No. 14-687

In the Supreme Court of the United States

STIEFEL LABORATORIES, INC., *et al.*,
Petitioners,

v.

TIMOTHY FINNERTY,
Respondent.

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

BRIEF IN OPPOSITION

Norman S. Segall
SEGALL GORDICH P.A.
801 Brickell Avenue
9th Floor
Miami, Florida 33131

Peter Prieto
Stephen F. Rosenthal
Counsel of Record
Matthew P. Weinshall
PODHURST ORSECK, P.A.
25 West Flagler Street
Suite 800
Miami, Florida 33130
(305) 358-2800
srosenthal@podhurst.com

Counsel for Respondent

Becker Gallagher · Cincinnati, OH · Washington, D.C. · 800.890.5001

A QUESTION PRESENTED

Whether a company that had been privately held for more than a century and had repeatedly represented that it "will continue to be privately held" owed a duty to a shareholder under § 10(b) of the Securities Exchange Act and SEC Rule 10b-5 to disclose its decision to sell the company prior to purchasing his shares back from him.

TABLE OF CONTENTS

APPENDIX

TABLE OF AUTHORITIES

CASES

STATUTES AND RULES

OTHER AUTHORITIES

INTRODUCTION

After a seven-day trial, a jury reasonably found that Petitioners, Charles Stiefel and Stiefel Laboratories, Inc. ("SLI" or "the company"), defrauded Respondent Timothy Finnerty, in violation of § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78(j)(b), and SEC Rule 10b-5, 17 C.F.R. § 240.10b-5 (collectively "§ 10(b)"). The fraud involved Petitioners' failure to disclose that they were actively pursuing the sale of the company, in conflict with their repeated assurances that the company would continue to be privately held, prior to having the company purchase shares of its own stock from Mr. Finnerty for $16,469 per share. Less than three months after SLI purchased Mr. Finnerty's shares, Petitioners announced a merger with GlaxoSmithKline ("GSK") in which remaining shareholders, including Charles Stiefel, received $69,705 per share, more than four times what SLI paid Mr. Finnerty per share.

The jury disbelieved Petitioners' protestations that they did not intend to deceive former employees like Mr. Finnerty out of the substantial profits SLI shareholders stood to earn from CEO Charles Stiefel's secret decision to sell the 162-year-old privately held and family-controlled company. The jury's condemnation of their intentional wrongdoing, the district court's denial of Petitioners' post-trial motions, and the Eleventh Circuit's decision all stand on firm legal ground.

The Petition asks this Court to disregard the jury's findings and decide that, as a matter of law, Petitioners were not obligated to inform Mr. Finnerty of the merger negotiations before purchasing his stock,

despite continuously representing to him that the company would remain privately held. It should be denied for multiple reasons. First, Petitioners failed to preserve the issue they ask the Court to review. Second, this case has unique facts that make it an unsuitable vehicle for considering Petitioners' question as a general matter. Third, a decision on the merits would have no practical effect, because an independent, alternative basis exists to affirm the jury's verdict. Fourth, no inter-circuit conflict exists. And finally, the decision below is manifestly correct.

STATEMENT OF THE CASE

Until the 2009 merger that gave rise to this litigation, SLI, a pharmaceutical company specializing in dermatological products, had been privately held and controlled by the Stiefel family since its founding in 1847. (App. 2a; R:459:83; R:506-1:52-53; R:552:86.)

Mr. Finnerty began working for SLI in 1986 as a sales representative. (App. 4a; R:552:8-9.) During his lengthy tenure at the company, Mr. Finnerty accumulated approximately 28 shares of SLI common stock in his Employee Stock Bonus Plan ("ESBP") account, which represented the bulk of his retirement savings. (App. 4a; R:552:27; PX:704.)

On August 29, 2008, SLI fired Mr. Finnerty, along with a slew of other employees, as part of a reduction in force. (App. 4a; R:552:18-22.) Under the ESBP, his termination was an event that permitted him—for the first time—to choose whether to take a distribution of his shares of SLI stock from the ESBP and sell ("put") them back to the company during a limited window of time. (App. 4a; R:550:11-13.) Mr. Finnerty was only 55

years old, and since the ESBP account "[wa]s my retirement," as he put it, he "did not want to take it." (App. 4a; R:552:30.) As a result, he initially declined to take a distribution of his shares. (App. 4a; R:552:29-30; PX:783.)

But after SLI sent him several letters over the next few months reminding him of his distribution and put rights and announcing major changes in the ESBP that concerned him (App. 4a; R:554:51-57; PX 105; PX 109), Mr. Finnerty signed and submitted a form on January 6, 2009 electing to take a distribution of his shares and exercising his put right. (App. 4a; R:552:34-35; PX:703.) On February 13, 2009, SLI acted on his request by purchasing his shares and transferring into his retirement account $92,961.24 in cash and a promissory note for $371,844.98. (App. 4a; PX:704.)

Mr. Finnerty had no inkling that, at the very same time he was deciding whether to take a distribution of his shares, Charles Stiefel had secretly decided to sell the company, a concept that had been, in Mr. Stiefel's words, completely "taboo" throughout his lifetime. (App. 5a; PX:114.) The Stiefels' pride in running a family-owned company for 162 years permeated the corporate ethos. (App. 10a; R:549:84, 88.) The company consistently hammered this message to its employees/shareholders. (*Id.*) A former SLI Board member and thirty-year SLI employee testified that the company routinely "emphasized" that it was "privately held"; it was "always the philosophy of the company" that it would remain so. (*Id.*) He "never thought the company would ever, ever be sold." (R:549:90.) Mr. Finnerty had a similar experience, testifying that management brought up the theme of SLI being

privately held "in virtually every meeting." (App. 10a; R:552:18.) Another SLI employee testified that the leadership team at SLI gave employees "a very clear understanding" that SLI "was a company that had been around for 160 years, privately owned by the Stiefels, and that there were no plans of selling the company or going public." (App. 10a; R:551:35.)

Petitioners put this fundamental corporate business plan in writing as well. In an August 2007 email announcing a $500 million private equity investment, Charles Stiefel comforted employees that the large capital infusion into the company would not change its basic plan. (App. 3a; DX:32.) He "emphasize[d] a few key messages that are important for all employees to understand," the first of which was that

> *Stiefel will continue to be a privately held company* operating under my direction as Chairman, Chief Executive Officer, and President. The Stiefel family will continue to hold a majority-share ownership in the company.

(App. 3a; DX:32 (emphasis added).) The press release SLI issued contemporaneously repeated that message almost verbatim. (App. 3a; PX:189.)

Mr. Finnerty relied on those representations when he elected to take a distribution of his shares and put them back to the company. (R:552:38-40.) By contrast, none of the executives whom the Stiefels made privy to the merger negotiations sold their stock when given the opportunity in January and February 2009. (R:550:70; R:551:112; R:553:31.)

In fact, several months *before* Mr. Finnerty made his decision to sell, Mr. Stiefel had secretly decided to

sell the company and took numerous steps to that end, including hiring investment bankers, estimating the potential purchase price, and entering into negotiations with a potential acquirer. (App. 5a-6a, 18a-19a.)

In an effort to downplay their interest in a merger and the likelihood of it occurring, Petitioners omit several relevant facts. (Pet. 4-5.) First, on the same day that Mr. Stiefel and his sons, also SLI directors, agreed to "start moving" on a sale of the company, they also agreed to offer certain high-ranking executives, including themselves, employment contracts for the first time in the company's history. (R:550:100; PX:117.) The contracts contained a "change-of-control" provision, guaranteeing the executive a generous pay-out if the company engaged in a transaction resulting in the Stiefels' loss of control of the Board. (PX:293:SLI-12-004186.)

Second, that same day, an investment banker advised Mr. Stiefel that "it was quite possible" an acquirer would pay between $2.7 billion to $4.7 billion for the company, and that a price per share of $60,000 would serve "as a floor." (App. 5a; PX:114; R:550:94; R:506-1:11; PX:115; R:550:98-99.) Third, on December 8, 2008, Mr. Stiefel and his sons formally met with their merger advisors, who presented a "timeline and work plan" predicting that a merger could be announced in March 2009, identified several "tier-one" acquirers, including Sanofi-Aventis and GSK, and reiterated their sale price prediction. (App. 5a; R:506-1:19-20; DX:300:BX-Stiefel-0015524-30, BX-Stiefel-0015537; PX:118; PX:119.)

Fourth, several investment bankers attended Mr. Stiefel's December 22, 2008 meeting with the CEO of

Sanofi-Aventis, one of whom observed that Sanofi's investment banker "had worked up a detailed valuation of SLI," which he viewed "as a sign that they were very serious." (R:550:103-105; PX:123.) Following the meeting, Mr. Stiefel reaffirmed to his sons that he was "excited to move forward" with potentially selling the company to Sanofi. (PX:123; R:550:105.) Approximately a week later, in late December 2008, Petitioners signed a formal engagement agreement with their merger advisors to assist them in negotiating a sale of the company. (App. 5a; R:550:106; DX:173:SLI-4-018970.)

In line with SLI's advisers' predictions, Sanofi-Aventis submitted a bid for SLI valuing it at $3.2 billion, and GSK submitted a higher bid of $3.5 billion, on March 24, 2009. (App. 5a-6a; R:550:136-37.) On April 20, 2009, SLI reached an agreement with GSK to sell itself for approximately $3.6 billion. (App. 6a; R:550:136-37.) The agreement valued each share at $68,515.29, and provided that shareholders could receive an additional $7,186.91 per share if certain contingencies occurred. (App. 6a; PX:63:SLI-4-000530.)

It is undisputed that Petitioners never disclosed their intention to sell the company or any of these events to Mr. Finnerty before he sold his shares to the company in January 2009. Their reason for doing so was clear: by harvesting stock at $16,469/share in early 2009, when they knew as early as November 2008 that it would likely sell at a "floor" price of $60,000/share, they increased their ownership percentage in the company and thereby further enriched themselves. (R:550:67-68; R:551:103-04.) A "payout spreadsheet" Brent Stiefel prepared and sent

his father and brother before the merger demonstrated that Charles Stiefel would earn an additional $4.7 million through this scheme. (PX:199:SLI-4A-085997, SLI-4A-086009; R:550:121-24; R:555:48-51, 126-27.) Brent Stiefel indiscreetly observed that ESBP buy-backs made "the $ go up for all of us!" (PX:199.) The Stiefels even spent time devising a code name for their covert plan that would not betray a motive of "gold and greed." (PX:124.) The jury ultimately saw through that veneer.

After the seven-day trial, the jury returned a general verdict with interrogatories, finding that Petitioners knowingly violated Rule 10b-5, that Mr. Finnerty justifiably relied on Petitioners' conduct, and that Mr. Finnerty was damaged in the amount of $1,502,484.90. (R:515:2-3.) The jury additionally found that Charles Stiefel had the power to control the general affairs of SLI and the specific corporate policy that resulted in the Rule 10b-5 violation (*id.*), rendering him liable for SLI's conduct as a control person under § 20(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78t(a).

Petitioners appealed the denial of their renewed motion for judgment as a matter of law and motion for a new trial. The Securities and Exchange Commission, which is pursuing a related enforcement action against Petitioners,[1] filed an amicus brief in support of Respondent. Br. of the SEC as Amicus Curiae in Support of Plaintiff-Appellee, Urging Affirmance (11th Cir. filed June 5, 2013).

---

[1] *See SEC. v. Stiefel Labs. Inc., et al.*, No. 11-cv-24438 (S.D. Fla.).

In a unanimous opinion, the Eleventh Circuit affirmed. (App. 2a.) On the issue relevant to the Petition—Petitioners' duty to disclose their merger negotiations to Respondent—the court held that the disclosure duty arose from Petitioners' repeated "will continue to be privately held" statements and the unique factual context in which they were made. (App. 8a-13a.) Because those statements "were reinforced by the company's history and longstanding philosophy," and SLI employees "had heard generations of Stiefels express their commitment to keeping SLI under the family's control," such employees "could have reasonably understood" those statements "to be assurances that SLI remained unavailable for acquisition." (App. 11a.) As a result,

> [t]he jury could have found that nondisclosure of SLI's interest in a merger with Sanofi-Aventis misled the investors who were also SLI employees into believing that the company remained unavailable for acquisition, when in fact it was engaged in serious talks with a potential acquirer. In other words, the jury could have reasonably concluded that nondisclosure rendered SLI's "will continue to be privately held" statements misleading or deceptive to the investors who were also SLI employees, thus giving rise to a duty to update.

