No. 13-791

IN THE

Supreme Court of the United States

JOHN J. MOORES, *et al.*,

Petitioners,

v.

DAVID HILDES, INDIVIDUALLY AND AS TRUSTEE OF THE DAVID AND KATHLEEN HILDES 1999 CHARITABLE REMAINDER UNITRUST DATED JUNE 25, 1999,

Respondent.

On Petition For Writ Of Certiorari
To The United States Court Of Appeals
For The Ninth Circuit

BRIEF IN OPPOSITION

MICHAEL A. LYNN
KYLE D. GOOCH
KAYE SCHOLER LLP
425 Park Avenue
New York, NY 10022
(212) 836-8000

ROBERT BARNES
KAYE SCHOLER LLP
1999 Avenue of the Stars,
Suite 1600
Los Angeles, CA 90067
(310) 788-1000

STEVEN S. ROSENTHAL
Counsel of Record
KAYE SCHOLER LLP
901 Fifteenth Street, NW
Washington, DC 20005
(202) 682-3500
steven.rosenthal@
kayescholer.com

Counsel for Respondent

QUESTION PRESENTED

Whether an investor who received stock pursuant to a false and misleading registration statement as part of a stock-for-stock merger transaction loses the civil liability remedy of Section 11 of the Securities Act of 1933, where he agreed to vote in favor of the proposed merger before the defective registration statement was filed.

RULE 29.6 STATEMENT

The David and Kathleen Hildes 1999 Charitable Remainder Unitrust Dated June 25, 1999 is not a corporate entity.

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BRIEF IN OPPOSITION

This case is not appropriate for this Court's review. The petition is based on a purported conflict between the Ninth Circuit's decision in this case and the Eleventh Circuit's decision in *APA Excelsior*.[1] No such conflict exists. The Ninth Circuit expressly stated that it was "not presented with the issue decided in *APA Excelsior*." Pet. App. 15a.

In June 2000, respondent David Hildes became a shareholder of Peregrine Systems, Inc. when his shares in another company, Harbinger Corporation, were exchanged for Peregrine shares in a stock-for-stock merger between the two companies. Unknown then to Hildes, the registration statement under which his Peregrine shares were issued was materially false and misleading. Hildes seeks to recover against petitioners, each of whom signed the defective registration statement, under Section 11 of the Securities Act of 1933.

Petitioners urged the courts below to reject Hildes's claim because, before the defective registration statement was issued, Hildes entered into a voting agreement that allowed Peregrine to vote Hildes's Harbinger stock in favor of the proposed merger. Petitioners assert that, contrary to the pleaded facts, Hildes could not possibly have relied on any misstatements or omissions in the registration statement because he had supposedly irrevocably commit-

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[1] *APA Excelsior III, L.P. v. Premiere Techs., Inc.*, 476 F.3d 1261 (11th Cir. 2007).

ted to exchanging his Harbinger stock for Peregrine stock.

But the facts alleged in Hildes's proposed amended complaint tell a different story. When Hildes signed the voting agreement, the proposed merger was subject to numerous conditions. Among them, Peregrine was required to file a truthful registration statement. Had Peregrine done so, Hildes and the Harbinger board would have discovered that the financial statements previously provided to them were materially incorrect. The planned merger would not have gone through and Hildes never would have received Peregrine stock. According to the Ninth Circuit, these facts demonstrate that the registration statement "played a role in the causal chain that resulted in the exchange of [Hildes's] stock." Pet. App. 15a. The Ninth Circuit's narrow, fact-based holding does not engage—much less conflict with—the Eleventh Circuit's decision in *APA Excelsior*, and expressly says so.

Petitioners also fail to disclose that the Eleventh Circuit expressly declined to consider whether the investors in that case were irrevocably committed; the court deemed the argument to be waived because the investors failed to raise it in their briefs. Here, in contrast, the Ninth Circuit affirmatively found that Hildes had pleaded facts showing he was *not* irrevocably committed, and that, for several reasons, could and would have avoided the exchange of shares had he known of the defective registration statement.

