Nos. 12-79, 12-86 and 12-88

In the Supreme Court of the United States

CHADBOURNE & PARKE LLP,

Petitioner,

v.

SAMUEL TROICE, *et al.*,

Respondents.

WILLIS OF COLORADO INCORPORATED,
BOWEN, MICLETTE & BRITT, INC., AND
SEI INVESTMENTS COMPANY,

Petitioners,

v.

SAMUEL TROICE, *et al.*,

Respondents.

PROSKAUER ROSE LLP,

Petitioner,

v.

SAMUEL TROICE, *et al.*,

Respondents.

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

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BRIEF FOR THE RESPONDENTS

Respondents Samuel Troice et al. respectfully request that this Court affirm the judgment of the United States Court of Appeals for the Fifth Circuit in this case.

STATEMENT OF THE CASE

Respondents allege that petitioners participated in or facilitated a fraudulent scheme to sell certificates of deposit (CDs) in violation of state law. Reversing the district court, the court of appeals held that the complaints are not precluded by the Securities Litigation Uniform Standards Act of 1998 (SLUSA), Pub. L. No. 105-353, 112 Stat. 3227 (1998). The court recognized that the CDs are not "covered securities" subject to the statute. Although the CD sales potentially involved misstatements "about" covered securities, those representations were made only "in connection with the purchase or sale of" the non-covered CDs, not any "covered security."

1. Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 adopted by the Securities and Exchange Commission (SEC) are the principal securities fraud provisions of federal law. Both apply to fraud, including a "material" omission or misrepresentation, "in connection with the purchase or sale of any security." 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b-5. A misrepresentation is "material" if a reasonable investor would regard it as important in making investment decisions. *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988). A material misrepresentation is made "in connection with the

purchase or sale of" the security if it "coincides" with that transaction. *United States v. O'Hagan*, 521 U.S. 642, 656 (1997). The term "security" is defined broadly to include a wide array of financial instruments, including certain certificates of deposit. *See* 15 U.S.C. §§ 77b(a)(1), 78c(a)(10).

The SEC may enforce Rule 10b-5 civilly, and the Department of Justice may bring felony prosecutions for willful violations. 15 U.S.C. § 78ff(a); 17 C.F.R. § 240.10b-5. Private purchasers and sellers have an implied right of action to sue for violations of Rule 10b-5. *Superintendent of Ins. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 13 n.9 (1971). But Congress subjected such suits to a variety of substantial restrictions in the Private Securities Litigation Reform Act of 1995 (PSLRA), Pub. L. No. 104-67, 109 Stat. 737 (1995).

When some plaintiffs sought to avoid those limits by filing their federal securities claims as state-law suits instead, Congress responded by enacting SLUSA. *See Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 82 (2006). SLUSA generally provides for the removal and dismissal of a state-law complaint brought by fifty or more plaintiffs "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). (Citations to Section 78bb(f) are to SLUSA's amendment to the 1934 Securities Exchange Act; SLUSA adopted parallel amendments to the Securities Act of 1933 as well.) The terms "material" and "in connection with" in SLUSA have the same meaning as under Section 10(b) and Rule 10b-5. *Dabit*, 547 U.S. at 85-86.

The term "covered security" is limited to only a subset of "securities": those traded on a U.S. national exchange, such as the New York Stock Exchange, NASDAQ, or a similar exchange, 15 U.S.C. § 77r(b)(1), 17 C.F.R. § 230.146(b), or issued by a federally registered investment company, 15 U.S.C. § 77r(b)(2). Congress concluded that these "nationally traded securities" required special and distinct protections from state-law suits because issuers were unable to control the jurisdictions in which they were traded. The purpose of the statute is thus "to make Federal court the exclusive venue for most securities fraud class action litigation *involving nationally traded securities*." H.R. Rep. No. 105-803, at 15 (1998) (Conf. Rep.) (emphasis added). In order to preserve state regulatory authority over fraud involving other securities that were not traded on national markets, Congress imported the phrase "covered security" from the National Securities Markets Improvement Act of 1996, Pub. L. 104-290, 110 Stat. 3416 (1996), where its role is to divide regulatory authority between the federal and state governments so that the federal government takes responsibility for "national offerings of securities," while states and individuals "retain authority . . . to bring actions pursuant to State laws and regulations prohibiting fraud and deceit." H.R. Rep. No. 104-622, at 16, 34 (1996).

2. This case arises from the infamous Ponzi scheme of Allen Stanford. The outlines of the fraud are well known and not disputed. Stanford controlled the Stanford International Bank (SIB), located in Antigua. SIB sold approximately $7 billion in certificates of deposit to more than 25,000 people over fifteen years. The CDs were debt instruments, redeemable by the

purchasers. They guaranteed a fixed rate of interest, not connected to the performance of SIB's portfolio.

Implementing a classic Ponzi scheme, SIB actually covered interest payments and redemptions using part of the proceeds from new CD sales. Meanwhile, Stanford wasted the remainder of the investors' money on personal luxuries and unprofitable investments. To shore up the scheme, Stanford and his colleagues manipulated their financial statements and lied to regulators about their financial condition and performance.

When the fraud was eventually discovered and collapsed, the effect was devastating. Thousands of individuals – including a great many retirees and small business owners – lost their entire life savings. *See, e.g.*, *SEC v. Stanford Int'l Bank*, *Ltd.*, 424 Fed. Appx. 338, 340 (5th Cir. 2011) (considering request for relief of "a retired, widowed school teacher" who "invested her entire retirement, approximately $550,000" in SIB CDs that "are now virtually worthless").

Eventually, the government brought a successful civil suit against Stanford and others under Rule 10b-5, as well as a criminal prosecution for willful violations of Section 10(b). Jurisdiction was premised on the fact that the CDs "offered and sold by the Defendants are 'securities' under" the Securities Act, Exchange Act, Investment Company Act, and Advisers Act. First Amended Complaint, *SEC v. Stanford Int'l Bank, Ltd.*, No. 3:09-cv-298, at ¶ 8 (N.D. Tex. Feb. 27, 2009); *SEC v. Stanford Int'l Bank, Ltd.*, No. 3:09-cv-298, at 10 (N.D. Tex. Order Nov. 30, 2011) (holding that the SIB

CDs were "securities under the federal securities laws").

Private purchasers of the CDs sought to recover their losses as well. As is relevant here, three groups of purchasers brought four private civil suits under state law. The cases were consolidated on appeal and in this Court. The thrust of all the complaints is that the various defendants misled the plaintiffs into purchasing the CDs or otherwise facilitated the fraudulent sales of the CDs.

Two groups of Louisiana residents filed two complaints (*Roland v. Green* and *Farr v. Green*) under Louisiana law in Louisiana state court. *See* J.A. 232-306 (hereinafter "Roland Compl."), 317-399 (hereinafter "Farr Compl."). Both named as defendants entities and individuals who had been involved in selling the CDs: SEI Investments Company, the Stanford Trust Co., the Trust's employees, and the Trust's investment advisors. The complaints allege that the defendants misrepresented the CDs as a "safe investment vehicle" with "little or no risk" that would produce "consistent, double-digit returns." J.A. 246 (Roland Compl. ¶ 12), 337 (Farr Compl. ¶ 14). They also misrepresented SIB as "competent and proficient" and overseen by both the Antiguan government and independent auditors. *Id*. Specifically with regard to petitioner SEI, the complaints alleged that SEI marketed the SIB CDs with knowledge that they were unregistered, knowingly permitted its name to be used in connection with the marketing of the SIB CDs, recommended the SIB CDs and maintained investments in them without conducting proper diligence, and failed to disclose material information about the risk of the SIB CDs in

reports that it issued to the plaintiffs. *Id.* 275-80 (Roland Compl. ¶¶ 100-13), 368-73 (Farr Compl. ¶¶ 104-17).

Other purchasers of the CDs filed two separate complaints under Texas law in the District Court for the Northern District of Texas, which oversees the federal Stanford-related litigation under the Multidistrict Litigation statute. One (*Troice v. Willis*) named as defendants SIB's insurance brokers. *See* J.A. 612-735 (hereinafter "Willis Compl."). The complaint alleges that the defendants played a central role in the fraud by misrepresenting the CDs as, for example, "insured by Lloyd's," "regulated by the United States government," and subject to "regular stringent Risk Management Review" by outside auditors. *Id*. 629, 650 (Willis Compl. ¶¶ 36, 77). According to the complaint, Stanford employees drafted insurance endorsement letters that the Willis petitioners placed on their own letterhead "with the clear intention that said letters be used by Stanford Financial for marketing purposes to retain or obtain actual and prospective clients for SIB." *Id*. 636 (Willis Compl. ¶ 51). The close working relationship between the insurers and Stanford meant that "perhaps no other third party had as much knowledge of Stanford Financial's worldwide operations as BMB and Willis." *Id*. (Willis Compl. ¶ 50). Indeed, according to the complaint, the insurers knew that Stanford was engaged in a massive fraud, but rather than disclose it, they aided it by drafting marketing letters falsely representing that the SIB CDs were safe. *Id*. 659 (Willis Compl. ¶ 94).

In their second complaint (*Troice v. Proskauer*), the plaintiffs named as defendants two of SIB's law firms.

See J.A. 422-493 (hereinafter "Proskauer Compl."). The complaint does not allege any misrepresentations by the firms, which are instead alleged to have knowingly facilitated the fraud by assisting SIB in evading regulatory oversight. *Id.* 476-491 (Proskauer Compl. ¶¶ 97-116) Principally, Tom Sjoblom – a partner initially at Proskauer & Rose LLP and then at Chadbourne & Parke LLP – lied to regulators and suborned perjury by SIB officers. *E.g.*, *id*. 455, 468 (Proskauer Compl. ¶¶ 60, 83).

Invoking SLUSA, the defendants removed the *Green* cases from Louisiana state court to federal district court. The Judicial Panel on Multidistrict Litigation then transferred the cases to the Northern District of Texas. Pet. App. 8a. (Citations to Pet. App. are to the Petition Appendix in No. 12-79.) The defendants filed motions to dismiss all four complaints under SLUSA. *Id*. They urged the district court to adopt an expansive interpretation of the phrase "in connection with" and hold that SLUSA barred the complaints even though the SIB CDs were not covered securities and did not convey any interest in covered securities, and despite the fact that SIB's representations did not affect the market for covered securities. The plaintiffs argued that the complaints should not be dismissed under the settled meaning of that phrase in the context of actions under Section 10(b) and Rule 10b-5, where it is the basis for asserting federal court jurisdiction.

