs in these cases did not intend to make an investment in a SLUSA-covered security. Pet. App. 39a-40a. But in *Dabit*, this Court held that "the identity of the plaintiffs does not determine whether the complaint alleges fraud 'in connection with the purchase or sale' of securities." 547 U.S. at 89. "Under [this Court's] precedents, it is enough that the fraud alleged 'coincide' with a securities transaction—whether by the plaintiff or by someone else." *Id.* at 85 (citing *O'Hagan*, 521 U.S. at 651)). Similarly, in *O'Hagan*, this Court rejected the proposition that the person defrauded had to be a party to any securities trade. 521 U.S. at 656 (holding "in connection with" requirement satisfied "even though the person or entity defrauded is not the other party to the trade.")

Because the requisite standard can be satisfied regardless of whether the plaintiff makes any investment at all, the plaintiff's intent in investing cannot be a mandatory factor for assessing SLUSA's "in connection with" requirement.

4. The Layers of Separation Between the Fraud and the Purchase or Sale. Even though the state law class action claims at issue here alleged fraud "in connection with the purchase or sale of a covered security," the Fifth Circuit held them outside the reach of SLUSA because there were "'multiple layers of separation' between the CDs and any security purchased by SIB." Pet. App. 40a (citation omitted); *see also* Pet. App. 43a. But, the existence of "multiple layers separation" is irrelevant to the "in connection with" requirement, and this Court rejected that precise analysis in *Bankers Life*. There, an insurance company's sale of its bond portfolio for full market value satisfied § 10(b)'s requirements because the fraudulent scheme involved a complex web of other, subsequent transactions that, when taken as a whole, were deceptive:

> [The company's] assets had been depleted, [but] its books reflected only the sale of its Government bonds and the purchase of [a] certificate of deposit and did not show that its assets had been used by [a director] to pay for his purchase of [the company's] shares or that the certificate of deposit [bought with the proceeds of the bond portfolio] had been

> assigned . . . and then pledged to [other companies].

404 U.S. at 8-9. That the deception allegedly occurred through subsequent transactions that were fraudulent only when aggregated did not defeat application of § 10(b): although "the full market price was paid for those bonds[,] . . . the seller was duped into believing that it, the seller, would receive the proceeds." *Id.* at 9.

* * * * *

Thus, for each of these reasons, the "more than tangentially related" test as applied by the court of appeals does not square with SLUSA's statutory text or this Court's prior decisions.

Even beyond the inappropriateness of these four factors on their own terms, however, several of them directly conflict with each other. As applied by the court of appeals, these contradictory factors produce an arbitrary and incoherent result, and should be rejected for that reason as well. *See, e.g.*, *Clinton v. City of New York*, 524 U.S. 417, 429 (1998); *Church of the Holy Trinity v. United States*, 143 U.S. 457, 459 (1892).

For example, while the court of appeals held that the "plaintiffs' perspective" was the "wrong" one from which to analyze the complaint in assessing SLUSA preclusion, Pet. App. 32a, it nonetheless placed great weight on the plaintiff's investment purpose in deciding that its "more than tangentially related" test was not satisfied, Pet. App. 39a-40a.

SLUSA, obviously, cannot simultaneously prohibit *and* mandate consideration of the investors' intent or the effect of the fraud on their investment decisions.

Similarly, the court of appeals explained that it had rejected the tests used by the Eleventh and Second Circuits for SLUSA preclusion, which consider whether a fraud "depended upon" or "'necessarily allege[s],' 'necessarily involve[s],' or 'rest[s] on'" covered securities transactions, because those tests impose "too stringent a standard." Pet. App. 32a-33a (quoting *IPM*, 546 F.3d at 1349; *Romano v. Kazacos*, 609 F.3d 512, 522 (2d Cir. 2010). Yet, despite finding in this case that "covered securities were in fact traded as a part of the fraud" when investors were induced to liquidate their existing covered securities assets to reinvest the proceeds in CDs, Pet. App. 41a, the Fifth Circuit nonetheless rejected these allegations as insufficient because "the entirety of the fraud [here did not] *depend[] upon* the tortfeasor convincing the victims . . . to sell their covered securities in order for the fraud to be accomplished," Pet. App. 42a (emphasis added). If the Fifth Circuit was correct that SLUSA can preclude a class action lawsuit even if the alleged fraud does not "depend upon" a covered securities transaction—a proposition with which petitioner agrees—then the Fifth Circuit clearly erred by refusing to dismiss *this* case simply because it did not read the complaint as alleging that the fraud depended upon the purchase or sale of a covered security.

II. The Alleged Fraud In This Case Was "In Connection With" the "Purchase or Sale of a Covered Security"

The putative state law class action in this case is precluded by SLUSA because, in at least two respects, respondents' second amended complaint alleged "a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security . . . ." 15 U.S.C § 78bb(f)(1)(a).