(App. 12a.)

The Eleventh Circuit took care to emphasize the narrow limits of it decision. (App. 14a.) It did not decide that Petitioners were obligated to disclose the details of its merger negotiations, or that they were even required to disclose any information to the public

at large. (*Id.*) Rather, it only held that Petitioners were obligated to inform Mr. Finnerty, prior to purchasing his shares, of just enough information to make their assurances that SLI "will continue to be privately held" not misleading. (*Id.*)

Petitioners moved for rehearing en banc, but that request was denied without a single active judge requesting a poll of the court. (App. 33a-34a.)

REASONS FOR DENYING THE WRIT

I. THIS CASE IS AN INAPPROPRIATE VEHICLE FOR REVIEW OF THE QUESTION PRESENTED.

A. Petitioners Have Waived The Issue They Ask The Court To Resolve.

Petitioners ask the Court to decide whether there is a duty under § 10(b) to update truthful prior statements, based on a purported conflict between the decision below and decisions primarily from the Seventh Circuit. Yet, before the Eleventh Circuit, Petitioners failed to question the existence of a duty to update, or cite any of the Seventh Circuit cases they now invoke. In fact, Petitioners expressly conceded the existence of the duty they now challenge. For this reason alone, the Petition should be denied. *See United States v. United Foods, Inc.*, 533 U.S. 405, 417 (2001) (refusing to consider arguments not pressed by petitioner below); *Delta Airlines v. August*, 450 U.S. 346, 362 (1981) (question presented in petition but "not raised in court of appeals . . . is not properly before us"); *United States v. Ortiz,* 422 U.S. 891, 898 (1975) (declining to consider an issue "which was raised for the first time in the petition for certiorari").

In their Eleventh Circuit appellate briefs, Petitioners conceded that, "[w]here a defendant's failure to speak would render the defendant's own prior speech misleading or deceptive, there may be a duty to disclose." *See* Br. for Defendants-Appellants, 16 (11th Cir. filed Feb. 14, 2013) (internal quotation marks and citations omitted). They conceded the point several more times at oral argument. (Resp. App. 4) ("So the controlling question comes down to did SLI's prior statements become misleading or deceptive between November 2008 and January 6, 2009, the date on which Finnerty exercised the put election."); (Resp. App. 8) ("The question is did anything that happened in November 2008 through January 6, 2009 have to be disclosed to keep this disclosure, the prior speech, from being false or misleading."); (Resp. App. 15) (conceding existence of duty to disclose arising out of prior statements); (Resp. App. 17) ("if they get a duty, which we admit we could have had if it made the prior statement false or misleading not to disclose …"); *see also* Resp. App. 34 (SEC counsel noting that "[t]he Defendants say that they did have such a duty to update and give more information ..."). Conceding this legal point, Petitioners instead argued that the merger negotiations did not render their prior statements misleading.[2]

---

[2] They relied largely upon the facts that they emphasize in their Petition (at 3-4, 7) – *i.e.*, that they disclosed in an August 2007 email that they might consider an initial public offering eight years later and would continue to evaluate all options when looking at the long-term financial needs of the company. Br. for Defendants-Appellants, 17-18 (11th Cir. filed Feb. 14, 2013); (Resp. App. 3, 5-8, 17).

Petitioners never distinguished between a duty to correct and a duty to update, as they do now, and never cited *any* of the Seventh Circuit decisions they now claim should control the case.[3] Nor can Petitioners claim that it necessarily would have been futile to raise such an argument below. To be sure, several prior Eleventh Circuit decisions had declared that a duty to disclose arises when a defendant's failure to speak would render the defendant's own prior speech misleading. *See, e.g., Badger v. S. Farm Bureau Life Ins. Co.*, 612 F.3d 1334, 1341 (11th Cir. 2010). But the only prior Eleventh Circuit decision holding that such a duty had been triggered involved a distinct fact pattern in which an accountant became aware that its client "was using its statements and reports to commit a significant fraud." *Rudolph v. Arthur Anderson & Co.*, 800 F.2d 1040, 1044 (11th Cir. 1986). Petitioners could have urged the Eleventh Circuit to distinguish *Rudolph* and follow the Seventh Circuit's decisions, particularly with respect to forward-looking statements, which *Rudolph* did not address. But they strategically chose not to.

Having already conceded the existence of a duty to disclose information necessary to prevent one's own

---

[3] Petitioners did cite *Hillson Partners Ltd. P'ship v. Adage, Inc.*, 42 F.3d 204 (4th Cir. 1994), in their reply brief to the Eleventh Circuit, but only in a section addressing Mr. Finnerty's alternative theory that Petitioner's announcement of the stock price gave rise to a disclosure duty. Reply Br. for Defendants-Appellants, 7 (11th Cir. filed July 15, 2013). Moreover, that case, as explained further on p. 24, *infra*, did not address the viability of a duty to update forward-looking statements, nor did it distinguish between a duty to correct and to update. Petitioners' reference to *Hillson* below in no way articulated the argument they now advance.

prior speech from becoming misleading, Petitioners should not now be permitted to challenge the existence of such a duty.

B. The Case Involves Unique Facts That Preclude Broad Review Of The Question Presented.

This is a unique, fact-bound case, with an extensive trial record. As a result, it does not lend itself to broad review of the viability and scope of a duty to update as a general matter.

SLI was privately held for more than a century; indeed, it was controlled by a single family. Because its shares were not publicly traded and were highly illiquid, the company disclosed very little to its shareholders, aside from its annual announcement of the share price and repeated assurances that the company would continue to be privately held. In contrast, all of the decisions Petitioners rely upon involved public corporations, which are required to periodically disseminate information to investors under SEC regulations. The existence of that regulatory disclosure regime for public corporations figures prominently in several decisions cited in the Petition. *See Higgenbotham v. Baxter Int'l Inc.*, 495 F.3d 753, 760-61 (7th Cir. 2007); *Gallagher v. Abbott Labs., Inc.*, 269 F.3d 806, 809-11 (7th Cir. 2001). Such regulatory considerations are insignificant here, since SLI was privately held. Moreover, the difference in the quantity of information regularly provided to shareholders—almost none for SLI compared to a regular stream for publicly-held companies—is a salient distinction that strengthens the case for imposing a limited duty to update on privately held corporations like SLI, whose

shareholders do not benefit from periodic disclosures or analyst coverage, and thus are more at risk for making investment decisions based on outdated information.

Another significant, unique fact is the direct-personal nature of the transaction in this case. Mr. Finnerty did not sell his shares through an impersonal, anonymous stock exchange; rather, he sold them directly to SLI, in response to several mailings from SLI prompting him to sell. None of the decisions cited in the Petition involved such a direct-personal transaction. A leading treatise on securities fraud has recognized the importance of this distinction:

> The duty to correct one's own prior statement would seem to be at its strongest in direct-personal transactions where the parties are dealing, and usually negotiating, with each other face to face. In this situation the probability of reliance on the prior statement is high, and correction is easy.

Alan R. Bromberg, Lewis D. Lowenfels, & Michael J. Sullivan, 2 BROMBERG & LOWENFELS ON SECURITIES FRAUD § 5:316 (2d ed.).[4]

The Seventh Circuit has recognized the significance of this distinction as well. *See Jordan v. Duff & Phelps, Inc.*, 815 F.2d 429, 431 (7th Cir. 1987); *Michaels v. Michaels*, 767 F.2d 1185, 1196 (7th Cir. 1985). A direct transaction between the firm and investor "allow[s] the investor to elicit the information he requires, while permitting the firm to extract promises of

---

[4] These commentators broadly define a "duty to correct" to include a duty to update. *Id.* § 5:290.

confidentiality that safeguard the [secretive merger] negotiations." *Jordan*, 815 F.2d at 431 (citations omitted).[5] The date of the transaction also "supplies a timing rule [for disclosure] on which the firm may rely." *Id.*

Because of the unusual context of this case, the Eleventh Circuit did not have to decide whether and when Petitioners had a "duty to update the public" about their merger negotiations. (App. 14a.) Rather, it only held that Petitioners "had a duty to update *Finnerty* at least before it repurchased shares of its own stock from him," *id.* (emphasis added), and even then, only needed to disclose the most skeletal facts necessary to make their prior assurances not misleading, such as that "a sale of the company was under consideration," *id.* This case, therefore, does not raise the much broader questions of whether and when a publicly traded company must disclose information to the entire market to make its prior statements not misleading.

Given the limited reach of the decision below—to direct-personal transactions between privately-held corporations and their investors, a factual scenario that rarely presents itself in published decisions—this Court's intervention is unwarranted.

---

[5] Petitioners have claimed that it would have been impractical to extract promises of confidentiality from Mr. Finnerty, who had moved on to work for a competitor of SLI by the time of the transaction. But the precise function of such an agreement would have prevented him from disclosing confidential information to his new employer. *See* App. 26a n.12. In addition, Petitioners also had the option of abstaining from purchasing Mr. Finnerty's shares. *See* App. 16a, 23a-24a.

C. Granting Certiorari Will Not Affect The Outcome, Because Alternative Grounds Require The Same Result.

The result in this case would stand regardless of whether or how this Court might resolve the Question Presented in the Petition. Even if, as Petitioners contend, § 10(b) did not support a duty to update prior truthful statements, Petitioners would still be liable for failing to disclose their merger negotiations to Mr. Finnerty, because a corporation must, as a matter of law, disclose all material information to those shareholders from whom it is purchasing its own stock, or abstain from trading with them.

As this Court established in *Chiarella v. United States*, 445 U.S. 222 (1980), a defendant's duty to disclose material information to a plaintiff arises under § 10(b) when "a relationship of trust and confidence" exists between them. *Id.* at 230. Such a relationship of trust and confidence exists between the shareholders of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation. *Id.* at 228. This particular relationship "gives rise to a duty to disclose because of the necessity of preventing a corporate insider from … tak[ing] unfair advantage of the uninformed minority stockholders." *Id.* (quotation marks omitted). As a result, under § 10(b), insiders who possess confidential, material information must either disclose the information or abstain from trading in the corporation's stock. *Id.* at 227 (citing *Cady, Roberts & Co.*, 40 S.E.C. 907 (1961)); *see also United States v. O'Hagan*, 521 U.S. 642, 652 (1997).

Every circuit court that has considered the issue, including both the Eleventh and Seventh Circuits, has concluded that the "disclose or abstain" rule also applies to corporations purchasing their own stock.[6] As one district court aptly put it, "the issuer attempting to repurchase its own shares is the insider par excellence." *Broder v. Dane*, 384 F. Supp. 1312, 1319 (S.D.N.Y. 1974) (quotation marks omitted). The rationale for imposing a disclosure duty on individual insiders—i.e., preventing them from taking unfair advantage of minority shareholders—applies with equal force to the corporation itself when purchasing its own stock from its shareholders. Accordingly, under § 10(b), SLI was required to disclose all material information to Mr. Finnerty before purchasing his shares, or to abstain from trading with him.[7]

---

[6] *See Castellano v. Young & Rubicam, Inc.*, 257 F.3d 171, 179 (2d Cir. 2001); *McCormick v. Fund Am. Cos., Inc.*, 26 F.3d 869, 876 (9th Cir. 1994); *Smith v. Duff & Phelps*, 891 F.2d 1567, 1574 (11th Cir. 1990); *Jordan v. Duff & Phelps, Inc.*, 815 F.2d 429, 431 (7th Cir. 1987); *Arber v. Essex Wire Corp.*, 490 F.2d 414, 418 (6th Cir. 1974); *Rogen v. Ilikon Corp.*, 361 F.2d 260, 268 (1st Cir. 1966); *see also* William K. S. Wang & Marc I. Steinberg, INSIDER TRADING § 5.2.3[C][1], at 310-11 (3d ed. 2010); 8 Louis Loss, Joel Seligman, & Troy Paredes, SECURITIES REGULATION 61 (4th ed. 2012).