The district court granted the motions. *Id*. 47a-73a. Preliminarily, the district court recognized that although the CDs are "securities," they are *not* "covered securities," because they are not traded on a national

exchange. *Id*. 61a. Fraud in the sale of the CDs thus would not itself trigger SLUSA.

The district court nonetheless held that the statute justified dismissing the complaints on two theories. First, the court found it to be a proper "inference" that one factor which led the plaintiffs to purchase the CDs was SIB's representation that "the SIB CDs were backed, at least in part, by SIB's investments in SLUSA-covered securities." *Id.* 64a-65a & n.11. Second, the court concluded that the complaints "imply" that to purchase a CD "at least one of the Plaintiffs" liquidated an individual retirement account, which "commonly" include "SLUSA-covered securities." *Id.* 68a-69a.

A panel of the Fifth Circuit unanimously reversed. The court decided to resolve the case by announcing a general legal standard to govern all cases in which "the fraud alleged was centered around the purchase or sale of an uncovered security, like the CDs at issue in this appeal." *Id.* 20a. After surveying the precedent of this Court and other courts of appeals, the Fifth Circuit adopted the Ninth Circuit's holding that "fraud is 'in connection with' the purchase or sale of securities if there is a relationship in which the fraud and the stock sale coincide *or* are more than tangentially related." *Id.* 32a (emphasis added) (quoting *Madden v. Cowen & Co.*, 576 F.3d 957, 966 (9th Cir. 2009) (internal quotation marks omitted)).

SIB did not make its misrepresentations contemporaneously with (or in the course of) the same transaction as its separate supposed purchase of "liquid assets"; the two thus did not "coincide." The Fifth

Circuit further concluded that SIB's representation *about* those liquid assets did not transform the case into one precluded by SLUSA. SIB's statement about its asset portfolio was "but one of a host of (mis)representations made to the Appellants in an attempt to lure them into buying the worthless CDs." *Id.* 35a-36a. "[T]he heart, crux, and gravamen of their allegedly fraudulent scheme was representing to the Appellants that the CDs were a 'safe and secure' investment that was preferable to other investments for many reasons." *Id.* 36a; *see supra* at 5-7 (discussing allegations of the complaints). The court accordingly concluded that "the purchase or sale of securities (or representations about the purchase or sale of securities) is only tangentially related to the fraudulent scheme alleged by [respondents]." Pet. App. 33a.

The court of appeals further reasoned that its

> conclusion that the allegations do not amount to being "in connection with" transactions in covered securities is bolstered by the distinction between the present cases and the so-called "feeder fund" cases arising from the Madoff Ponzi scheme. The SIB CDs, in contrast to the funds in which many individuals invested with Madoff, were not mere "ghost entities" or "cursory pass-through vehicles" to invest in covered securities. The CDs were debt assets that promised a fixed rate of return not tied to the success of any of SIB's purported investments.

Id. 37a (internal citations omitted).

The Fifth Circuit finally rejected the district court's holding that SLUSA precludes the complaints because at least one plaintiff presumably sold covered securities to generate funds to buy a CD. This is not a case, the court explained, in which "the fraud depended upon the tortfeasor convincing the victims of those fraudulent schemes to sell their covered securities in order for the fraud to be accomplished." *Id*. 39a. Thus, any such sale of covered securities by a plaintiff "was not more than tangentially related to the fraudulent scheme and accordingly, provides no basis for SLUSA preclusion." *Id.* 40a.

SUMMARY OF THE ARGUMENT

The complaints in this case are not precluded by SLUSA because they do not allege "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). The plaintiffs instead allege fraud in connection with the sale of the SIB certificates of deposit, which were not covered securities and which did not convey any interest in any covered security. They further allege that the scheme included misrepresentations that were unrelated to covered securities, such as that the CDs were insured and that SIB was closely regulated and audited.

Petitioners assert that the complaints nonetheless contain three allegations that trigger SLUSA. Each theory would require a radical expansion of not only SLUSA, but also Section 10(b) and Rule 10b-5, both of which use the identical standard to establish federal jurisdiction for actions initiated by private plaintiffs and the government.

First, one petitioner argues that SLUSA applies because the fraud led at least one plaintiff to sell covered securities to generate capital to buy the CDs. But the securities laws do not apply when the sale of securities was an incidental consequence – as opposed to the design or objective – of the scheme. Otherwise, the federal securities laws would apply to fraud in the defendant's sale of any asset, such as a house or a car, whenever the purchaser liquidates securities to finance the transaction.

Second, petitioners assert that SIB's claim that it owned "liquid assets" triggers SLUSA. Even accepting petitioners' speculation that "liquid assets" means "covered securities," SIB's misrepresentation was not about any "purchase or sale." The securities laws apply only to misrepresentations that "coincide" with securities transactions, not misstatements "about" securities ownership. On petitioners' reading, every false statement about securities ownership – whether in a credit application, a job interview, or anywhere else – potentially constitutes securities fraud. Congress did not intend to undo the established allocation of federal and state regulatory authority in that fashion.

Third, petitioners maintain that SLUSA applies to SIB's supposed promise to use proceeds from the plaintiffs' CD purchases to buy additional liquid assets. In fact, SIB made no such promise. In any event, there is no support for that reading of the statute: petitioners and the government identify no cases concluding that such a misrepresentation is subject to the federal securities laws.

That is no surprise. The securities laws do not apply to the sale of a non-covered asset when the seller misrepresents its intent to buy covered securities in which no other party will hold any interest. Such a misstatement is not "material" to any covered securities transaction because it does not affect either the behavior of any investor in covered securities or the national market for covered securities. It is not "in connection with" the purchase of covered securities because the misstatement is made at the time of the earlier sale of the non-covered asset; it does not coincide with the later purchase of the covered security.

Nor does such a misrepresentation implicate the interests underlying the federal securities laws: protecting the integrity of and public confidence in the regulated securities market. As the United States has admitted, the Stanford Ponzi scheme "had no prospect of affecting the market in [covered] securities." U.S. Cert. Br. 12. Presumably, whenever SIB actually bought covered securities, it did so honestly on the open market. SIB's statement that it would buy additional liquid assets did not introduce any dishonesty or unfairness into any trade in covered securities. Nor did it otherwise erroneously induce any seller to make or avoid such a transaction.

Petitioners' argument would undermine other important policies underlying the securities laws. Congress enacted SLUSA to limit abusive securities litigation with only a tangential relationship to actual securities fraud. But petitioners' rule would achieve the opposite result: their broad interpretation of "in connection with" would expand federal jurisdiction under Rule 10b-5, permitting private purchasers and

the SEC to bring suit for garden-variety common-law frauds with any tangential relationship to any security. And any willful misstatement would be subject to prosecution as a federal felony. Under the rule of lenity, the courts will find such an expansion of federal criminal jurisdiction only upon a plain statement of congressional intent that SLUSA does not contain.

Congress also crafted SLUSA to respect the states' regulatory authority by limiting the statute to fraud in connection with transactions in "covered securities" traded on national markets. Congress chose that language to preserve state-law remedies relating to non-covered assets like the SIB CDs. Petitioners' expansive reading of the federal securities laws would, however, displace those remedies, raising substantial federalism concerns.

For those reasons, petitioners' argument is undermined, not supported, by this Court's precedent holding that secondary liability is not available in a private suit under Rule 10b-5. The Court reasoned that state rather than federal law should determine liability in cases not directly involving securities fraud. Yet petitioners' theory would extinguish state group remedies in many cases that have never been regarded as subject to the federal securities laws. Moreover, this Court concluded that it was appropriate to limit the scope of liability under Rule 10b-5. But petitioners' argument substantially expands federal securities liability by significantly broadening the meaning of the phrase "in connection with."

Congress also wanted SLUSA to be easily administrable at the outset of the litigation. But a

ruling in petitioners' favor could not be evenly or efficiently applied in later cases. It would be impossible for the lower courts to know, for example, whether the defendant's asset pool included a sufficient proportion of covered securities to trigger SLUSA preclusion. Nor is there any reason to open the door to the new array of securities claims that petitioners would invite.

Finally, the Court should not defer to the SEC's argument in its *amicus* brief that the securities laws apply to any material misstatement "about" securities transactions. That interpretation conflicts directly with this Court's precedents: frequently, a statement "about" a transaction will not "coincide" with the transaction, as in "we bought this house in 1984" or "SIB previously purchased a pool of liquid assets." The *amicus* brief represents an unexplained, dramatic change in the position of the agency, which apparently had not advocated this interpretation since the adoption of the 1934 Act.

The reason for the agency's change in position seems obvious: aggrandizement. The broader this Court's interpretation of "in connection with," the greater the SEC's authority to bring civil actions under Rule 10b-5 and the Justice Department's power to bring felony securities fraud prosecutions. The agency's *amicus* brief is not entitled to deference under this Court's precedent, but if it were, that precedent should be overruled.

ARGUMENT

Petitioners' briefs make it easy to confuse what this case is about, and what it is not about. It is not about the proper interpretation of any term unique to the Securities Litigation Uniform Standards Act. It is instead about the construction of language common to both SLUSA and the provisions that confer jurisdiction over federal securities fraud claims – Section 10(b) of the Securities Exchange Act and Rule 10b-5. The phrase on which petitioners rest their argument – "in connection with the purchase or sale" – is the doorway through which private parties and the government must pass in initiating any federal securities fraud action. That is the avowed reason the United States has filed an *amicus* brief supporting petitioners. Petitioners' plea to stretch that doorway so significantly that every material claim "about" regulated securities passes through it would warp the securities laws and set them against the very thrust of this Court's modern jurisprudence seeking to limit federal securities litigation.

The Fifth Circuit's judgment should be affirmed because the federal securities laws – including SLUSA – do not apply to a defendant's sale of a non-covered asset (here, the CDs) through a false claim of ownership or claim of intent to buy covered securities in which no other person will hold an interest. Such a misrepresentation is not made "in connection with" any transaction in covered securities, because the statement and the transaction are separate events and thus do not coincide. *See United States v. O'Hagan*, 521 U.S. 642, 656 (1997). Nor is the misstatement "material" to such a transaction, because it does not

affect investor behavior in the covered securities markets. *See Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988).