First, the complaint alleged that Stanford induced respondents and others to purchase CDs by misrepresenting that SIB would invest the proceeds in a portfolio of covered securities. In particular, the complaint alleged that Stanford brokers told investors orally or through written marketing materials that:

- "investments in the CDs were liquid and the CDs could be redeemed at any time because SIB, through Stanford Financial, only invested the money in safe, secure and liquid assets," J.A. 433;

- "the bank [SIB] focuses on 'maintaining the highest degree of liquidity as a protective factor for our depositors' and that the bank's assets are "invested in a well-diversified portfolio of highly marketable securities issued by stable governments, strong multinational companies and major international banks," J.A. 444;

- "SIB's investments were liquid and diversified, and therefore that the CDs themselves were highly liquid and could be redeemed with just a few days notice," J.A. 444-45;

- "SIB was not a commercial bank and, instead of making loans, SIB took the money it received from the sale of CDs and itself invested in an allegedly diversified portfolio that included stocks [and] bonds," J.A. 458; and

- "an investment in SIB was safer than investing in U.S. banks because SIB did not make loans but instead invested in safe and highly liquid instruments," J.A. 470.

There can be no doubt that the "highly liquid" and "highly marketable" "stocks" and "bonds" described in the complaint refer to SLUSA-covered securities. Indeed, liquidity and marketability are precisely the reasons why "strong multinational companies" and "major international banks" list their securities on the New York Stock Exchange, the NASDAQ or other national exchanges—which is the very definition of a "covered" security under SLUSA. 15 U.S.C. § 78bb(f)(5)(E); *id.* § 77r(b)(1)(A)-(B). The district court specifically found that "SIB led the Plaintiffs to believe that the SIB CDs were backed, at least in part, by SIB's investments in SLUSA-covered securities," Pet. App. 65a & n.11, and the court of appeals acknowledged that the complaint alleged several "(mis)representations made to the [investors] in an attempt to lure them into buying the worthless CDs," including false "references to SIB's portfolio being backed by 'covered securities.'" Pet. App. 37a-38a, 44a.

The repeated allegations concerning the representation that SIB would invest CD proceeds in a portfolio of covered securities demonstrate that this promise cannot be dismissed, as the Fifth Circuit did, as tangential to the fraud. To the contrary, the complaint alleges that Stanford brokers emphasized the "'liquidity/marketability of SIB's invested assets' [as] the '*most important factor* to provide security to SIB clients,'" J.A. 444 (emphasis added); that based on this and other misrepresentations, "Plaintiffs decided to, and did, invest money in, and maintain investments in, the SIB CDs," J.A. 471; and that "[b]y year-end 2008, Stanford Financial had sold approximately $7.2 billion worth of SIB CDs by touting: . . . consistent, double-digit returns on the bank's investment portfolio," J.A. 449. Further, because the complaint alleges that Stanford was a "massive Ponzi scheme" dependent on CD sales to stay afloat, J.A. 480, the alleged misrepresentations concerning SIB's investment portfolio were integral to the fraud; indeed, respondents alleged that they were "material" to their investment decision, J.A. 471.

These allegations describe a fraud "in connection with the purchase or sale of a covered security" within the meaning of SLUSA. 15 USC § 78bb(f)(1)(a). There is no dispute that Stanford falsely promised CD purchasers that it would invest

CD proceeds in covered securities, while secretly intending to misappropriate those proceeds to continue a Ponzi scheme and fund Allen Stanford's lavish lifestyle. There was a false statement of material fact, and it concerned—and therefore was necessarily "in connection with"—the purchase of covered securities by SIB. Wherever the outer scope of SLUSA is, the allegations in this case do not approach it. The fraud and SIB's covered securities transactions are connected, "touch" and "coincide" because they are "not independent events"; each time Stanford made the representation about how SIB's assets would be invested, it engaged in deception to "further [its] fraudulent scheme." *Zandford*, 535 U.S. at 820-21.

There is no material difference between the allegations in the complaint in this action and the fact patterns that this Court and the SEC have consistently recognized as satisfying the "in connection with" requirement of § 10(b). In *Zandford*, this Court deferred to and adopted the SEC's longstanding view that "a broker who accepts payment for securities that he never intends to deliver . . . violates § 10(b) and Rule 10b-5." 535 U.S. at 819 (citing *In re Bauer*, 26 S. E. C. 770 (1947)); *accord Dabit*, 547 U.S. at 85 n.10. Similarly, in *Wharf (Holdings) Ltd. v. United International Holdings, Inc.*, 532 U.S. 588 (2001), this Court held that § 10(b) prohibited the defendant from selling "a security (the option) while secretly intending from the very beginning not to honor the option." *Id.* at 597. As the Court later explained, "the fraudulent intent [of the seller in *Wharf*] deprived the purchaser of the benefit of the sale." *Zandford*, 535 U.S. at 824. Likewise, here, Stanford falsely promised investors that the CDs it sold them would have certain characteristics because they were backed by investments in covered securities, while intending from the start never to make those investments. As in *Bauer* and *Wharf*, there was a promise to invest SIB's assets in covered securities that Stanford never intended to fulfill, and purchasers allegedly were deprived of the benefit of the CDs as a result. *See also In re Line*, 1996 SEC LEXIS 2746 (Sept. 30, 1996) (settled case) (SEC asserted that financial planner violated § 10(b) where he offered to hide temporarily the assets of parents seeking college financial aid by investing their assets in securities in his own name and paying them a fixed return, but he in fact misappropriated the funds).