[7] Petitioners countered below that this disclosure duty did not apply to them, because corporations do not owe shareholders fiduciary duties under Delaware law, and SLI was not a "closed corporation" under Delaware law. But the existence of a disclosure duty under § 10(b) is a matter of federal law, so whether Delaware law also recognizes such a duty is irrelevant. *See, e.g., Steginsky v. Xcelera Inc.*, 741 F.3d 365, 371 (2d Cir. 2014). For the same reason, it does not matter whether SLI met the definition of a closed corporation under state law. Those courts that have addressed this issue and described the defendant corporation as

Petitioners point out that the case was not tried on an insider-trading theory. (Pet. 9 n.1.) But it did not need to be for the verdict to be affirmed on this alternative, purely legal ground. See *Schweiker v. Hogan*, 457 U.S. 569, 585 & n. 24 (1982); *Lucas v. W.W. Grainger, Inc.*, 257 F.3d 1249, 1256 (11th Cir. 2001). Indeed, precisely because the disclosure duty exists as a matter of law, the issue would not have been left to the jury to decide in the first place; it simply would have been instructed that Petitioners owed Mr. Finnerty a duty to disclose all material information, a duty the jury necessarily found Petitioners to have violated. The issue was briefed on appeal, but the Eleventh Circuit did not reach it. *See* App. 15a n.5.

Because an alternative legal basis exists for affirming the jury's verdict, resolution of the Question Presented would be an abstract undertaking that would not affect the judgment. This case is, therefore, a poor candidate for certiorari.

II. THERE IS NO CIRCUIT SPLIT TO RESOLVE.

Petitioners' contention that this case implicates a conflict among the Circuits does not withstand scrutiny. Petitioners claim that decisions from the Seventh, Fourth, and Eighth Circuits have categorically rejected a § 10(b) duty to update prior truthful statements, in purported conflict with the decision below and decisions from the First, Second,

---

being "closed" appear to have intended the term to mean "privately held" (*Castellano*, 257 F.3d at 175), or "closely held" (*Jordan*, 815 F.2d at 431), which SLI indisputably was.

and Third Circuits. But the holdings from the Seventh, Fourth, and Eighth Circuits are far less sweeping than Petitioners suggest.

Those courts merely declined to recognize a duty to update truthful statements of historical fact and ordinary projections. They did not address the issue presented in this case: the existence of a much narrower duty to disclose material information necessary to prevent a particular kind of representation—forward-looking, continuing representations about the fundamental direction and intent of a company that remain "alive" in the minds of investors—from becoming misleading. In fact, the Seventh Circuit decision that Petitioners spotlight as creating the conflict expressly reserved judgment on this issue in a footnote that Petitioners simply ignore. As discussed below, the law in this area is harmonious, and no binding precedent in the Seventh, Fourth, or Eighth Circuits would have precluded those courts from holding, on these facts, that a disclosure duty exists.

1. Petitioners trace the § 10(b) duty to update "live" truthful statements to *Backman v. Polaroid Corp.*, 910 F.2d 10 (1st Cir. 1990), but its roots are actually much older. [8]

---

[8] *See, e.g., In re Phillips Petroleum Sec. Litig.*, 881 F.2d 1236, 1245 (3d Cir. 1989) ("There can be no doubt that a duty exists to correct prior statements, if the prior statements were true when made but misleading if left unrevised."); *Greenfield v. Heublein, Inc.*, 742 F.2d 751, 758 (3d Cir. 1984) ("[I]f a corporation voluntarily makes a public statement that is correct when issued, it has a duty to update that statement if it becomes materially misleading in light of subsequent events."); *Ross v. A.H. Robins Co., Inc.*, 465 F. Supp.

Then-Judge Alito authored an influential opinion for the Third Circuit on the existence and scope of the § 10(b) duty to update in *In re Burlington Coat Factory Securities Litigation*, 114 F.3d 1410 (3d Cir. 1997), on which the Eleventh Circuit relied in the case below. (App. 8a-9a.) In *Burlington*, the court surmised that the rationale underlying a duty to update truthful, forward-looking statements is that the statements "contained an implicit factual representation that remained 'alive' in the minds of investors as a continuing representation." *Id*. at 1432. The court then distinguished between "ordinary, run-of-the-mill forecasts," *id.* at 1433, and disclosures relating to "the announcement of a fundamental change in the course the company is likely to take," *id.* at 1434. Ordinary forecasts could not give rise to a duty to disclose subsequently discovered information, the court reasoned, because they "contain no more than the implicit representation that the forecasts were made reasonably and in good faith." *Id.* at 1433. But the latter type of forward-looking statements, such as statements concerning takeover attempts, could trigger such a disclosure duty, because "there may be room to read in an implicit representation by the company that

---

904, 908 (S.D.N.Y. 1979), *rev'd on other grounds*, 607 F.2d 545 (2d Cir. 1979) ("[T]here is a duty to correct or revise a prior statement which was accurate when made but which has become misleading due to subsequent events. This duty exists so long as the prior statements remain alive.") (internal quotation marks omitted); *SEC v. Shattuck Denn Mining Corp.*, 297 F. Supp. 470, 476 (S.D.N.Y. 1968) (holding that defendant had a "clear obligation to inform the investing public that negotiations previously announced as having been agreeably concluded were now re-opened, and that terms formerly agreed upon were abandoned").

it will update the public with news of any radical change in the company's plans." *Id* at 1434.

A few months after *Burlington*, the Third Circuit applied this standard in *Weiner v. Quaker Oats Co.*, 129 F.3d 310, 321 (3d Cir. 1997). The court held that the defendant's repeated guidance to investors that it would maintain its total debt-to-total capitalization ratio in a specified range could have induced a reasonable investor to expect that the defendant "would make another such prediction if it expected the ratio to change markedly in the ensuing year," which the defendant failed to do when it assumed a significant amount of debt to acquire another company. *Id.* at 317.

Consistent with the Third Circuit's decisions, the Second Circuit also recognized a narrow § 10(b) duty to update in *In re Time Warner Securities Litigation*, 9 F.3d 259 (2d Cir. 1993). The *Time Warner* defendant made numerous statements announcing its plans to raise capital through strategic alliances and expressing hope that alliance negotiations would go well. *Id.* at 262. Ultimately, negotiations did not go as well as expected, so the defendant initiated a new stock offering to raise capital, which diluted the rights of existing shareholders and caused the stock's value to decline. *Id.* The plaintiffs challenged the defendant's failure to disclose problems in the alliance negotiations and its consideration of alternative methods of raising capital. *Id.* at 267. The court held that the defendant did not have a duty to disclose problems in the alliance negotiations, because its initial statements expressing hope that the talks would go well "lack[ed] the sort of definite positive projections that might require later

correction." *Id.* But the court held that a question of fact existed as to whether the defendant had a duty to disclose its consideration of a stock offering, because reasonable investors could have understood the defendant's prior statements "to mean the company hoped to solve the *entire* debt problem through strategic alliances," an understanding that may have become misleading when the defendant began to consider a stock offering. *Id.* at 268. The court emphasized the limits of its holding, confining the duty to update to statements announcing a specific business goal and an intended approach to reaching that goal, and rejecting the notion that a company would be required "to disclose every piece of information in its possession that could affect the price of its stock." *Id.*

The First Circuit recognized a similarly limited duty to update in *Backman*, 910 F.2d at 17. The court held that "in special circumstances, a statement, correct at the time, may have a forward intent and connotation upon which parties may be expected to rely," and thus could give rise to a disclosure duty if changed circumstances render the statement misleading. *Id.* (citing *In re Phillips*, 881 F.2d at 1236).

These decisions of the First, Second, and Third Circuits thus draw a sharp distinction between run-of-the-mill, ordinary projections, statements of historical fact, and indefinite expressions of optimism, on the one hand, and forward-looking statements concerning fundamental corporate policy, on the other. These courts agree that the former set of statements cannot give rise to a duty to update, while the latter category—into which this case squarely fits—can.

2. The purportedly conflicting decisions from the Seventh, Fourth, and Eight Circuits only involved statements that fit into the first category described above. None involved a forward-looking, "live" statement concerning a defendant's fundamental corporate policy, so no actual conflict exists.

In the Seventh Circuit's leading case on the subject, *Stransky v. Cummins Engine Co.*, 51 F.3d 1329 (7th Cir. 1995), the defendant made historical statements about the performance of certain products and ordinary, run-of-the-mill earnings projections, which the plaintiff claimed became misleading because of subsequent events. *Id.* at 1334-36. As to the historical statements, the court recognized the existence of a "duty to correct," which "applies when a company makes a historical statement that, at the time made, the company believed to be true, but as revealed by subsequently discovered information actually was not." *Id.* at 1331. As to the ordinary financial projections, the court declined to recognize a duty to update. *Id.* at 1332.

But the court was careful to limit the reach of its holding on a duty to update. In a footnote that Petitioners ignore, the court declared:

> [W]e limit our analysis to whether a duty to update such predictions [about the performance of the defendant's products] exists. We express no opinion on whether the outcome would be the same if a plaintiff contested statements of intent to take a certain action.

Id. at 1332 n.4

The precise type of statement that the Seventh Circuit isolated and declined to analyze in *Stransky*—a statement of intent to take a certain action—drives this entire case. As described earlier, Petitioners repeatedly emphasized to Mr. Finnerty, in writing and at yearly sales conferences, that SLI "will continue to be a privately held company." These representations were not mere expressions of corporate hope and optimism. Petitioners did not just opine that staying privately held was preferable, nor state that we "hope" not to be sold. Because Petitioners had complete control over whether the company would be sold, unlike run-of-the mill financial projections, a declaration that the company would not sell itself was a definitive plan, an "assurance," as the Eleventh Circuit put it (App. 11a), which a reasonable investor would expect Petitioners to follow.

The Seventh Circuit has yet to address the issue it flagged but sidestepped in *Stransky*. Although that court has, at times, used broad language when discussing a duty to update, every case it has decided on the subject has involved an ordinary projection or historical statement of fact. *See, e.g., Higgenbotham*, 495 F.3d at 760-61 (historical earnings reports); *Gallagher*, 269 F.3d at 810-11 (historical statement of fact about uncertainties that would impact earnings and predictions of earnings growth); *Eisenstadt v. Centel Corp.*, 113 F.3d 738, 745-46 (7th Cir. 1997) (historical statements of fact that the defendant's "auction process was going well"); *Grassi v. Info. Res., Inc.*, 63 F.3d 596, 599-600 (7th Cir. 1995) (earnings projections). Since none of these decisions addressed a "statement[] of intent to take a certain action," *Stransky*, 51 F.3d at 1332 n.4, the broad language

rejecting a duty to update in some of them "cannot be considered binding authority," *Kastigar v. United States*, 406 U.S. 441, 454-55 (1972), on the narrow question presented in this case of whether such a statement could trigger a duty to disclose. Because that question remains unanswered in the Seventh Circuit, there is no conflict with the decision below, which actually cited *Stransky* with approval for the proposition that statements of historical fact do not give rise to a duty to update. (App. 8a.)

Nor is there any conflicting precedent in the Fourth or Eighth Circuit. The Fourth Circuit decision cited by Petitioners, *Hillson Partners Ltd. P'ship v. Adage, Inc.*, 42 F.3d 204 (4th Cir. 1994), only involved historical statements of fact regarding the defendant's earnings and ordinary financial projections, *id.* at 206-08, which were "neither material under the federal securities law nor pled with sufficient particularity to allege a claim for fraud," *id.* at 219. The court did not address a forward-looking, "live" statement concerning a defendant's fundamental corporate policy. Nor did it rule out the possibility of recognizing a duty to update in a different case. *Id.* ("Assuming that there can ever be a 'duty to update,' there was no such duty here."). In fact, prior Fourth Circuit decisions indicate that the court would deem a forward-looking statement actionable if it were "worded as a guarantee," *Raab v. Gen. Physics Corp.*, 4 F.3d 286, 290 (4th Cir. 1993) (internal quotation marks omitted), which is how the Eleventh Circuit ruled Petitioners' statements could have been understood. (App. 11a.)

Likewise, the Eighth Circuit decision Petitioners cite, *Minneapolis Firefighters' Relief Association v.*

MEMC Electronic Materials, Inc., 641 F.3d 1023 (8th Cir. 2011), only involved historical statements of fact, in the form of prior earnings reports and press releases about production problems at the defendant's plants. *Id.* at 1025-26. The court's refusal to recognize a duty to update such historical statements says nothing about its willingness to validate a duty to update forward-looking, "live" statements of fundamental corporate policy.