This Court can decide this case and provide substantial guidance to the lower courts without broadly articulating a general rule to govern every case in which representations about covered securities lead to the sale of a non-covered product. It need only address cases in which the defrauded party – here, the purchasers of the CDs – acquired no interest in the covered securities.

In an appropriate later case, this Court can consider whether SLUSA applies when the defrauded party instead holds some interest in the defendant's supposed portfolio of covered securities. In such a case, SLUSA may apply because the victim arguably purchases a share of the covered securities themselves, such that the fraud is "in connection with" a transaction in covered securities. That is the issue in the cases that petitioners cite involving so-called "feeder fund" investments in the Bernard Madoff Ponzi scheme. *E.g.*, *In re Kingate Mgmt. Ltd. Litig.*, No. 09-cv-5386, 2011 WL 1362106, at *8-*9 (S.D.N.Y. Mar. 30, 2011) (holding that SLUSA applied to investments in funds that "were essentially cursory pass-through vehicles by which investors could place their assets with Madoff, and the Funds placed the entirety of their assets with Madoff, making no independent investments whatsoever," all the while believing that they were actually "invest[ing] in the United States and in United States equities that are part of the S&P 100"). But that issue is not presented here.

To the extent this Court nonetheless follows the course of the Fifth Circuit and resolves this case on broader grounds, respondents endorse the court of appeals' holding that "fraud is 'in connection with' the purchase or sale of securities if there is a relationship in which the fraud and the stock sale coincide *or* are more than tangentially related." Pet. App. 32a (emphasis added) (citation and quotation marks omitted). Petitioners err in caricaturing the Fifth Circuit as holding "SLUSA inapplicable based on *other* alleged misrepresentations that did not relate to SLUSA-covered securities." Willis Br. 5 (emphasis in original) (citing nothing). In fact, if a complaint alleges a scheme involving unfairness or dishonesty in the market for covered securities, SLUSA applies because the fraud and the transactions "coincide," and it makes no difference whether the defendant also made other misrepresentations. But petitioners seek to extend SLUSA to fraud involving and affecting only transactions in *non*-covered securities. The court of appeals correctly held that in such a case, SIB's claim that it owned or would purchase liquid assets is at best only tangentially related to the purchase or sale of covered securities and therefore does not trigger SLUSA. Pet. App. 37a.

I. Under Well-Settled Law, The Complaints Do Not Allege Any Material Misrepresentation In Connection With The Purchase Or Sale Of A Covered Security.

Respondents allege that petitioners participated in or aided a fraudulent Ponzi scheme to sell the SIB CDs. It is uncontested that the fraudulent sale of the SIB CDs does not itself trigger SLUSA because the CDs

were not "covered securities." Instead, the CDs were simple, non-recourse debt instruments. *E.g.*, Pet. App. 37a. The interest rate was both fixed and guaranteed, not tied to the performance of SIB's portfolio of assets (including any covered securities). *Id*. And SIB's portfolio did not "back" the CDs – at least not in the meaningful sense that its assets were security for the plaintiffs' investment or determined the returns on that investment. *Contra* Chadbourne Br. 28. As discussed, the CDs conveyed no interest in SIB's assets. Put simply, then, misrepresentations about the CDs cannot be "in connection with the purchase or sale of a covered security," because the CDs are not covered securities, and do not convey any interest in covered securities.

The complaints' principal allegations of fraud similarly do not implicate SLUSA because they have nothing to do with covered securities. The defendants' scheme sought to mislead the plaintiffs into believing that the non-covered CDs were a safe and secure investment. Indeed, many of the petitioners – such as petitioner SEI and the law firm petitioners – are not alleged to have made any misrepresentations related to covered securities at all. Instead, the complaints allege misrepresentations about the CDs themselves.

For example, contrary to the erroneous, self-serving representation of the Willis petitioners that they are alleged to have "merely placed ordinary commercial insurance policies for SIB from Lloyd's of London," Br. 11, the complaints allege that the Willis petitioners knew of the fraud yet falsely stated that the CDs were insured – even allowing Stanford to distribute those representations on Willis's letterhead. *E.g.*, J.A. 637,

650 (Willis Compl. ¶¶ 52, 77). SIB and the law firm petitioners also falsely claimed that purchasers were protected from fraud because SIB was both heavily regulated and also regularly audited by a respected firm. *E.g.*, J.A. 485 (Proskauer Compl. ¶ 109). Petitioner SEI likewise marketed and facilitated investments in the unregistered and unlawful CDs. *E.g.*, J.A. 275-80 (Roland Compl. ¶¶ 100-13).

Without more, SLUSA does not apply. To the contrary, this is precisely the kind of case for which Congress preserved state-law claims by limiting SLUSA to fraud in connection with transactions in "covered securities." For the reasons that follow, petitioners' claims that the complaints nonetheless allege "a" single material misrepresentation in connection with the purchase or sale of a covered security lack merit.

II. SLUSA Is Not Triggered By The Plaintiffs' Supposed Sale Of Covered Securities To Purchase The CDs.

Petitioner Proskauer Rose alone argues (Br. 37-38) that SLUSA bars the complaints because the fraud led to a transaction in covered securities – not by SIB, but by one of the plaintiffs. Proskauer endorses the district court's theory that SLUSA applies because "at least one of the Plaintiffs acquired SIB CDs with the proceeds of selling SLUSA-covered securities." Pet. App. 69a. The principal importance of this theory is that it demonstrates the implausible implications of petitioners' attempt to give the securities laws their broadest possible construction.

Proskauer's argument fails because SIB's misrepresentations about the CDs were not "in connection with" those sales of other securities. To be sure, the securities laws do apply to a scheme in which the victim is induced to sell securities and then deprived of the proceeds. *See Superintendent of Ins. v. Bankers Life & Cas. Co.*, 404 U.S. 6, 10 (1971). But here, the complaints merely allege that SIB instructed its agents to "push" the CDs. J.A. 440-41. They do not allege – and there is no evidence – that the scheme's design or objective was to steal the plaintiffs' covered securities or to convert the plaintiffs' covered securities into worthless non-covered CDs, or that SIB's agents were instructed to (or in fact did) encourage the plaintiffs only to sell their covered securities. By all accounts, SIB did not care where the plaintiffs got the money to buy the CDs – whether from using cash on hand, taking out a loan, selling real property, liquidating securities, or some other source.

Imagine the radical consequences of Proskauer's contrary theory that an incidental sale of covered securities by one of the victims is made "in connection with" the fraudulent sale of SIB CDs. The same logic would apply to schemes to fraudulently sell *any* item – *e.g.*, a house, timeshare, car, or boat – that happens to be purchased even in part with the proceeds from liquidation of securities. Proskauer's theory would apply so long as *one* member of a large group of plaintiffs sold a share of stock to finance the purchase. SLUSA would immunize the defendants from traditional state-law group remedies. Meanwhile, the victims could bring individual securities fraud suits against the seller of the property in federal court under Rule 10b-5.

In addition, the government could bring its own securities fraud actions under the Rule. If the fraud were willful, the government could prosecute the seller for a felony. Indeed, the government's power to bring those actions is broader than SLUSA's limitation because Section 10(b) and Rule 10b-5 apply to misrepresentations in connection with transactions in "*any* security," not merely "covered" securities. The "in connection with" requirement is thus the principal check on the government's ability to threaten liability, a check which would be undermined by Proskauer's sweeping reading.

III. SLUSA Is Not Triggered By SIB's False Claim That It Owned An Existing Portfolio Of Liquid Assets.

Petitioners next argue that SLUSA applies to the complaints' allegation that SIB falsely claimed to own "liquid assets." That argument lacks merit for several reasons.

A. Preliminarily, petitioners dramatically overstate this allegation. Plaintiffs do not allege that SIB represented that its portfolio of "liquid assets" was composed exclusively – or even substantially – of "covered securities" traded on a U.S. national exchange. Petitioners' contrary assertion is speculation. *Accord* U.S. Cert. Br. 21 (recognizing that the status of the liquid assets as covered securities is an assumption or inference). SIB explained that its liquid assets constituted "a well-diversified portfolio of highly marketable securities issued by stable national governments, strong multinational companies, and major international banks." J.A. 444 (Proskauer

Compl. ¶ 41). SIB was an offshore bank in Antigua with access to massive global markets. So no plaintiff could have understood that his or her individual purchase would necessarily lead SIB to buy securities traded on a U.S. exchange. *Cf. Morrison v. Nat'l Austl. Bank Ltd.*, 130 S. Ct. 2869, 2885-86 (2010) (holding that the securities laws do not apply extraterritorially, and acknowledging that other countries have robust securities markets with elaborate regulatory schemes of their own).

B. Even a false representation by SIB that it owned "covered securities" would not trigger SLUSA. Petitioners' assertion that "misrepresentations about covered securities are clearly sufficient to satisfy the 'in connection with' requirement and trigger SLUSA," Willis Br. 34 (emphasis omitted) (citing nothing), thumbs its nose at the plain statutory text. A false claim to *own* covered securities is not made "in connection with" the "*purchase or sale of*" those assets. The federal securities laws – including SLUSA – by their terms do not apply to misstatements about the ownership of securities in which the defrauded party has no interest; they apply only to misrepresentations in connection with the "purchase or sale" of regulated securities. The statutes thus protect the integrity of trading in securities markets. That limitation must be respected, not overridden. If petitioners' reading were correct – *i.e.*, if every claim to "own" securities could be reconceived as a claim to have previously purchased those securities – Congress would have written the statutes to apply to misrepresentations "in connection with covered securities."

Even on petitioners' contrary view that every statement "about" securities purchases is *ipso facto* made "in connection with" those purchases, *e.g.*, Chadbourne Br. 24, the complaints do not allege that SIB misrepresented its "purchase" of its existing portfolio. For example, SIB did not misstate the manner or timing of how it acquired those assets. Petitioners presumably want this Court to *infer* that allegation. That is impermissible; by its terms, SLUSA looks to the complaint's actual allegations. But here the inference is also implausible: SIB never made the representation that petitioners attribute to it. SIB did not discuss when or how its portfolio was acquired.