Thus, *APA Excelsior* and this case are factually at odds, and there is, as the Ninth Circuit stated, no conflict between them.

Nor is there any conflict with the other lower court decisions petitioners cite. None of these cases even mentioned the narrow question resolved by the court of appeals here—whether an agreement to vote in favor of a stock-for-stock merger is always an irrevocable commitment to ultimately exchange stock pursuant to the merger, regardless of the investor's ability to rescind or abort the exchange.

Finally, the petition does not raise an important issue of federal law. Nothing about the decision impairs the operation of the federal regulation cited by petitioners, which requires that stock exchanged in connection with a corporate merger be registered under the Securities Act. By contrast, the result urged by petitioners *would* impair the operation of the Securities Act and its implementing regulations by depriving investors like Hildes from the protections and remedies of the Securities Act, contrary to the intent of Congress.

STATEMENT OF THE CASE

A. Statutory Background

To ensure compliance with the disclosure requirements of the Securities Act, Section 11 allows "*any* person" who acquired a security issued under a false or misleading registration statement to sue, among others, "every person who signed the registration statement." 15 U.S.C. § 77k(a) (emphasis added). Section 11 "places a relatively minimal burden on a plaintiff" in establishing a *prima facie* claim, requiring only that the plaintiff allege that he "purchased a security issued pursuant to a registration statement" containing a "material misstatement or omission." *Herman & MacLean v. Huddleston*, 459 U.S.

375, 382 (1983). A plaintiff need not allege nor prove causation, reliance or scienter. *See, e.g.*, *Hutchison v. Deutsche Bank Sec. Inc.*, 647 F.3d 479, 484 (2d Cir. 2011). A defendant may limit liability by proving that some or all of the alleged loss was caused by factors other than the misstatements or omissions (such as a general stock market decline). *See, e.g.*, 15 U.S.C. § 77k(e); *In re Worlds of Wonder Sec. Litig.*, 35 F.3d 1407, 1421–22 (9th Cir. 1994).

B. Facts

On April 5, 2000, Peregrine Systems, Inc. and Harbinger Corporation, both publicly traded software companies, entered into a merger agreement, subject to the approval of both companies' shareholders. Pet. App. 27a. On the effective date of the merger, all Harbinger stock would be exchanged for newly issued Peregrine stock to be registered with the Securities and Exchange Commission (SEC). *Id.* At the time, Hildes was a director and shareholder of Harbinger; petitioners were Peregrine directors. Pet. App. 3a–5a.

In the merger agreement, Peregrine represented and warranted that the to-be-filed registration statement would comply with all applicable securities laws and would not contain any material misstatements or omissions. *Id.* at 5a–6a. Harbinger's obligations to complete the merger were expressly subject to certain conditions. These conditions included (i) approval by a state-law-mandated supermajority of each company's shareholders; (ii) the SEC's acceptance of the to-be-filed registration statement; and (iii) performance by Peregrine of all covenants in the merger agreement including filing a truthful and

accurate registration statement. *Id.* at 5a. Harbinger had the power to terminate the merger agreement if any representation, warranty or covenant made by Peregrine was breached or became untrue. *Id.*

As a condition of the merger agreement, Peregrine required that certain Harbinger shareholders, including Hildes, execute voting agreements and proxies allowing Peregrine to vote their shares in favor of the merger. *Id.* at 6a. Hildes's voting agreement and proxy were both tied to the overall merger agreement: they terminated automatically if the merger agreement fell through. *Id.* While the proxy was irrevocable "to the fullest extent permissible by law" (*id.* at 6a), it could have been rescinded if it were discovered that the voting agreement had been induced by fraud. *Id.* at 13a; *see* Restatement (Second) of Contracts § 164.