In short, there is simply no conflict among the Circuits about whether the specific type of statements involved in this case—forward-looking, "live" assurances that the company would not be sold—may give rise to a duty to disclose the company's extreme departure from its announced and oft-repeated path. The few circuits that have decided cases involving such statements have uniformly recognized the existence of a disclosure duty. The decision below adheres to this common approach. Accordingly, there is no confusion among the lower courts warranting this Court's intervention.

III. THE DECISION BELOW IS MANIFESTLY CORRECT.

Finally, review is unwarranted in this case because the carefully reasoned opinion below is correct. Requiring the disclosure of information necessary to prevent a "live," forward-looking statement about the fundamental direction of a corporation from becoming misleading is consistent with the text and purpose of § 10(b) and SEC Rule 10b-5, and does not impose on corporations an unmanageable burden to disclose a "constant stream of corporate information," as Petitioners exaggerate (Pet. at 2, 18-19).

Section 10(b) of the Securities Exchange Act makes it unlawful to "use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of [SEC rules and regulations]." 15 U.S.C. 78(j)(b). SEC Rule 10b-5(b), in turn, makes it unlawful to "omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading." 17 C.F.R. § 240.10b-5(b). These provisions "are broad and, by repeated use of the word 'any,' are obviously meant to be inclusive," and should "be construed 'not technically and restrictively, but flexibly to effectuate [their] remedial purposes.'" *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 151 (1972) (quoting *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186 (1963)).

The broad language of Rule 10b-5(b) embraces the disclosure duty recognized in this case. The Eleventh Circuit evaluated Petitioners' "will continue to be privately held" statements "in the light of the circumstances under which they were made," 17 C.F.R. § 240.10b-5(b), that is, in their "context," which the court deemed "significant" (App. 11a). This fact-specific inquiry, required by Rule 10b-5(b), led the court to conclude that there was sufficient evidence for a jury to find that those statements became misleading when Petitioners omitted to disclose their active merger negotiations to Mr. Finnerty. (App. 11a-12a.) That is precisely the conduct that Rule 10b-5(b) prohibits.

In addition, recognizing Petitioners' disclosure duty under these circumstances advances the policies

underlying federal securities laws. As this Court has emphasized "time and again, a 'fundamental purpose' of the various Securities Acts, 'was to substitute a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the securities industry.'" *Basic Inc. v. Levinson*, 485 U.S. 224, 234 (1989) (quoting *Capital Gains Research Bureau, Inc.*, 375 U.S. at 186). This philosophy is grounded in Congress' recognition that "'[t]here cannot be honest markets without honest publicity. Manipulation and dishonest practices of the market place thrive upon mystery and secrecy.'" *Id.* at 230 (quoting H.R. Rep. No. 1383, 73d Cong., 2d Sess., 11 (1934)). Permitting those in Petitioners' position to maintain the "mystery and secrecy" of material information that contradicts their prior, "live," forward-looking statements would condone and encourage the intentional deception of investors like Mr. Finnerty, in obvious conflict with the intent of Congress. Indeed, even some of the commentators Petitioners cite agree with the wisdom of recognizing the precise type of limited disclosure duty applied in this case. *See* Donald C. Langefoort & G. Mitu Gulati, THE MUDDLED DUTY TO DISCLOSE UNDER RULE 10B-5, 57 Vand. L. Rev. 1639, 1678-79 (2004).

Petitioners nonetheless seek to protect their "mystery and secrecy" on the grounds that the decision below creates an unmanageable, costly "continuous disclosure system" that requires a company to constantly update every prediction it makes. (Pet. 2, 18-20.) That claim is wildly exaggerated, for it ignores the narrow limits of the Eleventh Circuit's decision.

As discussed earlier, the Eleventh Circuit was careful to limit its decision to the distinct facts of this case. (App. 14a-17a.) Given its prudent refusal to consider whether Petitioners needed to disclose information to the public at large, and its deference to "entrust[ing] the timing of disclosures to the business judgment of corporate officers … so long as the company and its insiders abstain from trading in the company's securities during this period of nondisclosure" (App. 14a), the decision cannot reasonably be read to require a "continuous disclosure system."

Moreover, the repetition and foundational nature of the "will continue to be privately held" statements, together with Petitioners' extreme departure from that announced plan, create a unique fact pattern that further limits the reach of the decision. Charles Stiefel's decision to sell the company, a concept that had forever been "taboo," is precisely the type of "radical change in the company's plans" that then-Judge Alito recognized should be disclosed. *Burlington*, 114 F.3d at 1434. But as the *Burlington* decision further demonstrates, recognizing a disclosure duty under these limited circumstances does not give rise to a generalized duty to update any and every prediction, no matter the context or subject matter. *Id.* at 1433-34. Petitioners' example of a company reporting in its 10K that it "had a good year" (Pet. 18 n.7) illustrates their error. Such a statement would not give rise to a disclosure duty under the decision below because it is a statement of historical fact. (App. 8a.)

Nor does this Court need to intervene for the sake of certainty or uniformity, contrary to Petitioners'

suggestion. (Pet. 17-20.) The disclosure duty about which Petitioners complain has been recognized for decades, without having any apparent deleterious effects on the economy. Waves of mergers and acquisitions have risen and fallen without this Court's intervention. Moreover, this Court has consistently rebuffed requests for the type of bright-line rules that Petitioners seek. *See, e.g., Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1319-22 (2011); *Basic*, 485 U.S. at 236. It should follow suit here.

CONCLUSION

For the foregoing reasons, the Court should deny certiorari.

Respectfully submitted,

Peter Prieto
Stephen F. Rosenthal
Counsel of Record
Matthew P. Weinshall
PODHURST ORSECK, P.A.
25 West Flagler Street
Suite 800
Miami, Florida 33130
(305) 358-2800
srosenthal@podhurst.com

Norman S. Segall
SEGALL GORDICH P.A.
801 Brickell Avenue
9th Floor
Miami, Florida 33131

Counsel for Respondent

APPENDIX

APPENDIX

TABLE OF CONTENTS

APPENDIX 1

UNITED STATES COURT OF APPEALS

ELEVENTH CIRCUIT

CASE NO.: 12-13947, 12-15060, 12-15642

[Dated June 30, 2014]

TIMOTHY FINNERTY,	)
Plaintiff/Appellee,	)
VS.	)
	)
STIEFEL LABORATORIES, INC.,	)
a Delaware Corporation,	)
CHARLES STIEFEL,	)
Defendants/Appellants.	)
	)

AUDIO TRANSCRIPTION OF

ORAL ARGUMENT

(JUNE 30, 2014)

This cause came on for hearing before the HONORABLE JUDGE ANDERSON, HONORABLE JUDGE MOODY, AND HONORABLE JUDGE SCHLESINGER pursuant to notice.

[p.2]

APPEARANCES:

ATTORNEYS FOR PLAINTIFF/APPELLEE
PODHURST ORSECK, P.A.
STEPHEN F. ROSENTHAL, ESQ.
MATTHEW WEINSHALL, ESQ.
25 West Flagler Street
Suite 800
Miami, Florida 33130
Srosenthal@podhurst.com
Mweinshall@podhurst.com

ATTORNEY FOR DEFENDANTS/APPELLANTS
GREENBERG TRAURIG
ELLIOT H. SCHERKER, ESQ.
333 Southeast Second Avenue
Suite 4400
Miami, Florida 33131
Scherkere@gtlaw.com

ALSO PRESENT:
DAVID LISITZA
[Attorney for Securities And Exchange Commission][*]

E X H I B I T S

NUMBER DESCRIPTION PAGE

(No exhibits were marked during this hearing.)

---

[*] Bracketed alterations reflect Respondent's corrections to the transcript. Struck-though text was in the original transcript.

[p.3]

JUDGE ANDERSON: Last case for the morning is Finnerty, the Stiefel Laboratories.

Mr. Scherker?

MR. SCHERKER: Yes, your Honor.

JUDGE ANDERSON: For ~~appellate~~ [appellant] Stiefel Laboratories.

MR. SCHERKER: May ~~I~~ [it] please the Court, Elliot Scherker on behalf of the ~~appellate~~ [appellant]. In August 2007, pursuant to its duty to disclose material facts to shareholders ~~his~~ [its] $500 million investment into the company, which was a major change in SLI's corporate culture, and told the shareholders on a written communication, which was introduced as Defense Exhibit 32 at trial, there are currently no plans for Stiefel to become a publicly traded company, defined the Blackstone arrangement and defined the exit agreement with Blackstone and then concluded, senior management continues to evaluate all options, all options when looking at the long term financial needs of the company.

So the question on this appeal based on undisputed facts is whether as of January 6, 2009, the date ~~in~~ [on] which Finnerty unilaterally and irrevocably put his stock to SLI, meaning [p.4] SLI had a mandatory obligation to accept the put election and buy back the shares at a set price, whether on that date SLI had any duty to disclose its very preliminary exploration of merger opportunities to Finnerty to keep the August 2007 statement from becoming misleading after the

fact. We submit the answer is firmly and unequivocally no.

To begin with the law in this circuit and in every circuit to have addressed the issue, as this Court held in the Williams decision is, quote, in the context of sales of stock while negotiations for merger or acquisitions are pending, courts have found no duty to disclose the negotiations. Finnerty would have the Court impose a duty based on our purported obligation, as he puts it, to correct or update prior statements that SLI would remain privately held.

Now, the first flaw in this theory, we submit, is that correct or update is not the duty standard. The standard as established in ~~Chiarella~~ [*Chiarella*], this Court recently in the ~~FindWhat~~ [*FindWhat*] decision 658 F.3d at page 1305 put it this way: a party who discloses material facts in connection with securities transactions assumes [p.5] a duty to speak fully and truthfully on those subjects, and as this Court stated in the ~~Badger~~ [*Badger*] case, 612 F 3d at page 1341 where a defendant's failure to speak would render the defendant's own prior speech misleading or deceptive, there's a duty to disclose. So the controlling question comes down to did SLI's prior statements become misleading or deceptive between November 2008 and January 6, 2009, the date on which Finnerty exercised the put election.

JUDGE ANDERSON: And I think it's pretty clear that whether or not there's a duty and whether or not the prior statements give rise to a duty is a question of fact. Is that not true?

MR. SCHERKER: Well, it's a mixed question, of course, but the facts here are undisputed so it's coming to this Court.

JUDGE ANDERSON: Which in other words, it's a jury issue.

MR. SCHERKER: When the facts are undisputed, it's an issue of law for the Court, and the facts are undisputed.

JUDGE ANDERSON: I understand that. We'll go into that in a little bit. Your opponents [p.6] suggests it's not just this statement of when the Black[stone] investment was being made, but there's a history of statements over time to the employees to the effect that this is a family owned closely held corporation and will continue to be, statements going back a long time, and indeed including even a statement to the same effect which corroborates the prior statements by the son, ~~Brant~~ [Brent], very shortly after this put in early January. So I think you have to since it is a fact question for the jury, you have to consider the Blackstone press to release and e-mail to the employees at the same time as that press release which said something to the effect that we'll continue to be held by the family under the operation of Charlie Stiefel, the CEO. You have to consider the prior statement in that history of repeated statements. Do you not?

MR. SCHERKER: Judge, couple of -- the answer to the question is yes, but let's look at what the prior history is. First of all, the testimony that you're referring to, Judge, is Tim Finnerty's testimony at R 552 page 17 through 18. That's the testimony about the prior statements. It goes back to Charles [p.7] Stiefel's

father, Werner Stiefel, and over 20 years at firm meetings they would say it's going to be a privately held company. That's basically what their case is about, but it can't be about that because of what Stiefel did in August 2007.

Now, remember what happened. Blackstone made the $500 million investment. Finnerty himself testified that caused a lot of consternation among employees, including the possibility that the company might be sold. So what did SLI do in response to that in exercising its duty ~~that~~ [as they] put it to correct or update the prior statements. That's when we exercised our duty, performed our duty to disclose, Judge Anderson, because we didn't say in August 2007, no, SLI will be a privately held company until the end of time. SLI will always be private.

Those are the kind of statements that Tim Finnerty said had been made over a period of 20 years, and that's basically the sum and substance of that testimony. We didn't say in August 2007, this will always be a privately held company. If that had been what we said in [p.8] August 2007, Finnerty would have had a much better case, but what we said, Judge Anderson, if I could read the sentence from Defense Exhibit 32, there was a series of what they call FAQs, frequently asked questions, that were appended to the e-mail. This is the FAQ. Will Stiefel Laboratories be going public? That was the question and then the answer, there are currently no plans for Stiefel to become a publicly traded company.