C. In any event, SLUSA would not apply even if SIB had expressly made a false claim specifically about its purchase of a portfolio of covered securities, because there is no merit to petitioners' proposed legal rule. The securities laws are not triggered by every false statement "about" a securities transaction. In SLUSA, Congress "imported" decisions that had construed the identical phrase – "in connection with a purchase or sale" – under Section 10(b) of the 1934 Exchange Act and Rule 10b-5. *Dabit*, 547 U.S. at 86. Under that settled body of law, a misstatement occurs "in connection with" the "purchase or sale" of securities only if it "coincides" with that transaction – and not if it merely describes the transaction. *O'Hagan*, 521 U.S. at 656.

Thus, in *O'Hagan*, the Court concluded that a lawyer violated Section 10(b) by using confidential information from his firm to gain an advantage in securities trades. The scheme was "in connection with the purchase or sale" of the securities because it

"coincided" with the trades: the misappropriation was complete only once the information was misused through trading. 521 U.S. at 656 ("[T]he fiduciary's fraud is consummated, not when the fiduciary gains the confidential information, but when, without disclosure to his principal, he uses the information to purchase or sell securities"). The Court's interpretation of "in connection with" was also informed by the policies underlying the securities laws. In such a case, the misappropriator "deceives the source of the information and simultaneously harms members of the investing public," *id.*, because "investors likely would hesitate to venture their capital in a market where trading based on misappropriated nonpublic information is unchecked by law," *id.* at 658. *See also Dabit*, 547 U.S. at 85, 89 (applying SLUSA to hold that brokerage's attempted "fraudulent manipulation of stock prices" coincided with contemporaneous stock sales, and therefore was in connection with sales, without regard to whether the plaintiffs were themselves purchasers or sellers); *SEC v. Zandford*, 535 U.S. 813, 820 (2002) (applying Rule 10b-5 to hold that broker who had sold client's securities and kept the proceeds for his own benefit had engaged in securities fraud because "[t]he securities sales and respondent's fraudulent practices were not independent events," so that the "fraud coincided with the sales themselves").

In this case, the fraud that induced the plaintiffs' purchases of the CDs did not coincide with SIB's supposed prior "purchase" of its supposed existing pool of liquid assets. At the time the plaintiffs bought the CDs, SIB claimed already to own those assets; by

definition, the prior "purchase or sale" of those assets was already complete.

Put another way, even on petitioners' characterization of SIB's representations, SIB misstated its *prior* securities purchases to establish its *present* creditworthiness. Imagine that SIB sold the CDs through the following false representation: "we can repay you because we bought 1 million shares of IBM six months ago." Or take the analogous purchase of another non-security that would be equally subject to petitioners' rule – a vehicle – based on the misrepresentation that "I can afford to repay this car loan because I own 1000 shares of IBM." The fraudulent sale of the CDs and the purchase of the car of course both "coincide" with the misrepresentation – all such frauds do. But under the securities laws the dispositive point is that neither "coincides" with the prior "purchase" of the IBM shares.

Petitioners' counter-argument is that SIB's misrepresentation about its prior securities purchases was part of a common scheme with its fraudulent sales of the CDs, so the two "coincide." But that is not the connection between fraud and securities transactions that triggers SLUSA. Instead, the defendant's misrepresentation must "coincide" with the transaction in the covered security; there must be a material misrepresentation "in connection with the purchase or sale" of *that* security. Here, SIB was not engaged in any scheme – over however long a period of time – to make misrepresentations in its purchase or sale of "covered securities." So SLUSA does not apply.

The fact that the federal securities laws – including SLUSA – do not apply in a case like this one is no accident or technicality. The statutes are directed at fraud in connection with transactions in regulated securities because their purpose is to preserve public confidence in and the integrity of the regulated securities markets on which those transactions occur. *O'Hagan*, 521 at 658 (explaining that an "animating purpose of the Exchange Act" is "to insure honest securities markets and thereby promote investor confidence"); *Zandford*, 535 U.S. at 819 (same); *see also Morrison*, 130 S. Ct. at 2884 (explaining that Section 10(b) "does not punish [all] deceptive conduct," but instead "seeks to regulate" only certain "purchase-and-sale transactions" in securities, and to "protect" only the "parties or prospective parties to those transactions") (internal quotation marks, citations, and alterations omitted).

By contrast, a misrepresentation like SIB's – that a party owns or previously purchased a portfolio of covered securities – does not, without more, substantially implicate those interests. It does not, for example, introduce any dishonesty into any transaction in any covered security or make it any less likely that any party would buy or sell securities on a U.S. national exchange. SIB's misrepresentations instead implicate ordinary state-law anti-fraud rules.

D. Petitioners' argument also must be rejected because, as discussed in more detail *infra*, it would override the allocation of federal and state regulatory authority traditionally recognized by the securities laws. Garden-variety fraud claims that have historically fallen within the province of the states

would be transformed into federal securities fraud cases. Individuals and businesses constantly make indistinguishable claims that they own assets (including securities) in asserting that they are reliable business partners or that they can repay debts. *See, e.g.*, *In re Oster*, No. 10-12629, 2011 WL 739539, at *1 (E.D. Mich. Feb. 24, 2011) (debtor represented that he owned millions of dollars in "marketable securities" to obtain bank loan).

Other hypotheticals trip off the tongue. Take an individual who applies for a car loan claiming to own assets including shares of Google stock, but overstates the number of shares or their value. Or a party seeks funding to purchase a building, falsely listing among his assets recently purchased shares of Xerox. In the commercial context, imagine that a party issues non-covered debt, stating that it can make interest payments because it owns a variety of revenue-generating or liquid assets, including commercial real estate, an operating business, and shares of Apple Computer, Inc.

Indeed, a ruling in petitioners' favor would extend the securities laws well beyond credit transactions, or indeed transactions of any kind. Parties misstate their stock holdings in diverse contexts. Debtors try to hide assets from creditors. *See In re Geller*, 314 B.R. 800 (Bankr. N.D. 2004) (debtor denied discharge after misrepresenting value of stock). Divorcing spouses conceal assets from each other. *See Macar v. Macar*, 803 So. 2d 707, 709 (Fla. 2001). Criminal defendants misrepresent their assets to courts. *Cf. United States v. Greig*, 2013 U.S. App. LEXIS 9935 (1st Cir. 2013) (bail determination); *United States v. Birrell*, 470 F.2d

113 (2d Cir. 1972) (Friendly, J.) (application to proceed *in forma pauperis*). The lovelorn overstate their wealth to get dates. *Cf.* SOME LIKE IT HOT (Ashton Productions 1957) (in which Tony Curtis impersonates the heir to Shell Oil in an effort to seduce Marilyn Monroe). And so on.

In fact, petitioners' interpretation extends the federal securities laws even further, to a party's statements about the holdings of third parties. For example, credit bureaus have been known to understate individuals' assets. *Cf. Dun & Bradstreet v. Greenmoss Builders*, 472 U.S. 749, 751 (1985). Biographers may misstate the holdings of their subjects. And applicants for jobs at trading firms misstate their experience in buying and selling stocks.

On petitioners' theory, those misstatements, if material to any transaction or interaction, all violate the federal securities laws because they were made "about," and therefore "in connection with," the prior purchase of the covered securities. The government may institute a civil securities fraud action and, if the misstatement was willful, a felony prosecution. Meanwhile, SLUSA bars any state-law class action to remedy the fraud.

Such a radical expansion of federal regulatory authority and parallel diminishment of traditional state police powers raises grave federalism concerns. That reading must be rejected, because "courts should assume that 'the historic police powers of the States' are not superseded 'unless that was the clear and manifest purpose of Congress.'" *Arizona v. United States*, 132 S. Ct. 2492, 2501 (2012) (quoting *Rice v.*

Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947)). SLUSA obviously does not manifest such a purpose.

IV. SLUSA Does Not Bar A Complaint Alleging That The Defendant Fraudulently Sold A Non-Covered Asset Through A False Promise To Use The Proceeds To Purchase Covered Securities For Itself.

Petitioners finally argue that the complaints allege that SIB falsely promised to use the proceeds from the plaintiffs' CD purchases to acquire covered securities. This is not an appropriate case in which to decide that question. Even if this Court were to accept petitioners' legal theory, SLUSA would not apply to the allegations of these complaints.

Unquestionably, the *Roland* and *Farr* complaints do not allege that SIB represented to those plaintiffs that it would use the proceeds of CD sales to purchase additional assets. Nor could the Court fairly imply such an allegation, which would be only incidental to the plaintiffs' claim of fraud in the sale of the non-covered CDs. So those suits may go forward even if petitioners were to prevail on this theory.

Petitioners' argument instead arises from the two *Troice* complaints. *E.g.*, J.A. 433 (Proskauer Compl. ¶ 24) (alleging misrepresentation that "investments in the CDs were liquid and the CDs could be redeemed at any time because SIB, through Stanford Financial, invested the money in safe, secure and liquid assets"); *id.* 628 (Willis Compl. ¶ 34) (same). Petitioners assert that the *Troice* plaintiffs' allegations are analogous to a claim that SIB falsely "represented that SIB would

invest plaintiffs' money in AAA-rated covered securities, but actually invested them in much riskier covered securities." Chadbourne Br. 31.

That analogy fails for two reasons. First, the hypothetical presumes that the plaintiff would hold an interest in the securities. That is not true of SIB's CDs. *See supra* at 18.

Second, SIB did not promise to use money from any particular plaintiff to buy anything. Instead, SIB represented its general practice. The contract for sale of the CDs is controlling, and it includes no such agreement. Under the securities laws, that is a critical difference. Petitioners' argument also depends on speculation because the "liquid assets" that SIB ostensibly said it would purchase do not equate with "covered securities." *See supra* at 21-22.

In any event, for the reasons that follow, SLUSA would not preclude the complaints even if SIB had promised to purchase additional securities with the proceeds of the plaintiffs' CD purchases.

A. SLUSA "Imports" The Previously Settled Interpretation Of "In Connection With" Under Section 10(b) and Rule 10b-5, Which Have Never Been Construed As Petitioners Propose.