The merger would not have occurred had the registration statement been truthful. Pet. App. 12a. The Harbinger board would have terminated the merger agreement for breach because the registration statement would have revealed previous misrepresentations made by Peregrine. *Id.* Even if the vote went forward, Harbinger shareholders—85% of whom were not bound by proxies—would have defeated the merger proposal. *Id.* at 12a–13a. Moreover, as the Ninth Circuit held, Hildes "could have personally avoided the exchange of [his] shares" by (i) selling his Harbinger stock to a third party; (ii) rescinding the voting agreement and proxy for fraudulent inducement; or (iii) filing a shareholder suit to enjoin the merger. *Id.* at 13a.

On May 22, 2000, Peregrine filed its registration statement with the SEC. *Id.* at 6a. Petitioners signed and approved the registration statement. *Id.* The financial statements in the registration statement overstated Peregrine's revenues by over $120 million (nearly half of its reported revenue) and understated Peregrine's net losses by over $190 million (seven-and-a-half times its reported loss). *Id.*

On June 16, 2000, Harbinger's shareholders approved the merger. *Id.* Peregrine issued 30 million new shares of common stock under the defective registration statement. *Id.* All outstanding shares of Harbinger stock, including Hildes's shares, were exchanged for Peregrine stock. *Id.*

Two years later, Peregrine disclosed financial irregularities that required the reversal of more than $500 million in previously reported revenues—nearly 40% of the total reported revenue over the prior three years. As a result of these disclosures, the SEC brought an enforcement action against Peregrine, more than a dozen Peregrine insiders were indicted, Peregrine sought bankruptcy protection, and the board of directors was replaced. Peregrine's stock price plummeted. Hildes lost almost the entire value of his investment—more than twenty-five million dollars.[2]

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[2] *See generally* Proposed Second Am. Compl., ECF No. 12-6, *Hildes v. Arthur Andersen LLP*, No. 3:08-cv-0008-BEN-RBB (S.D. Cal.).

C. Proceedings Below

Hildes was originally an unnamed member of a putative class action brought by Peregrine shareholders in the Southern District of California.[3] Pet. App. 7a. After the class plaintiffs entered into settlements with certain defendants, Hildes filed an individual suit in the District of New Jersey against, among others, Peregrine's former auditor, Arthur Andersen LLP. *Id.* The action was transferred to the Southern District of California for coordinated pretrial proceedings with the class action. *Id.*

In 2009, after opting out of additional class settlements, Hildes moved for leave to amend his complaint to add a Section 11 claim against petitioners. *Id.* at 7a–8a. Petitioners intervened to oppose Hildes's motion. *Id.* at 30a–32a.

The district court denied Hildes's motion, holding that his Section 11 claim was futile. *Id.* at 20a–30a, 32a–34a. The district court applied the "commitment theory," a judicially created legal fiction by which a security is considered to be purchased as of the date the purchaser was irrevocably committed to the transaction.[4] The district court concluded that Hildes

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[3] *In re Peregrine Sys., Inc. Sec. Litig.*, No. 3:02-cv-870-BEN-RBB (S.D. Cal. filed May 6, 2002).

[4] *See, e.g.*, *Westinghouse Elec. Corp. v. '21' Int'l Holdings, Inc.*, 821 F. Supp. 212, 215–16 (S.D.N.Y. 1993). The commitment theory was first applied in insider trading cases to prevent otherwise inequitable results. *See, e.g.*, *Radiation Dynamics, Inc. v. Goldmuntz*, 464 F.2d 876, 891 (2d Cir. 1972); *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 853 n.17 (2d Cir. 1968).

was irrevocably committed to exchange his Harbinger shares for Peregrine shares by virtue of the voting agreement and proxy; thus, according to the district court, Hildes had effectively "purchase[d]" his Peregrine shares before the registration statement was filed. Pet. App. 28a. As a result, the district court concluded, Hildes's claims were barred by a "negative causation" defense. *Id.*