Blackstone will have a defined exit arrangement with Stiefel at the end of eight years at which point Stiefel may choose to buy back its shares or exercise

other options, one of which might be an initial public offering.

Last sentence, senior management continues -- continues, not after eight years -- continues to evaluate all options when looking at the long term financial needs of the company. That is hardly an ironclad guarantee consistent with what Tim Finnerty said Werner Stiefel and Charles Stiefel had said over the years. We will always be a privately held company. No. It's that we will continue to look at all options. So we submit this was the disclosure. [p.9] That's why it's almost --

JUDGE ANDERSON: What part was in that same e-mail did it say we will continue to be privately held and the Stiefel family will continue to retain control and continue to hold a majority share ownership?

MR. SCHERKER: Judge, that's the press release. That's Plaintiff's Exhibit 189 in which that statement appears.

JUDGE ANDERSON: That is not in the e-mail.

MR. SCHERKER: What the e-mail says --

JUDGE ANDERSON: Under will continue to be a privately held company operating under --

MR. SCHERKER: Yes. It says Stiefel will continue -- it says the same thing that's in the press release.

JUDGE ANDERSON: Yes.

MR. SCHERKER: Stiefel will continue to be a privately held company operating under my direction as chairman, chief executive officer and president. The

Stiefel family will continue to hold the majority share ownership in the company.

JUDGE ANDERSON: So --

MR. SCHERKER: But we also said that we [p.10] will continue to evaluate all options.

JUDGE ANDERSON: -- does that take it out of being a question of fact into an undisputed fact as a matter of law?

MR. SCHERKER: These are the facts. The facts in this document are the facts. This is what we said in August 2007. The question is did anything that happened in November 2008 through January 6, 2009 have to be disclosed to keep this disclosure, this prior speech, from being false or misleading.

So what happened in November 2008 through January 2009? What happened was there was an unsolicited feeler from Sanofi-Aventis. We didn't go out marketing the company. We didn't have the company on the block. The undisputed testimony from Charles Stiefel, from Mr. ~~Muckerji~~ [Mukherjee], the Blackstone representative on the board was we weren't looking to sell the company at all. We had some cash flow problems. We had some revenue problems. We weren't marketing.

We got an unsolicited call -- not even an unsolicited call, an unsolicited indirect feeler, if you will, from Sanofi-Aventis. We followed up on it. As Mr. Stiefel testified, I [p.11] have a fiduciary obligation if I get -- to my shareholders, if I get a contact like that to reach out. He did. There was a preliminary meeting: No

discussion of price, no discussion of deals, no confidentiality agreement, essentially a meet and greet.

JUDGE MOODY: Let me just stop you a minute.

MR. SCHERKER: Yes, sir.

JUDGE MOODY: Let's go back to Judge Anderson's first question about whether or not perhaps this is a jury question. You started out by making the claim that Stiefel Labs had a mandatory obligation to accept the tendered stock on January 6.

MR. SCHERKER: Yes, sir.

JUDGE MOODY: They had no choice.

MR. SCHERKER: Yes, sir.

JUDGE MOODY: So part of your case is based on that mandatory obligation; right?

MR. SCHERKER: A piece of our case [where] that really matters is on the ~~Siantar~~ [scienter] issue.

JUDGE MOODY: Yes or no?

MR. SCHERKER: It's both yes and no unfortunately, your Honor, because as to the [p.12] first part of our case, if we had a duty to disclose, we had a duty to disclose to our shareholders. So we're not saying -- this is not the argument that Duff and Phelps made in ~~Smith V Duff and Phelps~~ [*Smith v. Duff and Phelps*].

JUDGE MOODY: Let me stop you there. Let's back up one week. One week prior to January 6 is when Stiefel Labs hires Blackstone.

MR. SCHERKER: Yes, sir.

JUDGE MOODY: To investigate the possibility of a sale.

MR. SCHERKER: Yes, sir.

JUDGE MOODY: So if there's no mandatory obligation to accept tendered stock one week later, don't you agree that it's a jury question about whether or not there was a duty to disclose or abstain from buying the stock on January 6.

MR. SCHERKER: To answer the question directly, no, sir, we don't agree that makes it a jury question. The importance of the put election is really much more in terms of the new arguments raised on appeal by the SEC and by Finnerty to try to support the verdict. It is an absolute truth and they now admit it, though [p.13] they didn't at trial, that we ~~have~~ [had] no choice but to accept the put election. It's important because we weren't trading in our own stock. It isn't insider trading. It isn't negotiating with a corporate -- insider negotiating but the --

JUDGE MOODY: That's not what they said. What they said was that ERISA gives you an out that you do not have a mandatory obligation to purchase tendered stock.

MR. SCHERKER: And they're wrong, your Honor. They're absolutely wrong. They now agree on appeal ~~then~~ [that] when there's a put, it's in their brief, when there's a put, we have to accept --

JUDGE ANDERSON: They may or may not be wrong, but I'm not totally convinced they are wrong. In

fact, I'm inclined to think that you -- while you did have an absolute obligation with respect to the put, it was not irrevocable in this sense. It could easily have been rescinded by mutual agreement of the two parties, and you could have called Finnerty in as in ~~Smith~~ [*Smith*] and ~~Jordan~~ [*Jordan*] in the Seventh Circuit, ~~Smith~~ [*Smith*] in the Eleventh Circuit required [p.14] confidentiality and given him an option to rescind the put.

Now, there's a question in that regard: How many puts were actually made between November 29, which I think is the date of the first indications of this merger, and when the Wall Street Journal published it in March? How many puts were there?

MR. SCHERKER: Judge, I don't know that that information specifically is in the record, but let me fix two things here. It was November 23 when the first conversations occurred and the put period ended in February because then there was a mandatory blackout by virtue of the revaluing of the shares.

JUDGE ANDERSON: So are we talking about the puts that would have been -- or really are we talking about the puts that were actually placed between that November 23 date and January 6 in effect.

MR. SCHERKER: And, of course, we're only talking about Finnerty because he's the only party on this appeal.

JUDGE ANDERSON: That's right, but relevant to the question of whether -- in other words, I [p.15] think you have the obligation that ~~Smith~~ [*Smith*] ~~on~~ [our own] circuit indicated to make this confidential disclosure which would eliminate the concern about a

public disclosure which does concern me considerably that it would, at the very least, ~~tender~~ [hinder] merger negotiations and perhaps be seriously adverse interest to the corporation and all of its shareholders. But there is no such concern about a public offering if the number of people to whom you could have put this, to whom you could have made this confidential disclosure is anything like the 40 involved in ~~Jordan~~ [*Jordan*] or in ~~Smith~~ [*Smith*]. I don't think we know how many, but if, you know, if there were 500 people, I would be concerned about the public knowing about these negotiations, but -- do you understand why I'm asking the question about the numbers?

MR. SCHERKER: Yes, sir, and let me answer it a couple of different ways because there's a couple of points that need to be made here. First, there were five to 600 participants in the plan.

JUDGE ANDERSON: Right.

MR. SCHERKER: Second, there are 100 [p.16] shareholders in addition to the five to 600 participants in the plan so we are talking about a large number of people overall. We have no control over when someone exercises a put. The statute says we have to honor it. The regulations say we have to honor it. Now, remember, Finnerty had been fired. He was not happy about having been fired.

JUDGE ANDERSON: He had been fired in a RIF; is that correct?

MR. SCHERKER: That's correct. He had a conversation with Charles Stiefel about how he was unhappy about his package, and then he went to work for a competitor. So the SEC's theory would mean that

if we get something from a disgruntled employee who is now working for a competitor as to which we have a statutory obligation to honor the put that we should reach out for that disgruntled employee working for a competitor and say how about giving us a confidentiality agreement before we pay you on your put, as to which Finnerty could easily say no, I'm not going to do that, give me my money, and then go running back to his employer and say something is going on at SLI.

[p.17]

Nothing supports that kind of bizarre result that would essentially make us disclose to the world ~~and the guys that are~~ [in the guise of] supposedly being fair to Finnerty and would violate our fiduciary duty to our other shareholders and plan participants, which is to pursue this opportunity without putting it on the Wall Street Journal front page. We know what happened when it went on the Wall Street journal's front page on March 20, four days before the deal was done: People were being fired, people were concerned all over the place, and a competitor gets that information in the scenario that you described, Judge Anderson, and they can go after our customers, they can go after our employees, they can go after our top performers, nothing in the law -- everything in the law ~~saying~~ [says] otherwise. So it all comes back to --

JUDGE ANDERSON: Everything in the law except ~~Smith~~ [*Smith*].

MR. SCHERKER: Judge, it's very important that Smith, this Court assumed a duty to -- the information was material. The defendant, Duff and Phelps, in this

case, was taking the [p.18] extraordinary position that we would have a duty to disclose to the world, but we have no duty to disclose to these insiders because they signed a contract. They essentially waived it. That's the only issue you decided in ~~Smith V Duff and Phelps~~ [*Smith v. Duff and Phelps*] was if you have a duty -- assuming you have a duty because it says that right in Judge Johnson's opinion, will assume that it was material and would have had to have been disclosed, for example, by a public corporation. You said, what a result it would be that a publicly traded corporation would have a duty to disclose but a private corporation wouldn't. It was the reverse, but you also recognized in ~~Smith~~ [*Smith*] that premature disclosure of sensitive merger negotiations kills mergers, and it's just a matter of common sense that it would. That it was definitely a possibility.

Stiefel has a fiduciary obligation to all of its shareholders to pursue all options for the company and to create a scenario from whole cloth. It doesn't exist anywhere in the case law that says you have an obligation to call on a planned participant who was working for a competitor who was under no obligation to do [p.19] anything with you and disclose this otherwise undiscloasable information.

And Judge Moody, let me get back to where I was before. If we had a duty to disclose the almost nonevents that occurred in the preliminary exploration events that occurred between November 23 and January 6, 2009 to make our prior statement not misleading, we have that same duty as to all shareholders, as to everybody to whom we should have

disclosed just as we did in August 2007, so it starts with that. If we didn't have a duty --

JUDGE ANDERSON: I'm not sure that's correct either. It is true that I think both ~~Smith~~ [*Smith*] and ~~Jordan~~ [*Jordan*] arose in the context of a closed corporation, and it's also true that the general rule that disclosures, the duty to disclose arising out of prior statements becoming misleading applies to a public corporation as well as a closed corporation.

MR. SCHERKER: Yes, sir.

JUDGE ANDERSON: All that's true, and I have seen no cases on this, but I also know ~~supreme code and basics~~ [the Supreme Court in *Basic*] said that this concern about the publicity in a merger situation [p.20] relates to the duty to disclose rather than materiality, which was at issue in ~~basic~~ [*Basic*].

Therefore, it seems to me as a matter of common sense that the duty might be different in different situations, and the duty might be different here if the company could have disclosed confidentiality in confidence to this employee as opposed to a public corporation. You see what I mean?

MR. SCHERKER: I do, your Honor. Duty to correct a prior statement. Let's just call it that for short.

JUDGE ANDERSON: Which is a fact issue and therefore very fact sensitive which seems to me this public concern would weigh into that.

MR. SCHERKER: Judge, bear in mind and I know I'm way over my time and I apologize.

JUDGE ANDERSON: This is a hard case and we're going to provide time.

MR. SCHERKER: Thank you, your Honor. It's important to take a step back and remember that the closed corporation duty to disclose theory was never tried. That was never tried.

JUDGE ANDERSON: I understand that. That came up on --

[p.21]

MR. SCHERKER: Posttrial.

JUDGE ANDERSON: Rule 50.

MR. SCHERKER: And is raised here as right for the wrong reason. We never had the opportunity to try what you call the fact intensive question of duty that a closed corporation would have to this jury. We didn't have an opportunity to try the question whether we should even be treated as a closed corporation for purposes of imposing this duty. There is no standard anywhere in federal law for that. The SEC wants to make it any privately held corporation, use this Court essentially for a rump rule making process to create that rule.

We believe it's under Delaware law. We believe a jury would have had to have been instructed on the law to determine, one, whether we're a closed corporation, but more importantly the key factual issue in this trial wasn't duty. The key factual issue in this trial was ~~Siantar~~ [scienter] as we note in our second point on appeal. We never had the opportunity to defend against a closed corporation theory based on ~~Siantar~~ [scienter].