1. Congress would not have regarded a suit like this one as a vexatious form of securities litigation that should be precluded by SLUSA, given that such claims have always been brought under state law, not subject to the federal securities laws. In the eight decades

since the Exchange Act's adoption, no administrative or judicial ruling at any level of the federal system – by the SEC, a district court, a court of appeals, or this Court – has ever extended Section 10(b) or Rule 10b-5 to a case like this one. Petitioners and the government identify no case arising from the fraudulent sale of a non-security based on the defendant's mere representation that it will use the proceeds to purchase a security in which no other party will hold any interest. That includes any case in which the security would increase the value of the fraudulently sold non-security. To the contrary, it previously has been settled that the federal securities laws look to "the product that was marketed to the investor, not what the defendant actually did with the investor's money." *Instituto de Prevision Militar v. Merrill Lynch*, 546 F.3d 1340, 1352 (11th Cir. 2008). *See also Ring v. Axa Fin., Inc.*, 483 F.3d 95, 100-02 (2d Cir. 2007).

Petitioners note that – as the SEC's civil suit and the criminal prosecution against Stanford demonstrate – SIB's sales of the CDs were subject to Rule 10b-5. That is true, but misleading. It is only true because of the coincidence that the non-covered asset which SIB sold (the CDs) happened also to be a "security" subject to Section 10(b) and Rule 10b-5. *See supra* at 4. It is misleading because petitioners' legal rule applies much more broadly to misrepresentations "about" securities in the course of *any* transaction. The federal securities laws would equally apply to a suit alleging fraud by a borrower (or a purchaser on credit), if the defendant promised to purchase stocks that could be liquidated to pay the debt. *See supra* at 26-28. They also would apply if the defendant falsely promised to sell an existing (or non-existent) stock portfolio to resolve any

obligation. And they would apply if two people enter into a business partnership, in which one promises to finance the venture, misrepresenting his securities holdings in the process to secure more favorable partnership terms.

For example, this Court held unanimously that FDIC-insured certificates of deposit issued by U.S. banks are not "securities" at all. *Marine Bank v. Weaver*, 455 U.S. 551, 559 (1982). In the same case, the Court held that a profit-sharing agreement between two parties, "negotiated one-on-one," was likewise "not a security." *Id*. at 560. But if petitioners prevail, they will create an end-run around *Marine Bank*. Any time an FDIC-insured CD is marketed using representations about securities, or any time the negotiations for a one-on-one agreement involve similar representations, the specter of federal securities liability will loom. Put simply, the federal securities laws would come to overlap not only with all fraud laws, but all contract law, any time any statement about a security is material to a transaction.

The government's statement that "the scheme here differs from the paradigmatic SLUSA-precluded case," U.S. Br. 19, is the closest it can come to a frank acknowledgment that it has never seen such a case dismissed under SLUSA. The government does say that the "lower courts have recognized that the 'in connection with' requirement can be satisfied when a party falsely promises to carry out a securities purchase or sale or falsely claims to have done so." *Id.* 20. But it cites no case in which the defendant falsely promised to purchase the securities for *itself*. In most of the cases it cites, the defrauded party held (or would

have held, but for the fraud) an interest in the regulated securities. *See Instituto de Prevision Militar*, 546 F.3d at 1349 ("[T]he investor could state a claim for fraud under § 10(b) even though securities were never purchased on his behalf. It was sufficient that the manager accepted and deposited [the investor's] monies as payment for securities with no intent to deliver them.") (internal quotation marks and citation omitted); *In re Herald, Primeo, & Thema Sec. Litig.*, No. 09-289, 2011 WL 5928952, at *8 (S.D.N.Y. Nov. 29, 2011) ("Madoff's announced intention to purchase covered securities (*i.e.*, stocks and options) for the benefit of Funds in which Plaintiffs invested satisfies the requirement that Plaintiffs' claims against JPM and BNY, Madoff's bankers, were made 'in connection with the purchase or sale of a covered security.'") (quoting SLUSA); *Barron v. Igolnikov*, No. 09-4471, 2010 WL 882890, at *4-*5 (S.D.N.Y. Mar. 10, 2010). In the others, the defendant was a trader who falsely claimed to have executed trades for others. *See In re Orlando Joseph Jett*, Admin. Pro. File No. 3-8919, 2004 WL 2809317, at *22 (Mar. 5, 2004); *In re Richard J. Line*, Admin. Pro. File No. 3-9134, 1996 WL 582948, at *2 (Sept. 30, 1996).

The few cases that petitioners cite (Willis Br. 38-40) are easily distinguished as well. In some, the plaintiffs lost money when funds ostensibly invested for their benefit were misappropriated. *See Grippo v. Perazzo*, 357 F.3d 1218, 1220-21 (11th Cir. 2004); *Horattas v. Citigroup Fin. Markets Inc.*, 532 F. Supp. 2d 891, 893 (W.D. Mich. 2007) (holding that SLUSA applied to allegation that the manager of an endowment breached fiduciary duty by liquidating covered securities in favor of imprudent investments, thereby

harming plaintiff beneficiaries); *Scala v. Citicorp*, No. 10-3859, 2011 WL 900297, at *1 (N.D. Cal. Mar. 15, 2011) (alleging a "'Madoff-style' Ponzi scheme" in which the perpetrator held "himself out as an investment consultant who would invest money on client's behalves"). In others, the defendant's misrepresentations manipulated the market for covered securities. *See U.S. Mortgage, Inc. v. Saxton*, 494 F.3d 833, 845 (9th Cir. 2007) (holding that SLUSA applied when publicly traded company made material misstatements in financial statements in an effort to manipulate its stock price). And the remainder (Willis Br. 40 & n.10) refer to the Madoff "feeder fund" cases, distinguished *supra* at 16. None of these cases are remotely similar to this one – *i.e.*, a case involving only transactions in non-covered securities that do not convey any interest in covered securities, and in which the defendants' fraud does not implicate public confidence in or the integrity of the market for covered securities.

2. Petitioners' inability to cite a single case on point is no surprise. The securities laws do not apply to a party's sale of a non-covered asset through a false statement of an intention later to buy a covered security for itself. The misrepresentation is neither made "in connection with" nor "material" to the purchase or sale of the covered security.

a. Such a misrepresentation does not "coincide" with the purchase of a covered security. The fraud – the sale of the non-covered product – is complete before any later purchase or non-purchase of a covered security. Here, plaintiffs allege that SIB committed fraud in the sale of the CDs. That fraud was complete

immediately, and certainly well before SIB would have gone on to invest the proceeds. The transactions were thus distinct. By contrast, in *O'Hagan*, the Court found it critical that the defendant's fraudulent misappropriation was not complete until he used the information to purchase securities. *See supra* at 24.

It is not enough that the fraud and the later purchase of covered securities could be characterized as part of a common scheme. In *O'Hagan*, the Court rejected a very similar argument. The Court agreed with the SEC that Section 10(b) would not apply to a scheme to embezzle funds to purchase stocks. "[M]oney can buy, if not anything, then at least many things; its misappropriation may thus be viewed as sufficiently detached from a subsequent securities transaction that § 10(b)'s 'in connection with' requirement would not be met." 521 U.S. at 656-57. The Court found it significant that such a scheme would not implicate the statute's purpose "'to insure the maintenance of fair and honest markets.'" *Id.* at 657 (quoting 15 U.S.C. § 78b). That precise logic applies here. Like the embezzlement hypothesized in *O'Hagan*, SIB's fraud was in misappropriating the plaintiffs' funds by selling worthless CDs. SIB could have used other funds – including its own cash on hand – to purchase additional liquid assets.

In *O'Hagan*, Justice Thomas forewarned that parties in later cases – like petitioners and the SEC here – would try to evade any sensible limits on the application of the securities laws. The result, he warned, would be "inconsistent and incoherent interpretation of the relevant statutory language." 521 U.S. at 692 (Thomas, J., concurring in part and

dissenting in part). The significant further extension of the federal securities laws now proposed by petitioners "is no better than an ad hoc interpretation of statutory language [that] can provide no basis for liability." *Id.* Petitioners' attempt in this case to eliminate those sensible limits should be rejected.

Petitioners' contrary argument that because SLUSA contains the word "connection," it reaches frauds with even highly attenuated relationships to covered securities transactions (Proskauer Br. 22-23) has numerous flaws. The securities laws actually use the phrase "in connection with," which is distinct (indeed an entirely different part of speech) from the word "connection." This Court's settled precedents interpret that phrase to require that the fraud and the transaction "coincide." And in any event, the word connection has the strained reading that petitioners embrace only in the hyper-literal sense that "'really, universally, relations stop nowhere,'" which this Court has repeatedly rejected. *N.Y. State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 655-56 (1995) (quoting HENRY JAMES, RODERICK HUDSON xli (New York ed., World's Classics 1980)). This Court has refused to read such a phrase with "uncritical literalism," because otherwise "for all practical purposes pre-emption would never run its course." *Dan's City Used Cars, Inc. v. Pelkey*, 133 S. Ct. 1769, 1778 (2013) (citing *N.Y. State Conference*, 514 U.S. at 655). *See also, e.g.*, *Egelhoff v. Egelhoff*, 532 U.S. 141, 147 (2001).

b. Petitioners' argument also cannot be squared with SLUSA's requirement that there be a "misstatement" that is "material" to the purchase or

sale of the covered security. In *Basic Inc. v. Levinson*, the Court held that a statement is "material" if it would be "significant to the trading decision of a reasonable investor." 485 U.S. 224, 235 (1998). That will be true when there is a "substantial likelihood" that it would "significantly alter[] the 'total mix' of information made available." *Id.* at 231-32.

The only transactions in covered securities implicated by petitioners' theory were SIB's purchases for itself. Petitioners are reduced to arguing that "[h]ere, that 'someone' [who purchased covered securities] was SIB." Willis Br. 38. But petitioners never offer a theory of how a statement like SIB's could be material to its own purchase or sale of a covered security. SIB knew when it intended to buy securities, and (more often) when it did not. It was not misled at all, much less materially. By analogy, a plaintiff who purchases securities based on a representation that it *knows* to be false would obviously have no claim for securities fraud. So too for SIB.