Second, the complaint in this case satisfies SLUSA's "in connection with" requirement in an additional way: it alleges that Stanford sought to grow the Ponzi scheme in a manner that necessarily led investors to liquidate covered securities. In particular, the complaint alleges that Stanford "'head hunt[ed]' for U.S. brokers and financial advisers" with existing clients by paying the brokers large bonuses and commissions to "transfer their book of clients over to Stanford Financial" and to "'push' the SIB CDs on investors like Plaintiffs." J.A. 440-41. The complaint also alleges that the clients who were "pushed" into the CDs were of modest means: many "invested their life savings and retirement funds with Stanford Financial (through SIB)," and many "have amounts invested which are too small to justify the cost and expense of individual litigation." J.A. 471, 473. The only plausible way such investors could have purchased the billions of dollars in CDs described in the complaint is if some of them liquidated their pre-existing investments to reinvest in the CDs. Moreover, as the district court recognized, retirement funds of the sort that were liquidated to reinvest in the CDs typically include SLUSA-covered securities. Pet. App. 69a. In all events, the SEC's forensic audit of several Stanford investor accounts demonstrated that some CD purchasers did fund their purchases by liquidating pre-existing securities investments, J.A. 221 [R.E. 124], of which the district court took judicial notice, J.A. 771. The court of appeals accepted this determination, finding that "covered securities were in fact traded as part of the fraud." Pet. App. 41a.

These allegations likewise allege a misrepresentation of a material fact "in connection with" a SLUSA-covered securities transaction. Misrepresentations about the safety, liquidity and returns on the CDs induced investors to sell covered securities to reinvest in the CDs. "Since there was a 'sale' of a [covered] security and since fraud was used 'in connection with' it" (*i.e.*, to induce it), *Bankers Life & Cas. Co.*, 404 U.S. at 12, the state law class claims here are precluded by SLUSA. Indeed, this case is strikingly similar to *Bankers Life* and *Zandford*. In each case, as here, entities and people "were injured as investors through . . . deceptions, which deprived them of any compensation for the sale of their valuable securities." *Zandford*, 535 U.S. at 822; *Bankers Life & Cas. Co.*, 404 U.S. at 10

("Manhattan was injured as an investor through a deceptive device which deprived it of any compensation for the sale of its valuable block of securities."). In each case, as here, the sellers were induced to sell securities when they were "duped into believing that [they], the seller[s], would receive the proceeds." *Bankers Life & Cas. Co.*, 404 U.S. at 9-10; *see also Zandford*, 535 U.S. at 822 (sellers "were duped into believing respondent would 'conservatively invest' their assets in the stock market and that any transactions made on their behalf would be for their benefit for the 'safety of principal and income'"). Just as in those cases, the complaint here alleges a fraud "in connection with" the sale of a covered security, and therefore is precluded under SLUSA.

The Fifth Circuit attempted to distinguish those decisions on the invalid ground that it did not matter to Stanford whether investors sold covered securities to fund CD purchases; all that mattered was that they bought the CDs. Pet. App. 42a. Similar arguments were summarily rejected in both *Bankers Life* and *Zandford*. As this Court explained, what the perpetrator of the fraud does with the money is "irrelevant" to the "in connection with" requirement:

> The fact that respondent misappropriated the proceeds of the sales provides persuasive evidence that he had violated § 10(b) when he made the sales, but misappropriation is not an essential element of the offense. Indeed, in *Bankers Life*, we flatly stated that it was

> 'irrelevant' that 'the proceeds of the sale that were due the seller were misappropriated.'

Zandford, 535 U.S. at 822 (quoting *Bankers Life & Cas. Co.*, 404 U.S. at 10)). Once fraud has induced a sale of a covered security, as alleged in this case, the "connection" required by SLUSA has been established. Here, as in *Zandford*, "[t]he securities sales and [the] fraudulent practices were not independent events," 535 U.S. at 820-22, and SLUSA's "in connection with" requirement was thus satisfied.

CONCLUSION

For the foregoing reasons, this Court should reverse the decision of the court of appeals with instructions that the complaint should be dismissed with prejudice.

Respectfully submitted,

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