A unanimous panel of the United States Court of Appeals for the Ninth Circuit (Ninth Circuit Judges Fletcher and Trott and Tenth Circuit Judge Lucero, sitting by designation) reversed the district court's judgment. *Id.* at 1a–19a. The court held that, at the time he entered into the voting agreement and proxy, Hildes was *not* irrevocably committed to exchanging his Harbinger shares for Peregrine shares because Hildes had "plausibly allege[d]" that "the merger would not have occurred" if the registration statement had been accurate. *Id.* at 12a. The court found that Hildes had adequately alleged "several theories under which the planned merger would have collapsed" if the registration statement had been accurate: the Harbinger board would have terminated the merger due to Peregrine's breach of warranties, the shareholder votes would have failed, and Hildes would have sued to enjoin the merger or to rescind his voting agreement. *Id.* at 12a–13a.[5]

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[5] In light of its holding on the irrevocable commitment issue, the Ninth Circuit did not reach two other arguments raised by Hildes, each of which provided an independent basis to reverse the district court's judgment. First, Hildes argued that the commitment theory did not apply in the context of a conditional

(continued...)

The court of appeals denied petitioners' motion for rehearing by the panel or rehearing *en banc*, with none of the active judges in the Ninth Circuit voting for rehearing *en banc*. Pet. App. 41a–42a.

REASONS FOR DENYING THE PETITION

I. There Is No Circuit Split

There is no conflict between the Ninth Circuit's decision below and the Eleventh Circuit's decision in *APA Excelsior*, which is distinguishable on both factual and legal grounds.

The plaintiffs in *APA Excelsior* were investors in a company being acquired in a stock-for-stock merger. 476 F.3d at 1263. The plaintiffs signed voting agreements and proxies allowing the acquiring company to vote their shares in favor of the merger. *Id.* at 1263–64. The Eleventh Circuit affirmed summary judgment in favor of defendants on the plaintiffs' Section 11 claims. Applying the commitment theory, the court held that the plaintiffs had effectively purchased their shares on the date that they entered into the voting agreements and proxies. *Id.* at 1267, 1269–70. The Eleventh Circuit held that "impossibility of reliance" was a defense to a Section 11 claim "where sophisticated investors participating in an arms-length corporate merger make a legally bind-

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merger. *See SEC v. Nat'l Student Mktg. Corp.*, 457 F. Supp. 682, 704–05 (D.D.C. 1978). Second, Hildes argued that impossibility of reliance is not a valid defense to a Section 11 claim. *See Fed. Hous. Fin. Agency v. Bank of Am. Corp.*, 2012 WL 6592251, at *2–3 (S.D.N.Y. Dec. 18, 2012); *Westinghouse Elec.*, 821 F. Supp. at 218.

ing investment commitment months before the filing of a defective registration statement." *Id.* at 1277.

The Eleventh Circuit's decision in *APA Excelsior* is different from, and not in conflict with, the Ninth Circuit's opinion here in at least three significant ways.

1. *APA Excelsior* never addressed the issue at the crux of Hildes's argument—that signing a voting agreement and proxy was not an irrevocable commitment to exchange stock. That argument was waived by the *APA Excelsior* plaintiffs, who failed to raise the issue in their briefs. *See id.* at 1266, 1269–70.

The waiver was a product of the case's unique procedural history. The *APA Excelsior* district court initially granted summary judgment for defendants on the basis that the plaintiffs lacked standing. *Id.* at 1266. In a prior appeal, the Eleventh Circuit reversed that ruling, but observed that the defendants failed to raise the "seemingly more attractive argument that, due to the time of their investment decision," the plaintiffs "could not possibly have relied on the registration statement."[6] On remand, taking this *dicta* as the "law of the case," the district court granted summary judgment for defendants on the ground that the timing of plaintiffs' commitment precluded any possible reliance on the registration statement. 476 F.3d at 1266. In the second appeal, the plaintiffs never challenged the factual issue regarding the timing of their commitment in either their opening

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[6] *APA Excelsior III, L.P. v. Premiere Techs., Inc.*, 2004 WL 6064402, at *5 (11th Cir. Sept. 23, 2004).

or reply briefs; instead, they "argued repeatedly throughout both briefs that the timing of their commitment was 'irrelevant' for Section 11 purposes and that impossibility of reliance is no bar to their claim." *Id.* at 1269. When, belatedly, the plaintiffs did raise the issue for the first time at oral argument, the Eleventh Circuit declined to consider it, deeming it waived:

> [I]t is not necessary for us to decide if the district court was correct in holding that the timing of Plaintiffs' investment commitment was law of the case. Rather, Plaintiffs waived the issue by not challenging that clear and express holding. . . . In summary, we accept the . . . conclusion . . . that Plaintiffs made a binding investment commitment prior to the registration statement.