SIB thus did buy some liquid assets, just vastly fewer than it represented. *See, e.g.*, J.A. 594 (Walther Aff. ¶ 9) (stating that as of December 2008, cash and equivalents represented nine percent of SIB's portfolio, and investments with money managers, including some liquid assets, represented approximately ten percent). But there is no allegation that those transactions involved material misstatements by any party, nor any allegation that the transactions were conducted in anything but an honest and open manner. SIB presumably paid the market price, without any unfair advantage over its counterparties or others in the market, and there is no allegation to the contrary.

Nor did SIB's false statement of an intention to buy additional securities have any other material effect on the national securities markets. As the United States explained at the certiorari stage, in an exceptionally important point that it omits without explanation from its brief on the merits: "the investors to whom the misrepresentations were made never purchased any covered securities themselves, and the fraud had *no prospect* of affecting the market in such securities." U.S. Cert. Br. 12 (emphasis added).

Petitioners' contrary argument is that the complaints allege that SIB's false statement of intent to buy more covered securities was material to sale of the non-covered CDs. *E.g.*, Willis Br. 11 (arguing that the misrepresentations "were a material part of Stanford's scheme" to sell CDs); *see also* Chadbourne Br. 37. But the securities laws ask whether the misstatement was "material" to the purchase or sale of the regulated security, *i.e.*, whether it would be "viewed by the reasonable investor as having significantly altered the 'total mix' of information available" regarding *that* security. *E.g.*, *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1318 (2011) (holding that information relating to adverse effects from a pharmaceutical company's products is "material") (quoting *Basic*, 485 U.S. at 231-32). For SLUSA's purposes, the misrepresentation must be material to the transaction in the *covered* security.

SLUSA thus is not triggered by the fact that the fraud had a material effect on the party's purchase of some other, non-covered asset. On petitioners' contrary view, the securities laws apply to misstatements that have *immaterial* consequences for securities

transactions, if they materially affect anything else. That would stretch Section 10(b) and Rule 10b-5 to protect participants in the market for non-covered assets, and would extend SLUSA to transactions that Congress expressly excluded from its ambit. Petitioners' attempt to expand the securities laws makes no sense, and the statutes have never been construed in that fashion.

c. Petitioners argue to the contrary that their position is supported by decisions holding that the federal securities laws apply even when the defrauded party or the plaintiff in the case was not a party to any securities transaction. *E.g.*, Willis Br. 38. That argument is a straw man. Respondents do not argue that SLUSA is inapplicable because no plaintiff traded in covered securities. Rather, SIB's misstatement did not coincide with, and was not material to, the "purchase or sale of a covered security" by *any* person – whether or not a party to this case. *Dabit*, 547 U.S. at 85.

The three cases cited by petitioners are thus unhelpful to their argument. In *Dabit*, the Court held that SLUSA applied to the claims of plaintiffs who "owned and continued to own" securities – so-called "holders." *Id*. at 76. In contrast to this case, it was uncontested (and dispositive) that the defendant's misrepresentations materially affected transactions in covered securities by other parties: the complaint alleged that Merrill Lynch "used its misinformed brokers to enhance the prices of its investment banking clients' stocks" causing "clients and brokers both [to] continue[] to hold their stocks long beyond the point when, had the truth been known, they would have

sold"; moreover, "when the truth was actually revealed . . . the stocks' prices plummeted." *Id.* at 75. The Court held that this misconduct – "fraudulent manipulation of stock prices – unquestionably qualifies as fraud 'in connection with the purchase or sale of securities.'" *Id*. at 89. The misrepresentation was accordingly subject to Rule 10b-5. The Court held that the plaintiffs' status as "holders" of covered securities was not relevant under SLUSA; it affected only their standing to sue under the Rule. *Id.*

In *O'Hagan*, the defendant defrauded his law firm, which did not engage in securities trades. *See* 521 U.S. at 647. But the Court specifically found that the misappropriation coincided with the defendant's securities trades; the fraud was not "consummated" until those transactions occurred. *See id.* at 656; *see also supra* at 24. Furthermore, because the defendant's possession of confidential information gave him an unfair advantage, it was uncontested that the fraud was material to trading in the market. *See* U.S. Br., *O'Hagan*, at 4 n.1.

And in *Zandford*, the defendant misappropriated his clients' stocks by trading them and converting them to his own use. 535 U.S. at 815-16. Again, the link to trading was obvious: the defendant effectively stole the clients' shares and then sold them. Such a scheme "represents an even greater threat to investor confidence in the securities industry" because it "undermines the value of a discretionary account," a principal mechanism by which retail investors participate in the market. *Id.* at 822.

B. Petitioners' Reading Would Undermine SLUSA's Central Purposes.

Petitioners err in their constant refrain that the Fifth Circuit's judgment should be reversed because the phrase "in connection with" should be given a "broad" construction to reach "complex frauds." *E.g.*, Proskauer Br. 24; Chadbourne Br. 25-26. "Broad" is not a rule of decision. If it were, then every fraud with any relationship to covered securities would be immune from state-law group actions under SLUSA and subject to claims for securities fraud under Rule 10b-5. It would reach, for example, Proskauer's astounding theory – which the other petitioners seemingly hope goes unnoticed – that a single plaintiff's incidental sale of securities to purchase an asset triggers the securities laws. But that is not the law. Every statute has its limits, and petitioners' argument exceeds SLUSA's.

This Court has repeatedly explained that the phrase "in connection with" "must not be construed so broadly as to convert every common law fraud that happens to involve securities into a violation of § 10(b)." *Zandford*, 535 U.S. at 820. *See also The Wharf (Holdings) Ltd. v. United Int'l Holdings*, *Inc*., 532 U.S. 588, 596 (2001) (holding that Section 10(b) should not be read to "permit numerous plaintiffs to bring federal securities claims that are in reality no more than ordinary state breach-of-contract claims"); *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 472 (1997) (holding that "to bring within the ambit of the Rule all breaches of fiduciary duty in connection with a securities transaction" would "'add a gloss to the operative language of the statute quite different from its commonly accepted meaning'") (citation omitted); *Chiarella v. United States*, 445 U.S.

222, 232 (1980) ("[N]ot every instance of financial unfairness constitutes fraudulent activity under § 10(b).").

Instead, the language must be construed flexibly in order to "*effectuate its remedial purposes*," *Zandford*, 535 U.S. at 819 (emphasis added) (citation and quotation marks omitted), and address "the particular concerns that culminated in SLUSA's enactment," *Dabit*, 547 U.S. at 86. As just explained, SIB's misstatements do not implicate the securities laws' *raison d'être*: to protect the integrity of and public confidence in the federally regulated market for covered securities. For three further reasons, petitioners' interpretation would not fulfill the purpose of the securities laws, including SLUSA; it would affirmatively undermine them.

1. Congress sought to limit vexatious litigation alleging tenuous claims of securities fraud "involving *nationally traded* securities" – *i.e.*, covered securities. *Id*. at 81 (emphasis added). SLUSA thus embodies "the congressional preference for national standards for securities class action lawsuits involving nationally traded securities." *Id.* at 87.

The Fifth Circuit's ruling fulfills Congress's purpose. Because it conforms to the settled understanding of the phrase "in connection with," *see supra* at 30-31, it applies SLUSA to cases involving frauds in connection with "nationally traded securities" that are subject to Rule 10b-5 and in turn to the restrictions imposed by the PSLRA. Petitioners' interpretation does not; there is no precedent for recognizing an allegation of this type involving fraud in

connection with non-securities assets as a basis for jurisdiction under Rule 10b-5.

Indeed, petitioners' theory would undermine Congress's goal of limiting securities fraud litigation. The phrase "in connection with" is a double-edged sword: reading it broadly does limit state-law group actions under SLUSA, but it also expands the right of private civil litigants and the government to bring securities fraud suits under Rule 10b-5. The same phrase appears in both provisions; in Rule 10b-5 it is the basis for recognizing federal jurisdiction. *See supra* at 15. That is why the government supports petitioners.

If petitioners prevail, the number of federal securities lawsuits will rise as plaintiffs invoke federal remedies and the discovery provided by the federal rules of civil procedure in numerous cases that previously were regarded as ordinary state-law fraud claims. In turn, the Department of Justice would have broader jurisdiction to bring federal criminal prosecutions. *See* 15 U.S.C. § 78ff(a) (specifying criminal penalties for willful violations of Section 10(b) and Rule 10b-5). As Justice Scalia explained in parallel circumstances in *O'Hagan*, the securities laws do not contain the clear statement of congressional intent required by the "principle of lenity" to expand federal criminal liability in that fashion. 521 U.S. at 679 (Scalia, J., concurring in part and dissenting in part).

2. Petitioners' interpretation also undermines Congress's decision in SLUSA to preserve – not to override or displace – the states' historical role in

providing civil remedies for fraud. The statutory history demonstrates that Congress recognized "the importance of maintaining the vital role of state law in regulating *non*-national securities." Pet. App. 28a (emphasis added). Congress preserved "the appropriate enforcement powers for state regulators, and the right of individuals to bring suit." S. Rep. No. 105-182, at 8 (1998). What Congress left to state law is just as important as what it precluded under federal law.

Thus, while Congress used Section 10(b) as the model for SLUSA's scope, it made a significant change. Section 10(b) broadly applies to fraud in connection with "any" security, but SLUSA applies only to a "covered" security. The purpose of the change was to preserve state regulatory authority and, as the Fifth Circuit explained, Congress's concerns in enacting SLUSA "are unique to the world of national securities." Pet. App. 27a. Specifically addressing the subset of securities that are traded on national exchanges, Congress concluded that issuers "can not control where their securities are traded," with the consequence that "a single state can impose the risks and costs of its peculiar litigation system on all national issuers. The *solution to this problem* is to make Federal court the exclusive venue for most securities fraud class action litigation *involving nationally traded securities*." H.R. Rep. No. 105-803, at 15 (1998) (Conf. Rep.) (emphasis added). Petitioners cite and quote this Court's decision in *Dabit* and the Conference Report on SLUSA dozens of times, but always skip the essential discussion of Congress's exclusive focus on nationally traded securities.