As a matter of fact, the district judge excluded all lay testimony that we tried to [p.22] present on whether we had -- was an automatic put, which they now admit -- we had to accept the automatic put, which they now admit so the issue that we're discussing here, if the Court is going to regard it as fact intensive was never tried to a jury, and if the Court is going to establish a rule something like what the SEC wants, then we should get a new trial where we can defend against that, particularly on ~~Siantar~~ [scienter]. Let's put that over here for now.

The duty question that you're raising is still this is still an omissions case. Read their brief. They will tell you on appeal this is a pure omissions case. The duty to disclose in a pure omissions context arises from one of two places: Fiduciary duty, special fiduciary duty that requires it or a duty to correct a prior statement. All they get, all they get from their new duty, the newly created duty on appeal based on closed corporation status is fiduciary duty to disclose what this Court presumed in ~~Smith~~ [*Smith*], for example, was material information. That issue wasn't decided, it was presumed.

So if they get a duty under that special [p.23] fiduciary duty or if they get a duty, which we admit we could have had if it made the prior statement false or misleading not to disclose, we're still in the same place and the question is did we have to disclose -- under either duty scenario, did we have to disclose the preliminary discussions that occurred between November 23, 2008, most of which were internal, only one of which was even an external preliminary conversation, did we have to disclose the Blackstone

engagement to explore alternatives, so as to make our August 2007 disclosure that senior management would continue to consider all options for the company's financial future not false and not misleading.

JUDGE ANDERSON: Okay.

MR. SCHERKER: Either way they end up in the same place.

JUDGE MOODY: You sent the notice out on December 22, 2008 about current price. Wasn't there a communication to Finnerty around December 22?

MR. SCHERKER: That wasn't current price, your Honor. That wasn't current price. That was the valuation done in October in the [p.24] standard course that we always have to do every year under ERISA and it was a price as of March 2008.

JUDGE MOODY: Right.

MR. SCHERKER: It was as of March 2008.

JUDGE MOODY: Right, but by then the discussions had already started.

MR. SCHERKER: By then there had been a preliminary meeting, but the disclosure was the price in March --

JUDGE ANDERSON: I had that question too, that December 22 letter to him in effect reminded him that he had the opportunity to make this put. Is that not what it did?

MR. SCHERKER: He said he made the put because we were changing our plans.

JUDGE ANDERSON: Answer my question, Counsel. Did not that December 22 letter remind Finnerty that he had an opportunity to make this put.

MR. SCHERKER: I don't recall him saying that it did, but it could have had that affect, but we didn't invite it. We didn't invite him to trade, and he testified that the reason he cashed in was because -- had nothing to do with [p.25] anything else except that we were changing our benefit plan, we were changing our 401K, we were putting them together in one, and he said, you know, you're changing the plan, I decided to get out.

JUDGE ANDERSON: All right.

MR. SCHERKER: So that was his motivation without dispute.

JUDGE ANDERSON: I interrupted you. Did you have further questions about that.

JUDGE MOODY: No.

MR. SCHERKER: Judge, what I was saying was it was an as of March 31, 2008 price. That's all that was communicated, and under ERISA you value once a year and it stays that whatever period a put can be exercised.

JUDGE ANDERSON: Did he answer your question, Judge Moody?

JUDGE MOODY: I've heard enough.

JUDGE ANDERSON: Okay. Thank you, sir.

MR. SCHERKER: Thank you. I appreciate the extra time, your Honor.

JUDGE ANDERSON: Mr. Rosenthal.

MR. ROSENTHAL: Good morning. May I please the Court, Stephan Rosenthal along with Matt [p.26] Weinshall at counsel table on behalf of Tim Finnerty.

As the Court knows, Mr. Finnerty was an employee as a salesman for his career at Stiefel Labs. For 22 years, he heard the same mantra repeated, and this is the history, your Honor, Judge Anderson mentioned that the company is proud to remain a privately held company. Going back to 1847, I had to look this up, James Polk was in the White House at the time. This company had recited that mantra time and time again.

Mr. Scherker represented that the only testimony was Finnerty's about the history of those representations, but in fact there was testimony from two other witnesses about that history, ~~Suny~~ [Sunni] Buria and Richard ~~Machi~~ [Mackay], both of whom testified that was the drum beat and the steady constant message from the company. The jury found in this case that the defendant's actions of not disclosing a ground breaking decision to completely reverse courts with all history in the company and inconsistent with every representation they had ever made concerning what the company was going to do in [p.27] the future and to actually take action from November through December of 2008 at the very time that Mr. Finnerty and a number of other employees who had been RIFed were making the one time only decision that they had for the very first time, the window --

JUDGE ANDERSON: How many puts were there during this period of time?

MR. ROSENTHAL: I don't know the answer, your Honor.

JUDGE ANDERSON: I need to know it. Is it in the record, do you think?

MR. ROSENTHAL: I'll have to ask my co-counsel to see if he can find it for us during the argument. We'll endeavor to do that.

JUDGE ANDERSON: All right.

MR. ROSENTHAL: And if we can't, we certainly can submit something right afterwards.

JUDGE MOODY: Would you address opposing counsel's statement that you now concede that the put on January 6 was mandatory on them to accept without disclosing or abstaining.

MR. ROSENTHAL: Yes. What we concede is that under the law, as of the date that a put is made, there's an obligation to pay under the [p.28] internal revenue code, 26 USC 509 or so.

JUDGE ANDERSON: Within 30 days.

MR. ROSENTHAL: Right. Within 30 days, Judge Anderson.

JUDGE ANDERSON: Unless to do so would cause a breach of fiduciary duty or would violate the securities laws. Is that not correct?

MR. ROSENTHAL: I believe that's correct and to your specific questions about whether or not they could have done something with regard to a confidentiality agreement in advance, obviously, that's a little different than what you're asking. But after January 6,

could they have refused to honor the put is an issue that wasn't really tried in this case because plaintiff's counsel deliberately limited his argument to the jury and limited the case to --

JUDGE MOODY: Well, isn't the issue whether or not they had a duty to disclose or abstain, not really whether they had to honor the put.

MR. ROSENTHAL: That's exactly right. Let's mark January 6 as a critical date. We don't need this issue of what they could have done afterwards and the Court doesn't, [p.29] respectfully, to affirm this because the case was pitched as what should they have done before January 6, which is the day that Mr. Finnerty delivered his put. Okay. The evidence is overwhelming not only that they had a duty, because it is as Judge Anderson pointed out, a jury question as to whether or not the omissions were material and the jury found that they were, but it's also -- I'm sorry, misleading, but it's also a jury question as to whether the omissions were misleading and -- sorry, were material. I always get those two confused.

Let me just tell the Court this quick rendition of those facts. I'd like to hit on Judge Moody's question which went earlier to materiality and the questions about duty and then take on the ~~Siantar~~ [scienter] and ERISA issues in that order, if possible.

On November 26, 2008, Charlie Stiefel and his sons get together. They have this meeting on Thanksgiving day, which doubles as a compensation committee meeting for the company because they control the company. They make a decision on that date because of conversations, which is all documented in e-mail, that

Mr. [p.30] Stiefel, Charlie, has with Blackstone's person who is on the board at Stiefel by virtue of their half billion dollar investment in the company, which also happens to have a mergers and acquisitions investment banking arm that they ought to look into selling the company, and they broach what is called a taboo subject. Taboo because forever they've never even considered selling the company. On the same day, they had that conversation with the investment bankers who give them an idea of potential earnings multiples that there could be.

JUDGE ANDERSON: What day is this?

MR. ROSENTHAL: November 26, Thanksgiving day 2008.

JUDGE ANDERSON: Okay.

MR. ROSENTHAL: And there's an e-mail on Plaintiff's Exhibit 114 and 115. On the same day at that meeting, they decide to do something unprecedented. They give employment contracts to top executives at the company, something that had never, ever been done. Those employment contracts contained two very eyebrow raising terms: One was that if there was a change of [p.31] control, these people with these contracts, the select top few executives, would get bonuses, and if there was a merger, this new stock that they got, preferred shares, would accelerate ~~investing~~ [in vesting] upon a merger.

On December 8 about a week and a half later, they have a meeting with Blackstone's merger and acquisitions group, which presents to them the Stiefels a 50 page plan, which is in the record as defendant Exhibit 300 in the appendix which has targeted tier

one acquirer companies, one of which was GlaxoSmithKline, which ended up being the one that purchased them, potential prices, and a projected schedule for the sale of the company, which in retrospect, turned out to be only a month off.

Between December 10 and December 30, again, all before January 6, Charlie Stiefel negotiates with Blackstone's M&A group, the investment banking arm the terms of a retention agreement. They finally signed that agreement, the draft is I think dated December 16, and they finally sign the agreement on December 30. But they're back and forth throughout the month of December, and that agreement specifically charges Blackstone, [p.32] M&A, to negotiate ~~an effective~~ [and effect a] sale of the company.

Again, during the time on December 22 when Blackstone -- I'm sorry, when Stiefel Labs sent Mr. Finnerty this letter reminding him of the opportunity to sell his shares. On December 22, coincidentally, that very same day, Mr. Stiefel, Charlie Stiefel has a summit with the CEO of Sanofi-Aventis, a large pharmaceutical corporation, that it expressed interest in buying the company ~~in~~ [and] which started this process.

It's not just the two CEOs together, they both have advisors, investment bankers and the evidence says that the Sanofi folks had worked up a detailed valuation of Stiefel Labs which indicated to the Blackstone people that they were serious about acquiring the company. Under this ~~Courts precedented SEC versus Ginsburg~~ [Court's precedent in *SEC v. Ginsburg*] where you have a meeting of the CEOs and there's price terms that have been contemplated on

both sides, that's a very material development, and the last point I want to make on materiality without beating it dead is that after that meeting on the same day, Charlie Stiefel, the [p.33] controlling shareholder, CEO and chairman of the board who had the ability to control the decision making as the jury found in this case of Stiefel Labs writes his sons who are also board members and his wife saying I'm excited to move forward.

So there's no question that there were material developments that were completely omitted from shareholders during the time relevant before January 6.

And the icing on the cake on this is that none of those top executives who had knowledge of what you call project jump sold their shares during this time. They all held on to it and they made a four times multiple just two to three months later when the deal was consummated. That's materiality.

My co-counsel, Mr. Weinshall has given me the testimony that Judge Anderson, you had asked for, and, I believe it's on pages 32 to 33 of the record volume that contains his testimony. I don't have that right here.

JUDGE ANDERSON: Of whose testimony?

MR. ROSENTHAL: Tim Finnerty.

JUDGE ANDERSON: Okay.

[p.34]

MR. ROSENTHAL: I'm going to read the note he handed me because it might be responsive to your

question. He testified that he received the put request from and as a result -- the form. As a result, made the decision to sell his shares because if you recall, the facts of this case in approximately October 2008, he received notification from the company, which is something the company does and, by the way, this is relevant to the general issue of, boy, this is a difficult obligation on us to disclose to our five or 600 plan participants whether -- you know, what we're doing. Very limited field of people, and they don't find out as they've argued in one of their briefs just after the fact at which point their hands are tied by their construction of ERISA.

They actually reach out to these people and notify them. Why? Because this is a -- the only time you become eligible is death, retirement, or termination, so it's not the type of thing that's on employees' minds throughout their careers at the company. There's a realization event, so to speak, they notify them.

[p.35]

So in October, they notified Mr. Finnerty. He said he decided and his testimony is to this effect, he wanted to stand pat. He wanted to hold onto his shares. It wasn't until December 22, 2008 when the company sent another letter that effectively solicited his selling of his shares that he decided -- he changed his mind. He actually made some calls back and forth to the company, wasn't able to get any information that really revealed enough to him and decided to do it.

Let me speak about duty. Judge Anderson, you're absolutely correct that the fact-based portion of this, which the jury determined, is pivotal because we agree

on the standard. The Rudolph case, which Judge Anderson, you were on the panel from and the Ziemba case, which, Judge Anderson, you wrote, say that a duty to disclose arises where a defendant's failure to speak would render the defendant's own prior speech misleading or deceptive. That's the standard. The jury determines whether or not something was misleading. That's the Clay versus Riverwood case, also the Time Warner's Securities case from the second circuit. The question for the [p.36] trier of fact.