Id. at 1269–70.

"Significantly," the Eleventh Circuit "declined to consider" the argument made by Hildes in this case. Pet. App. 14a. Thus, as Judge Lucero's unanimous opinion held, the Ninth Circuit was "not presented with the issue decided in *APA Excelsior*." *Id.* at 15a.

2. *APA Excelsior* was decided on different facts. There, the plaintiffs' voting agreement expressly provided that the acquiring company was under no obligation to file a registration statement with the SEC. 476 F.3d at 1264–65. The Eleventh Circuit emphasized this fact in reaching its conclusion that reliance was impossible. *See id.* at 1276 (finding that plaintiffs could not have "purchased pursuant to the

registration statement, particularly since . . . no registration statement was even required as to their shares"). By contrast, the Harbinger–Peregrine merger agreement not only required Peregrine to file a registration statement, but also expressly required that it be truthful in all respects. Pet. App. 5a. Thus, unlike in *APA Excelsior*, the Peregrine registration statement was a specifically negotiated safeguard in the merger.

3. The two cases were decided on different procedural postures. *APA Excelsior* was decided on summary judgment based on a fully developed record of undisputed facts. The Eleventh Circuit found, for example, that the plaintiffs there conducted only "superficial due diligence" before committing to a transaction with few safeguards. 476 F.3d at 1264–65. In stark contrast, Hildes's claim was dismissed at the pleadings stage. As the Ninth Circuit emphasized, the court was required to "accept as true all well-pleaded, non-conclusory allegations" in Hildes's proposed amended complaint. Pet. App. 4a n.1. The court of appeals concluded that Hildes "provide[d] several theories under which the planned merger would have collapsed but for the misrepresentations" in the registration statements, and that those misrepresentations "played a role in the causal chain that resulted in the exchange of [Hildes's] stock." *Id.* at 12a–15a. There was no such finding in *APA Excelsior*.

For at least these three reasons, and as set forth in the Ninth Circuit's opinion, there is no conflict between this case and *APA Excelsior*.

II. There Is Also No Conflict With Other District Court Section 11 Decisions

The court of appeals' decision is not in conflict with the handful of district court decisions cited by petitioners (Pet. 16–18).

1. Contrary to petitioners' argument, the Ninth Circuit's decision does not conflict with district court decisions involving Rule 144A exchanges. A Rule 144A exchange, also known as an *Exxon Capital* exchange, is a capital-raising technique in which a company makes a private offering of unregistered bonds to investors, who have the option to exchange them for later-issued registered bonds.[7] None of the three cases cited by petitioners considered whether an agreement to vote in favor of a conditional merger was an irrevocable commitment to exchange stock.[8] Moreover, the investors' losses had already been realized when they received their unregistered bonds before the registration statements were filed. The issue was not lack of reliance, but lack of causation. Here, where the registration statement was filed *before* Hildes received his Peregrine stock, the Ninth Circuit held that there was a causal nexus between the defective registration statement and Hildes's injury.

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[7] *See In re Levi Strauss & Co. Sec. Litig.*, 527 F. Supp. 2d 965, 975 n.11 (N.D. Cal. 2007); 17 C.F.R. § 230.144A.

[8] *See In re HealthSouth Corp. Sec. Litig.*, 261 F.R.D. 616 (N.D. Ala. 2009); *In re Refco, Inc. Sec. Litig.*, 503 F. Supp. 2d 611 (S.D.N.Y. 2007); *In re Levi Strauss & Co. Sec. Litig.*, 527 F. Supp. 2d 965 (N.D. Cal. 2007).