Congress specifically took the phrase and definition of "covered security" from the National Securities Markets Improvement Act, Pub. L. No. 104-290, 110 Stat. 3416 (1996), in which their function is to allocate regulatory authority between federal and state law. *See* H.R. Rep. No. 105-803, at 13. That statute, enacted the year after the PSLRA, amended the securities laws to provide that the federal government would regulate "covered securities" without disturbing the states' regulation of other securities. The purpose of the distinction was to "eliminate the costs and burdens of duplicative and unnecessary regulation" of covered securities. H.R. Rep. No. 104-622, at 16 (1996). But critically, it was not Congress's intention "to alter, limit, expand, or otherwise affect in any way any State statutory or common law with respect to fraud or deceit . . . in connection with securities or securities transactions." *Id.* at 34.

Under this allocation of responsibility, "State governments generally retain[ed] authority to regulate small, regional, or intrastate securities offerings, and to bring actions pursuant to State laws and regulations prohibiting fraud and deceit, including broker-dealer sales practices abuses." *Id*. *See also* H.R. Rep. No. 104-864, at 40 (1996) (Conf. Rep.) ("Smaller, regional, and intrastate securities offerings remain subject to state regulation. The Managers have preserved the authority of the states to protect investors through application of state antifraud laws."). And in enacting SLUSA, Congress determined to "preserv[e] the appropriate enforcement powers of State securities regulators and not chang[e] the current treatment of individual lawsuits." Pub. L. No. 105-353, § 2.

Petitioners' interpretation of SLUSA would override Congress's judgment not to interfere with state remedies for frauds relating to non-covered assets. A ruling in petitioners' favor would preclude important remedies and leave consumers largely unprotected from frauds that Congress determined not to address in the federal securities laws. As discussed, petitioners' theory extends SLUSA to numerous misstatements that have never before been recognized as a basis for a claim of securities fraud under Rule 10b-5. On the other hand, fraud and aiding-and-abetting claims similar to those set forth in respondents' complaints have long been recognized and adjudicated under state law. *See, e.g.*, *Kinzbach Tool Co. v. Corbett-Wallace Corp.*, 160 S.W.2d 509, 514 (Tex. 1942) (Texas common law cause of action for participation in another's breach of fiduciary duty); *Flowers v. Dempsey-Tegeler & Co.*, 472 S.W.2d 112, 114 (Tex. 1971) (statutory liability under Texas Securities Act); *Waterman v. Alta Verde Indus., Inc.*, 643 F. Supp. 797, 808 (E.D.N.C. 1986) (state-law liability for aiding and abetting the sale of unregistered securities); *Adamson v. Lang*, 389 P.2d 39, 42 (Or. 1964) (state-law liability for aiding and abetting fraud against shareholders).

This case thus stands in stark contrast to *Dabit*, in which this Court held that SLUSA reached claims brought by "holders" of securities in part because those claims were traditionally regulated by federal, not state, law. 547 U.S. at 88. Here, the opposite is true: these suits are traditional, long-recognized state-law actions.

To be sure, petitioners' theory would not foreclose every remedy for every plaintiff. Indeed, it would enable a broader array of claims under Rule 10b-5 and therefore increase the amount of litigation in the federal courts. But federal securities law claims are subject to a variety of restrictions under the PSLRA. And the SEC manifestly does not have the resources to bring enough actions to substitute for the deterrent effect of the prospect of state-law class actions.

Further, the consequences for the states' rights and the remedies of victims would be significant. State law, unlike Rule 10b-5, generally recognizes secondary liability. *See, e.g.*, 12A JOSEPH C. LONG, BLUE SKY LAW § 12:6 (chart explaining that some form of secondary liability "appears to be available in all states"). The ruling petitioners seek would override the judgment of sovereign states – in the exercise of their historic police powers – that holding parties like petitioners liable is important to deterring fraud and protecting consumers. It would effectively eliminate the state-law remedy by barring a procedural mechanism – group and class actions – that reflect the states' judgment that collective actions are an important procedural tool. The only parties who could afford to proceed individually are massive institutional investors; the retirees and small business owners who stand to lose everything and who most need protection from fraud would lose out.

So petitioners cry crocodile tears in asserting that their interpretation of SLUSA is necessary to target complicated and sophisticated frauds. *E.g.*, Proskauer Br. 23-24. Their goal is immunity for the secondary actors often involved in those frauds. Under the Fifth

Circuit's decision, if fraud actually occurs in connection with transactions in covered securities, the statute obviously applies. If it involves the purchase or sale of any form of "security" – whether covered or not – the SEC has jurisdiction to bring an action under Rule 10b-5. The only upshot of petitioners' sweeping position is to eliminate significant and longstanding remedies provided by the states in cases traditionally not subject to the federal securities laws.

These cases are a perfect example. Many of the plaintiffs lost everything, and individually they do not have anything approaching the massive resources required to litigate a Rule 10b-5 action against sophisticated defendants whose legal fees are often insured. Petitioners are alleged to have participated in and aided SIB's fraudulent sales of the non-covered CDs, yet because most are secondary actors, if they were to prevail here they would largely avoid their duty to compensate the victims. Petitioners would not be held responsible, notwithstanding the fraudulent representation that the non-covered CDs were a safe investment because SIB was heavily regulated. The petitioner insurance brokers would evade liability under state law for their representations that the CDs were insured. The law firm petitioners also would likely evade liability by forcing each plaintiff to litigate his or her claim individually.

For related reasons, petitioners and some *amici* err in contending that this Court must adopt their position to effectuate the principle that the federal securities laws do not impose secondary liability in private suits under Rule 10b-5. A ruling in petitioners' favor would extinguish group remedies under state law in

numerous cases that are not subject to the Rule, overriding the states' sovereign prerogative to recognize secondary liability under their police powers. It is settled that "[s]tate law claims may at times provide for broader liability than federal law provides, such as aiding and abetting liability in cases of fraud." SECURITIES & EXCHANGE COMMISSION, STUDY ON INVESTMENT ADVISERS AND BROKER-DEALERS 46 (Jan. 2011), http://sec.gov/news/studies/2011/913studyfinal.pdf (citing Cal. Corp. Code § 25403(b) (extending liability to any "person that knowingly provides substantial assistance to another person in violation of any provision of this division or any rule or order thereunder.")). In turn, this Court found it appropriate not to recognize secondary liability under the securities laws in part because this area is "already governed by functioning and effective state-law guarantees," while recognizing that the federal securities laws "do[] not reach all commercial transactions that are fraudulent and affect the price of a security in some attenuated way." *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 161-62 (2008).

Further, a decision of this Court adopting petitioners' sweeping interpretation of "in connection with" would expand rather than contract the scope of liability under Rule 10b-5. More cases, not fewer, would be filed as federal securities fraud claims. But this Court limited secondary liability to reduce the "risk that the federal power would be used to invite litigation beyond the immediate sphere of securities

litigation and in areas already governed by functioning and effective state-law guarantees." *Id.*[*]

3. Finally, petitioners' interpretation would undermine Congress's determination that SLUSA would be easily administered at the outset of the case, permitting the trial court to determine promptly whether it was subject to removal and dismissal. A ruling in petitioners' favor would be unadministrable. In a misguided attempt to eliminate this one case, petitioners would have this Court lay a field of land mines that the state and federal courts would inevitably trigger for decades to come. Petitioners offer no legal standard at all, other than the implausibly "broad" rule that the securities laws apply to every statement "about" securities transactions. Petitioners variously suggest that it is relevant that they believe that SIB's statements about covered securities were "central" or "critical" to the fraud and that the complaints state that the fraud was "material" to the purchase of the non-covered CDs. *E.g.*, Chadbourne Br. 41, Proskauer Br. 35, Willis Br. 34-35. But they also

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[*] Petitioners' claim that "[r]espondents' counsel has boasted that he intentionally pled only state-law claims in order to 'get around' the PSLRA and federal-law limitations on suing defendants only remotely connected to the primary wrongdoer," Willis Br. 4, is an extraordinary and irresponsible misrepresentation because it falsely impugns another member of the bar as personally attempting to evade federal law. That statement was *not* made by – and was *not* attributed to – respondents' counsel: it was exclusively an (erroneous) characterization by the author of the daily online entry that petitioners cite. *See* Julie Triedman, ***Fifth Circuit Green-Lights $7 Billion Claims Against Proskauer, Other Stanford Advisers***, AmLaw Daily (Mar. 20, 2012).

disavow those factors as "irrelevant." *E.g.*, Chadbourne Br. 18; Proskauer Br. 30; Willis Br. 35.

Imagine how lower courts would apply a ruling in petitioners' favor. One need only observe that both the district court and the government support dismissal of these complaints only through a series of inferences and assumptions. *See supra* at 8, 21. Among other things, it is not at all clear to what extent SIB's misrepresentations involved "covered securities," as SIB only referenced "liquid assets." In a later case, would SLUSA apply to a fraud involving a portfolio of assets including seventy-five-percent covered securities? Twenty-five percent? One percent? Similarly, if petitioners prevail, how should the lower courts address the many cases in which a party is alleged to have falsely represented that it has a "growing" asset base? Is that sufficiently close to infer representations about covered securities that trigger SLUSA? As the Fifth Circuit explained, "every bank and almost every company owns some covered securities in its portfolio, and every debt instrument issued by these banks and companies is backed by this portfolio in the same way the CDs were ultimately backed by the assets in SIB's portfolio." Pet. App. 29a.

None of that massive potential expansion of the securities laws and resulting indeterminacy would serve any useful purpose. As discussed, the government and petitioners have failed to identify any other case like this one. This case is easily resolved through a rule that the lower courts can apply without opening the door to innumerable claims under federal law: SLUSA is not triggered merely by a defendant's false representation that it owned or intended to

purchase covered securities in which no other person would have an interest.

C. Petitioners' Argument Cannot Be Reconciled With Several Provisions Of SLUSA.

Several textual features of SLUSA make it very unlikely that Congress intended to preclude state-law group actions merely because the defendant stated that it intended to purchase covered securities. Begin with Congress's decision to limit the statute to a "covered" security rather than "any" security (as under Section 10(b) and Rule 10b-5). If Congress wanted expansively to preclude state-law suits like this one that involve fraud in the sale of non-covered assets, it would not have gone to the trouble of excluding those assets.

If petitioners are right, it also makes no sense that Congress limited SLUSA to the "purchase or sale" of a covered security. If Congress actually targeted suits alleging frauds that have no effect on the *market* for covered securities, it would not have required that the misrepresentation be made in connection with transactions in those securities. It would have written the statute more broadly to apply to any misstatement "relating to" or "about" covered securities.