Mr. Scherker started by reading this e-mail from 2007 about some ambiguous, in my opinion, language about the time that they might consider all options. Without getting into the ~~35:16~~ parsing of that language, I think we can all say from a common sense objective standpoint, at best it's ambiguous and, therefore, at best it's a jury question, and the jury determined that it was materially misleading.

In addition, as Judge Anderson pointed out, the e-mail itself from Charlie Stiefel said, which enclosed as an attachment these frequently asked questions that contained the language that defendants are relying upon, his cover e-mail to his -- to ~~plaintiff's~~ [plan] participants which is sort of the overriding statement says I want to emphasize a few key messages that are important for all employees to understand. Stiefel will continue to be a privately held company operating under my direction as chairman, CEO, and president, and the Stiefel family will continue to hold the majority share interest -- ownership in the company, point-blank.

They don't equivocate. They don't make any [p.37] protective statement that's buried down in the

frequently asked questions in ambiguous language, which frankly, we think only signifies as to anybody reading it that in eight years after the $500 million investment by Blackstone matures, we may consider other options because that's what it says. In the press release that they make on the same day, they mirror the absolute language that Charlie Stiefel tells all of his employees. They don't qualify it.

With respect to duty arising from the price per share issue, I want to just tell the Court something interesting that may not be as clear in the briefs and it's something that has been benefitted by the SEC's presentation. So in October 2008 they send him the e-mail which tells him that the share price is $16,469 a share. On December 22 in that letter, they send him the current share price. Admittedly it has a parentheses underneath it that says March 31, 2008, but what is their obligation to reveal a fair and current , quote unquote, share price?

The plan certainly doesn't restrict them from doing anything different. They sort of protect themselves by saying well, we were [p.38] obligated only to disclose as of the previous valuation date which happened to have been March 31 at the end of the fiscal year for us. Well, ~~no,~~ [not] so if you look at the plan, the plan just says you have a right as a participant in the plan to get the current fair market value as of or as per a regulation. This is Plaintiff's Exhibit 56, section 7.6.

Then you go look to that regulation which is in the record. It's 54.4975-11D5, and that says, one, valuations must be made in good faith, and, two, the value must be determined as of the most recent valuation date under the plan, cross-references back to

the plan. So then when the valuation has to be done under the plan? There is no fixed valuation date under the plan. There is no fixed valuation date.

In fact, what it says in section 9.7 is the value shall be determined, quote, from time to time as may be necessary for any purpose under the plan. Well, we submit that one of the purposes under the plan is to comply with the regulation that requires valuations to be done in good faith and also to comply with the securities laws so their valuations are not [p.39] protected by any language in the plan.

JUDGE ANDERSON: Let me ask you a few questions. Is it not true that the obligation to buy as a result of the put is subject to the exceptions, one, if it would violate the fiduciary duty to do so and, two, if it would violate the securities laws? Is that true or not.

MR. ROSENTHAL: Yes, I think that's right. In fact, and I get the -- we did not argue that in detail in our brief, but certainly what the 28J letter from the SEC who may be in a better position to address this issue says, look, this is the position -- not only does this make sense and if you look at the Sarbanes-Oxley provision that we've talked about in the briefs concerning that exemption to the blackout period, it's sort of a cousin to the argument you're talking about, your Honor. That makes clear there's harmony between the statutes.

The position that the SEC has brought to the Court's attention that the solicitor general and the Department of Labor are taking before the United States Supreme Court right now on a cognate issue is that an ERISA, compliance with [p.40] an ERISA plan cannot require one to violate the securities laws.

Basically, you have to comply with the securities laws and if it turns out that you haven't been a faithful plan administrator in so doing, I don't think anybody can say that you have acted unlawfully or imprudently by following your obligations under securities laws to disclose because just to that point had Mr. Finnerty given the put and then they said you know what, we really need to tell this guy, they had a ~~conscious~~ [conscience] moment and they said before we take his money, his retirement and sell it on the cheap, because we know it's going to be on the cheap at this point, let's let him know. If they had told him, I think your Honor is absolutely correct, and I'm not aware of any principle of law that would prohibit --

JUDGE ANDERSON: What about just delaying even without letting him know, without disclosing, just delaying because to abide would violate the securities laws or the fiduciary duty.

MR. ROSENTHAL: Correct and that's the disclosure [or] abstain, I think, portion. The [p.41] abstain portion of the options were available to them and the problem is they did not do that. They should have said to shareholders, if they didn't want to disclose because they felt this was too sensitive and could jeopardize the deal.

JUDGE ANDERSON: The problem from your standpoint is that was not presented to the jury, was it?

MR. ROSENTHAL: The issue of whether they could do it before January 6 was.

JUDGE ANDERSON: Yes, the blackout was presented to the jury, which is a related question.

MR. ROSENTHAL: Yes. If I can take a moment to speak to that.

JUDGE ANDERSON: I'd like to hear about that.

MR. ROSENTHAL: Okay. So you know, let's remember this all is packaged under ~~Siantar~~ [scienter], first of all, so the standard of review here is very differential because it's a denial of a motion for new trial. Judge King was evenhanded in his rulings. Ultimately what happened in the terms of the evidence that came out at trial was that the defendants were able to put in [p.42] testimony from their witnesses that said we were not permitted to dishonor the put, you know, the judge did not allow legal testimony concerning what a blackout meant and, frankly, it's very confusing, and so it's probably best that he did not, but he allowed them to get their jury charge on ~~Siantar~~ [scienter] as well.

JUDGE ANDERSON: What was the jury charge?

MR. ROSENTHAL: The jury charge was at record 509[:]12, the standard jury instructions from the Eleventh Circuit at the time, and this was sort of a debate within a debate, but the first sentence of that instruction says it must be shown that the defendant acted intentionally and with a mental purpose to deceive, manipulate or defraud, that's uncontested. That's the standard for ~~Siantar~~ [scienter]. It goes on then to -- there's two other sentences or clauses. One represents the material misstatement and the other represents a material omission. This was an ~~omission's~~ [omissions] case tried as an ~~omission's~~ [omissions] case, and that second sentence says that the defendant acted in that way if he knew of the existence of material facts

that were not disclosed, although the defendant also knew that knowledge of those [p.43] facts would be necessary to make the defendants[’] other statements not misleading. That’s the failure to update.

JUDGE ANDERSON: Okay. Now, tell me a little bit about what issue with respect to the blackout was before the jury.

MR. ROSENTHAL: The question I believe of whether or not Stiefel Laboratories could have abstained prior to January 6 was a question -- they argued to the jury that they had to honor this put election, so they had the benefit of what we’re calling this blackout issue even though they did not have a specific instruction concerning it.

JUDGE ANDERSON: Right.

MR. ROSENTHAL: So it all relates to ~~Siantar~~ [scienter]. If they were able to argue that -- and the other thing is they also got to argue that this is their belief. Whether or not they’re right or wrong on the law, this is our belief that we didn’t have a choice here, folks. We had to honor these put elections. We didn’t -- we couldn’t put in a blackout. We couldn’t prevent trading. Turns out they’re wrong, but the point is they got to argue --

[p.44]

JUDGE ANDERSON: What was evidenced that they were wrong before the jury?

MR. ROSENTHAL: I don’t recall, your Honor. I don’t recall if there was specific evidence that said you could not impose a blackout because the judge

precluded that legal argument because it really is a legal question. All we argued was that prior to January 6, they had an obligation to disclose what was going on to Mr. Finnerty or at least not trade, close the trading window, just say something like --

JUDGE ANDERSON: So you argued that they had the right to impose a blackout.

MR. ROSENTHAL: Prior to January 6.

JUDGE ANDERSON: Yes.

MR. ROSENTHAL: And frankly --

JUDGE ANDERSON: In other words, at the beginning -- in other words, you argued to the jury that when negotiations with the merger started, they could have imposed a blackout, and actually you had, as I recall or I'm recalling now, you had some evidence from lay witnesses that blackouts were imposed from time to time.

MR. ROSENTHAL: That's correct. And I've just found the portion of the argument that I [p.45] wanted to point you to, your Honor. On record 555, pages 47 to 48, plaintiff's counsel argued to the jury in closing that a suspension should have been imposed when they started considering a sale of the company. Right. This is before January 6.

Basically, they should have imposed a black -- not a blackout. That's a term of art. They should have imposed a suspension when they started considering a sale of the company. So from Thanksgiving through New Year's or really until January 5, in this case it would[n't] have made a difference, they had an

obligation and I don't think that there's any question in the law that they were prohibited from doing so when you look at the arguments about how Sarbanes-Oxley provision and the regulations interface with the ERISA provisions -- I'm sorry, the securities provisions. I realize I'm way over time. I have another issue I would like to talk about, but in light to have Court's --

JUDGE ANDERSON: Did he answer your question?

JUDGE MOODY: Yes.

JUDGE ANDERSON: All right. Thank you, [p.46] sir.

MR. ROSENTHAL: Thank you, your Honor. We respectfully urge the Court to affirm.

JUDGE ANDERSON: All right. Mr. ~~Lasitza~~ [Lisitza], would you pronounce your name for me?

MR. LISITZA: Yes. It's Dave Lisitza.

JUDGE ANDERSON: Lisitza.

MR. LISITZA: Lisitza. It's very hard. For the Securities Exchange Commission as amicus in support of the plaintiff appellee urging affirmance.

In the course of discussing the two independent duties that the defendants had, I think I can maybe touch on some of the questions that you've already had. The first is with regard to the duty that arises from someone's prior speech. The defendants say that they did have such a duty to update and give more information about the status of the company and they say, but we made a statement that then nullified that. It neutralized the natural normal implications of what

we already said, and surely there can be times when a company has a duty to update, which they say they do, and it could be neutralized, but in those [p.47] circumstances, we think that it's a factual question.

It would be very difficult to decide that as a matter of law and you have a jury verdict here so it seems there's not a great deal of controversy about the duty to update.

JUDGE ANDERSON: I think we understand that. We understand that argument.

MR. LACITA: Okay. Yes, but I believe that's all there is to say then about that. We can then turn to the separate independent duty they have whereas if they say nothing, do they still have a duty to disclose or abstain? The Court asked concern about the number of puts, which is a real concern in the normal case because you would not only have to make disclosures, especially about a merge[r] context. You don't want that information getting out, but first of all, that does not change the fact that they have a duty. It might change how they execute it. Abstention might be more appropriate in those situations.

The second point that we would like to make is that --

JUDGE ANDERSON: Could they really abstain?

[p.48]

MR. LISITZA: Could they?

JUDGE ANDERSON: Yes.

MR. LISITZA: Yes.

JUDGE ANDERSON: Under what authority?

MR. LISITZA: Well, we brought the Court's attention to the idea that the Department of Labor has taken a position that they can abstain from trading, and they -- the Department of Labor based that and supported its brief with two cases, the ~~Harris verses Amgen~~ [*Harris v. Amgen*] case from the Ninth Circuit.

JUDGE ANDERSON: Give me the cites if you...

MR. LISITZA: Yes. It's 738 F.3d 1026.

JUDGE ANDERSON: Okay.

MR. LISITZA: At 1041 to 42. That's in our 28 J letter.

JUDGE ANDERSON: Okay.

MR. LISITZA: The second case that absolutely says this is ~~Kopp versus Klein~~ [*Kopp v. Klein*], 722 F.3d 327 at 340.

JUDGE ANDERSON: What court is that?

MR. LISITZA: That is the Fifth Circuit.

JUDGE ANDERSON: Okay.

MR. LISITZA: Both of those cases were [p.49] decided after the briefing here was complete.

JUDGE ANDERSON: Okay.

MR. LISITZA: Now, the actual mechanics of how they abstain, both cases just say you have to do it, and the Department of Labor says you cannot trade on inside information if you [are a] plan fiduciary. The actual mechanics we think are described in that ERISA

provision that we pointed out that's part of section 36 of Sarbanes-Oxley. It's very mechanical though. I mean, when the Department of Labor said, yes, you can do this, they just said, you know you absolutely can't trade on this information. Don't allow new redemptions to occur, don't allow sales to occur. And the mechanics I think were blessed then in Sarbanes-Oxley, but I believe that was a duty that was dischargeable and that people would have, corporations would have even prior to Sarbanes-Oxley and the Department of Labor doesn't say you must use this provision. I think it's a very mechanical point.