2. Also contrary to the petition, the decision below does not conflict with cases applying Section 11's so-called "tracing" requirement, under which a plaintiff who acquires stock on the open market must trace his shares back to a defective registration statement. *See Guenther v. Cooper Life Sciences, Inc.*, 759 F. Supp. 1437, 1438–40 (N.D. Cal. 1990) (plaintiffs who purchased their shares on the open market lacked statutory standing because they were unable to trace their shares back to the allegedly defective registration statement). Tracing Hildes's shares back to the defective registration statement is not an issue here because there is no dispute that Hildes's Peregrine shares were issued under the defective registration statement.

In sum, none of the district court decisions petitioners cite speaks to the issue the Ninth Circuit decided, which is whether Hildes adequately alleged that he was not irrevocably committed to the exchange of his shares.

III. Review Is Not Warranted At This Stage Of The Case

The Ninth Circuit's judgment is not final. The decision only addressed whether Hildes adequately pleaded a Section 11 claim. The case will continue though discovery to final adjudication on the merits. If petitioners prevail, there is no need for this Court to address the question presented in the petition. If Hildes prevails, however, there will be opportunity enough for the Court to address the issue following a final judgment on the merits.

IV. The Petition Does Not Present An Important Question Of Federal Law

Petitioners' claim of "confusion" (Pet. 19) about the interplay between the commitment theory and SEC rules does not warrant this Court's review.

Before 1972, shares exchanged in a stock-for-stock merger did not need to be registered under the Securities Act. The SEC changed this by adopting Rule 145 "to make available the protection provided by registration" to "persons who are offered securities" in mergers and other types of business transactions. 17 C.F.R. § 230.145, Preliminary Note. The rule was designed precisely to protect investors like Hildes by requiring entities like Peregrine to register shares issued in a stock-for-stock merger, and to do so based on a truthful registration statement. Rule 145 provides that the exchange of stock in a merger is deemed to involve an "offer," "offer to sell," "offer for sale" or "sale," thus triggering the Securities Act's registration requirements. *Id.* § 230.145(a)(2).

Nothing in Rule 145 purports to draw the lines between what constitutes an "offer" and what constitutes a "sale." That line is drawn by the judicially created commitment theory, which establishes the date of the sale by looking to the point at which, "in the classical contractual sense," the parties "obligated themselves" to carry out the sale. *Radiation Dynamics*, 464 F.2d at 891. The Ninth Circuit's narrow holding—that Hildes adequately alleged that he was not irrevocably committed to exchange his stock—does not impair the operation of Rule 145 or the Securities Act generally.

As this Court has recognized, the "basic purpose" of the Securities Act is "to provide greater protection to purchasers of registered securities." *Herman & MacLean*, 459 U.S. at 383. Petitioners ask this Court to interpret the Securities Act in a way that is fundamentally at odds with this purpose by depriving investors like Hildes of the protections afforded by the registration process, including the Section 11 civil remedy. Under petitioners' view of the law, an investor loses all rights under Section 11 by signing a voting agreement, even if the registration statement is a negotiated safeguard in the transaction, even if its filing is a key link in the causal chain leading to the investor's loss, and even if the investor plausibly alleges that the filing of a truthful registration statement would have resulted in the cancellation of the merger. To apply the commitment theory in such circumstances would contravene the "broad remedial purposes" of the Securities Act and SEC Rule 145. *Id.* at 386.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

STEVEN S. ROSENTHAL
Counsel of Record
KAYE SCHOLER LLP
901 Fifteenth Street, NW
Washington, DC 20005
(202) 682-3500
steven.rosenthal
@kayescholer.com

MICHAEL A. LYNN
KYLE D. GOOCH
KAYE SCHOLER LLP
425 Park Avenue
New York, NY 10022
(212) 836-8000

ROBERT BARNES
KAYE SCHOLER LLP
1999 Avenue of the Stars,
Suite 1600
Los Angeles, CA 90067
(310) 788-1000

Counsel for Respondent

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