Petitioners' interpretation also makes a hash of the fact that SLUSA applies when there is "a" single allegation of a covered misrepresentation. Petitioners' theory is that the statute reaches frauds with *no* adverse effect *at all* on the market for covered securities. If that were so, why would Congress even require the nominal hook of "a" misstatement "about"

covered securities? SLUSA makes sense only when read more narrowly to apply to frauds that adversely affect the market for covered securities. In those cases, in which the fraud itself directly implicates the federal interest, it makes perfect sense to say that "a" material misstatement in connection with a securities transaction triggers SLUSA.

Petitioners also make nonsense of SLUSA's reference to complaints "alleging" that single misrepresentation. The text makes sense if limited to frauds that are material to trades in the federally regulated market for covered securities. In such cases, the statute achieves Congress's goal to preclude state-law suits that seek to evade the restrictions of the PSLRA because the plaintiffs *must* allege these misrepresentations in order to state a claim. If the plaintiffs omit or delete them, the complaint fails by its own terms. Thus, if private plaintiffs had brought suit on the facts of prior cases involving SLUSA or Section 10(b), but omitted the allegations of securities-related misrepresentations, there would have been no cases to pursue. *See, e.g.*, *Dabit*, 547 U.S. at 89 (fraudulent conduct occurred for the sole purpose of manipulating stock prices); *Zandford*, 535 U.S. at 822 (holding that victims were "injured as investors through respondent's deceptions, which deprived them of any compensation for the sale of their valuable securities"); *O'Hagan*, 521 U.S. at 647 (fraud was not consummated until attorney used misappropriated information to purchase securities); *Basic*, 485 U.S. at 228 (fraud constituted misleading statements that artificially depressed stock prices, causing harm).

By contrast, on petitioners' reading, SLUSA functions as a pleading game at best or a trap for the unwary at worst. Petitioners turn SLUSA into a form of postmodern literary criticism – certain words in the complaint trigger federal regulation, no matter what the substantive reality. If petitioners prevail, later plaintiffs in similar cases will avoid SLUSA preclusion merely by omitting any allegation of a misstatement relating to covered securities. This case is a perfect example. These complaints could proceed without that allegation because they allege fraud in connection with the purchase or sale of a *non*-covered asset. They further allege that the scheme included numerous misrepresentations that do not relate in any way to covered securities. The fact that the suits could go forward on the identical legal theory absent any allegation about covered securities also demonstrates that these complaints are not an example of the "vexatious" litigation that Congress targeted in SLUSA.

Congress could not have intended SLUSA to function that way. But not because there is a rule against writing a narrow complaint or amending a somewhat broader one: the statute specifically looks to the allegations of the plaintiffs, who are masters of their complaint. Congress enacted SLUSA to target a class of suits, not to change how complaints are worded. But the only effect of petitioners' reading is to extend SLUSA to a class of cases in which the allegations that trigger the statute's preclusive effect may simply be omitted in the first instance or later deleted. That makes no sense.

D. There Is No Basis To Defer To The SEC's Newfound Interpretation Of The Securities Laws.

Petitioners ask this Court to defer to the SEC's argument – set forth in its *amicus* brief – that the securities laws apply to any misstatement "about" securities transactions. *See* U.S. Br. 23. That theory is unquestionably sweeping. For all petitioners' rhetoric that SIB's portfolio supposedly "backed" the CDs (*e.g.*, Willis Br. 20; Proskauer Br. 37) and that SIB's misrepresentations were "central" to the fraud (*e.g.*, Chadbourne Br. 41), neither of those points has any relevance under the SEC's theory.

The SEC's position lacks merit. It obviously conflicts with this Court's precedent, which holds that a misstatement is "in connection with" the purchase or sale of a security only if it "coincides" with that transaction. *See supra* at 23-24. The Court has never held – or even suggested – that a statement merely "about" securities transactions suffices.

Very frequently, a statement "about" a transaction will not "coincide" with it. Take the statements "we bought this house" and "I will buy a boat." Both are "about" the purchase. But whether such a statement "coincides" with the transaction depends entirely on context. The promise "I will buy a boat from you" may well coincide with the transaction. If false, that particular statement would likely be a material misrepresentation in connection with the supposed purchase.

On the other hand, the statement may address a transaction that is, for example, either long over ("we bought this house in 1984") or contemplated in the future ("I will buy a boat from someone once we finally get a beach house"). Or the transaction may be close in time but only tangentially related to the transaction, as in: "Our daughter was born last month, the day after we bought this house." So too for the representation "SIB previously bought a pool of liquid assets." Each statement is "about" a "purchase or sale," but none "coincides" with the transaction at issue.

No deference is warranted to the SEC's contrary view. Congress enacted Section 10(b) almost eighty years ago. The SEC has had enforcement authority ever since. The government undoubtedly has brought thousands of enforcement actions in administrative proceedings and district courts that could have been resolved by the sweeping rule it now proposes. The government's brief canvasses the agency's prior enforcement history, U.S. Br. 21, yet it fails to identify a single case in which it took the position that every statement "about" securities purchases is *ipso facto* "in connection with" those purchases. Instead, the government's brief announces an entirely new and substantially different interpretation of those statutes, without any explanation for the agency's change in position. *See Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 742 (1996) ("Sudden and unexplained change, or change that does not take account of legitimate reliance on prior interpretation, may be 'arbitrary, capricious [or] an abuse of discretion,'" and unworthy of deference) (internal citations omitted).

The SEC also fails to acknowledge that its own complaint arising from this fraud asserted jurisdiction under Section 10(b) and Rule 10b-5 based only on the CDs' status as "securities." The agency's complaint does not even mention SIB's representations that it owned or would purchase liquid assets as a basis for jurisdiction under the securities laws, as opposed to merely aspects of the fraud. *See supra* at 4.

In *Zandford*, this Court found it significant that the Court's interpretation of the phrase "in connection with" corresponded to the SEC's longstanding position. *See* 535 U.S. at 819. This case presents the opposite scenario, in which the agency's established understanding of the statute affirmatively undermines its position. The SEC has a long-settled interpretation of the securities laws, which it now jettisons without explanation. This Court appropriately has been deeply dubious of such late-breaking, unexplained claims of agency authority. *E.g.*, *Christopher v. SmithKline Beecham Corp.*, 132 S. Ct. 2156, 2168-69 (2012) (denying full deference to agency opinion announced for first time in an *amicus* brief).

Moreover, the reason for the agency's significant change in position appears to be simple aggrandizement. The government wants this Court to impose the broadest conceivable interpretation of "in connection with" to expand substantially its own civil and criminal enforcement authority. To the extent the Court reads that language broadly, the government may bring more civil suits under Rule 10b-5 and felony prosecutions under Section 10(b). The government acknowledges that its interest in this case is that "the relevant language in SLUSA was borrowed from, and

should be interpreted consistently with, similar language in Section 10(b)." U.S. Br. 2. "Accordingly, the decision in this case will have significant implications for the administration and enforcement of the federal securities laws by the Department of Justice and the Securities and Exchange Commission." U.S. Divided Arg. Motion 3. In an era of aggressive and expanding agency action, a ruling for petitioners would create the constant prospect that individuals and businesses would face securities fraud claims and prosecutions initiated by the federal government. *Cf. City of Arlington v. FCC*, 133 S. Ct. 1863, 1877-78 (2013) (Roberts, C.J., dissenting); *O'Hagan*, 521 U.S. at 691-92 (Thomas, J., concurring and dissenting).

Put another way, this case is the proverbial one-night stand between the government and these defendants. Imagine that the Question Presented in this case instead arose in a Rule 10b-5 suit by the SEC or a felony securities fraud prosecution by the Department of Justice over similar misrepresentations by the defendant about "covered securities" in the course of obtaining a non-securitized loan. The avowed purpose of the government's brief is to establish its authority to bring such a case. But the defendant would take the position – obviously correct – that its conduct could not be federal securities fraud because it had nothing to do with the purchase or sale of a security.

If the SEC's *amicus* brief nonetheless would qualify for deference, it would be because the agency is interpreting the parallel language of its own Rule 10b-5 under this Court's decision in *Auer v. Robbins*, 519 U.S. 452 (1997). If so, then *Auer* should be overruled. As

Justice Scalia has explained, that decision inappropriately invites agencies to assume the role of both lawmaker and law enforcer. *See Talk Am., Inc. v. Mich. Bell Tel. Co.*, 131 S. Ct. 2254, 2266 (2011) (Scalia, J., concurring). This case is a perfect example. The SEC regularly invokes its power to initiate *and* adjudicate administrative enforcement actions. *See* U.S. Br. 1-2. By imposing a dramatically broader reading of the securities laws, the agency expands both its power to accuse firms and individuals of securities fraud and its authority to find them guilty of it.

V. Petitioners Are Not Entitled To Dismissal Of The Complaints In Their Entirety In Any Event.

Petitioners assume that if the allegations they identify do trigger SLUSA, then respondents' complaints must be dismissed in their entirety. That issue is not encompassed by the Question Presented. If the judgment below is not affirmed, the plaintiffs' right to proceed further should be addressed by the court of appeals on remand. The better view is that SLUSA requires the dismissal of only those claims that depend on the prohibited allegations, and the plaintiffs may amend their complaints to delete non-essential allegations. *See Proctor v. Vishay Intertechnology Inc.*, 584 F.3d 1208, 1226-27 (9th Cir. 2009); *In re Lord Abbett Mut. Funds Fee Litig.*, 553 F.3d 248, 255-57 (3d Cir. 2009); *Dabit v. Merrill Lynch, Pierce, Fenner & Smith, Inc.,* 395 F.3d 25, 47 (2d Cir.2005), *rev'd on other grounds,* 547 U.S. 71 (2006). The court of appeals also may determine in the first instance whether the claims of the *Roland* plaintiffs may proceed in state court because once the Fifth Circuit entered its remand

order, 28 U.S.C. § 1447(d) deprived the federal courts of further appellate jurisdiction. *See Kircher v. Putnam Funds Trust*, 547 U.S. 633, 648 (2006); *Roland* Br. in Opp. 7-9.

CONCLUSION

The judgment of the Fifth Circuit should be affirmed.

Respectfully submitted,

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