But there's one other point I wanted to make about the number of puts because I know that's data you're looking for and I don't have [p.50] it, but we did point out that the ~~commissions~~ [Commission's] case is that the part of the fraud here was that the defendants wanted to accelerate buy backs and this is not the first time you've heard this from us. It's on the first page of our brief. It goes from the first page to the second page.

Part of it was they wanted to accelerate buy backs. The company had always -- the allegation is and it's not part of this case, the SEC's allegation is that there was an acceleration. The company had always offered its own stock and then it tried to move people into what was more diversified. Don't put all your eggs in the Stiefel basket, you should also be in IBM, you should be in Apple, and in that matter fraudulently accelerate the buy backs so if all you had before you was a large number of redemptions, large number of puts, that might not be all the data you're looking for in this particular case, even though it might be relevant to how a regular company, you know, discharges its duty.

I think that the only other point that I should address is -- well, maybe two other points. The first is it's not a new rule [p.51] making. As the Court recognized, it exists for closed corporations a duty to abstain or disclose. It exists for public corporations. There's no distinguishing factor about a privately held company when they control the shares. It's very appropriate.

JUDGE ANDERSON: Let me ask you a couple of questions.

MR. LISITZA: Yes, please.

JUDGE ANDERSON: I think I understand, but I'm not sure at all and you are supposed to be the expert. I do think when a put is made in an ERISA plan, there is an obligation on the company to buy, and I think it's within 30 days. Is it not true that there is an exception to that if the buy would be a violation of the securities laws?

MR. LISITZA: I mean, yes. We pointed out that provision is -- it's part of ERISA and it's section 306 of [the] Sarbanes-Oxley act. I can give you the long USC code, but I believe it's in our brief and you've stated the position very well. ERISA doesn't put people between a rock and a hard place on this issue. Imagine if there's merger negotiations for a company and the plan [p.52] fiduciaries know or it comes to their attention we're just a Ponzi scheme. We're worthless. At that point to say, well, it's imprudent that ERISA ties their hands and they must allow people to, you know, contribute to this, it just doesn't work that way. The securities laws to the extent there is a conflict or they come to a head, that provision you're pointing out of Sarbanes-Oxley

and the IRS code say when they collide, the federal securities laws are basically a trump. That you cannot -- you're not required to do that.

JUDGE ANDERSON: Okay. That answers that question. Thank you.

MR. LISITZA: Yes.

JUDGE ANDERSON: Is there also an exception of that obligation to buy if to do so would violate a fiduciary duty? My law clerk found that somewhere in the law, and I promise you I can't remember where, but nobody cited it and you're not familiar with that.

MR. LISITZA: I'm not and we do have a limit, you know, as how much we want to be experts on ERISA. I think you would look the Department of Labor said the authorities that [p.53] they cited and I don't know if we need to go so broad as a full fiduciary duty here. It's certainly the duty imposed that it comes from when you have a duty of trust or confidence to abstain or disclose is present and I'm not familiar with that other broader --

JUDGE ANDERSON: Okay. I understand you can't help me on that. Thanks.

MR. LISITZA: Sorry.

JUDGE ANDERSON: Do you have any questions, Judge Moody?

JUDGE MOODY: No.

JUDGE ANDERSON: Do you? All right. Thank you. All right. Mr. Scherker?

MR. SCHERKER: Thank you, your Honor. As to the question as to how many puts were exercised between December 1, 2008 and February 2, 2009 when the window closed, the exhibits we bring the Court's attention to are Plaintiff's Exhibit 199, Plaintiff's Exhibit 777, Plaintiff's Exhibit 778 which reflect a total of 190 puts exercised between December 1, 2008 and February 2, 2009. The duty that the SEC wants the Court to create, a duty that was never tried to the jury in this case and on which the jury [p.54] was never instructed falls apart if it starts with the presumption that the information that has to be disclosed to plan participants is material, and that of course is their position is that this is material information that should be disclosed to plan participants because if it has to be disclosed to plan participants, then it has to be disclosed to all shareholders.

Having made the statement that we made in August 2007, having made the statements that they would have the Court focus on for a period going back to 1840 and the Polk presidency or whatever, if we had a duty to disclose what happened, if we did between November 23, 2008 and January 6, 2009, then we had a duty to all of our shareholders on all five to 600 of the plan participants and there's no way to cabin it. What this Court recognized in ~~Smith~~ [*Smith*], what the Seventh Circuit recognized in ~~Jordan~~ [*Jordan*] is if you're negotiating with a corporate insider, if you're sitting down with essentially your partner because that's what we basically had in those cases, if you're sitting down with your partner who is trying to decide whether or not to retire and is basing that decision on what [p.55] the stock might be worth and you're negotiating a price for the stock, you can say you want

to talk to me, we have to have a confidentiality agreement, otherwise, don't talk to me as opposed to an employee of a competitor who is exercising an irrevocable put, and, Judge Anderson, I'll get to the stuff about fiduciary duty that they're arguing and securities laws. It's a very important part of this case, and I ask the Court's indulgence in letting me get there, but as of right now, you cannot carve out, you cannot carve out a duty to Tim Finnerty and say that's the only duty you have because if it's an ~~omission's~~ [omissions] case and our duty is to speak so as to make a prior statement not misleading, then we have that duty to all of our shareholders, and if a company was foolish enough --

JUDGE ANDERSON: Or at least 190 which would maybe be the same as a public announcement.

MR. SCHERKER: It's one-third of the plan members.

JUDGE ANDERSON: So get to the question of why.

[p.56]

JUDGE MOODY: Or abstain.

JUDGE ANDERSON: Yes. Let's get to the question of why you could not have abstained and I have three: A, because you should have imposed a blackout, which was before the jury. B, abstained because otherwise it would violate the securities laws, and C, [abstained] because otherwise it would violate the fiduciary duty.

MR. SCHERKER: Judge, I would be happy to address that and thank you for the opportunity. There is nothing, repeat, nothing in title 26409H, which is the

Internal Revenue code, not ERISA, that creates the mandatory obligation on the part of a company to honor the put, and if the employer's securities are not readily tradable on an established market, a right to require that the employer repurchase employer securities under a fair evaluation formula. That's 26409H. That requires us to honor the put, and as I said, the other side now agrees and you heard it again this morning that we are required to honor the put. The only circumstance under which you can get out in front, Judge Moody , that is abstained ahead of time because there's no authority to abstain [p.57] once the put is exercised is under 29CFR2520.101, which is cited in our brief and we go to it at great length.

JUDGE ANDERSON: Yes, give me that again.

MR. SCHERKER: Sure, your Honor. It's 29CFR2020.101-3, which is an ERISA regulation. That regulation creates the authority for blackouts, and if I might pause for a moment and note again, we requested the Court which had ruled before trial that blackouts were a legal question and would not allow their expert testimony, referred to it as unworkable and confusing, taking the issue away and when we tried to put on lay testimony ruled that it's a question of law. Yes, one witness testified. One of our witnesses testified. I don't think we have a choice but to honor the put. But when we tried to bring out testimony from the plan administrator, Mr. ~~Patula~~ [Pattullo], that he had to honor puts when they came in the door, the Court ruled that's not a question for lay testimony. That's not a question for lay opinion. I'm going to instruct the jury on it.

When we presented the Court with an instruction drawn precisely from the statute and [p.58] the regulations, the Court refused to give it to the jury. So of course they argued to the jury all they had to do was say no. All they had -- this is at record 555 page 47 through 48. The other way this could have been remedied is don't let Mr. Finnerty trade. Don't let him sell his stock, and yet we never got an instruction to the jury on what the law is on what our obligations are under ERISA.

JUDGE ANDERSON: Now --

MR. SCHERKER: But let's get right to 2520, Judge Anderson, because that's where your question derives from.

JUDGE ANDERSON: Well, what you haven't addressed now -- you've addressed blackout, but you have not addressed why you could not have abstained because it would -- otherwise would violate the securities law, A, and B, fiduciary duty.

MR. SCHERKER: Judge, read this regulation from front to back. There is no abstention. There is no authority under ERISA to abstain.

JUDGE ANDERSON: What about...

MR. SCHERKER: There's authority to impose a blackout. That's the only authority, is a [p.59] blackout.

JUDGE ANDERSON: You say there's nothing in either the statutes or the regulations which makes some exception on the basis of securities laws. I'm talking about the statutory -- I think it's statutory, and you argue in your brief that applies only to some

affirmative statement in the statute itself as opposed to generalized securities laws. That's what I'm aiming at.

MR. SCHERKER: I understand, your Honor, and I'm going to beg your indulgence because we're going to have to start from the beginning on the statute and the regulation. The statute and the regulation allow the imposition of blackouts, which are suspensions by the company. The company can impose a blackout. As a matter of fact, every company that has an ESOP does, for example, when they do the evaluations. They're imposed with regularity.

What they're talking about is an exception to the definition of blackout. It is under exclusions in 29CFR2520.101 and it repeats the statutory language and expands on it. The term, quote unquote, blackout perifod does not include [p.60] a suspension, limitation, or restriction and then it lists a couple of things: One, A, which occurs by reason of the application of the securities laws. That is an exclusion from the definition of a blackout. Now when a blackout is imposed, there are very clear obligations in the statute and the regulation. You have to publicly disclose a blackout, you have to say when it's going to end, and you have to say what the reasons are. In other words, you have to tell the world what you're doing.

JUDGE MOODY: But the exception is you can have a suspension if it's required by the securities laws.

MR. SCHERKER: No, your Honor. This is an exclusion from the definition of blackout period, and the exclusion says suspension, limitation, or restriction which occurs by reason of the applications of the

security laws, and as we point out in our brief, the securities laws, section 12K2, for example, create suspensions, restrictions, or limitations. It happened after 9/11. It happened during the Bear Stearns implosion. The SEC issues an order under 12K2 and says trading is suspended. [p.61] Trading is -- there is no trading in the stock or trading is suspended on the market.

JUDGE ANDERSON: Why should we not interpret that section to say that there could be an abstention, i.e. a blackout, without these notices?

MR. SCHERKER: First of all, that's what the statute has to mean, not that a company can do it. A company can't suspend trading in stock.

JUDGE ANDERSON: I'm asking you a question why we should not hold that a company could do it because it would violate the securities laws for them to buy this stock.

MR. SCHERKER: I understand.

JUDGE ANDERSON: With insider information.

MR. SCHERKER: Here is the scenario that this would create. A company gets an unsolicited call about a potential merger and says great, let's blackout trading while we inside continue to trade. We won't tell them why. We won't give any notice. We won't --

JUDGE ANDERSON: Well, that's clear you can't do that. You can't try -- you certainly cannot trade on inside information.

[p.62]

MR. SCHERKER: Judge, the blackout rules were adopted in Sarbanes-Oxley to prevent the Enron situation where the plan members are frozen out while insiders can trade, but if you carve out a blackout, the kind of suspension that the SEC would have you create, you basically you do one of two things: You either put a button in the CEO's desk that he or she has to hit and say blackout whenever they get any phone call about any possibility of a deal, about an acquisition, about a merger, about any new opportunities, about a new product that they might be able to buy, and you thereby give notice to the world that you're doing something, including notice to your competitor's employees such as Mr. Finnerty where you create massive opportunities for -- to put it in all other ways, corporate mischief because you give unfettered power to corporations to declare a blackout whenever they think something might be happening. You have a carefully structured legislative scheme. You have carefully structured regulatory scheme of notice and reasons and limitations on blackouts and because you want to call it securities laws because they [p.63] want to call it securities laws, you create both unfettered power and massive disclosure because, truth is, a company says out of nowhere, we're blacking out because of the securities laws. Everybody knows something is going on and you've effectively disclosed it.

JUDGE ANDERSON: I think --

MR. SCHERKER: Judge Moody, the answer to your question is abstain is just disclosure under another name.

JUDGE ANDERSON: Thank you very much.

MR. SCHERKER: Thank you, your Honor.

JUDGE ANDERSON: Court will be in recess until tomorrow.

[p.64]

REPORTER'S CERTIFICATE

I, THERESA RUST, Court Reporter, certify that I was authorized to and did stenographically report the foregoing audio and that this transcript, pages 1 through 63, is a true record of the proceedings before the Court.

I further certify that I am not a relative, employee, attorney, or counsel for any of the parties, nor am I a relative or employee of any of the parties' attorney or counsel connected with the action, nor am I financially interested in the action.

Dated this 14th day of January, 2015.

/s/_____
THERESA RUST,
Court Reporter