

June 14, 2011

On June 13, 2011, the United States Supreme Court issued a decision resolving the question of who may be deemed to have made a misrepresentation for purposes of primary liability in a private action under Rule 10b-5 and Section 10(b) of the Securities Exchange Act. In *Janus Capital Group, Inc. v. First Derivative Traders*, No. 09-525 (2011), the Court held that the only person or entity that may be held liable for having "made" a statement within the meaning of Rule 10b-5, is one "with ultimate authority over the statement, including its content and whether and how to communicate it." The Court also emphasized that attribution of a statement to an individual or entity "is strong evidence that a statement was made by—and only by—the party to whom it is attributed."

*Janus* builds off of the *Stoneridge v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 165 (2008) and *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994) decisions which had previously limited who could be held liable in a private action under Rule 10b-5 and Section 10(b) by eliminating scheme liability and liability for aiders and abettors. Together, these decisions appear to have eliminated liability from a private right of action under Rule 10b-5 and Section 10(b) for secondary actors, such as accountants, bankers and lawyers, that provide services to and often review and contribute to issuers' public statements.<sup>1</sup>

## Background

This case involved alleged misrepresentations contained in mutual fund prospectuses. Plaintiffs brought the securities class action against Janus Capital Group, Inc. (JCG), a publicly traded company, and its wholly-owned subsidiary Janus Capital Management LLC (JCM). JCG was the creator of a family of mutual funds. The mutual funds were held by a separate and independent legal entity, the Janus Investment Fund. Janus Investment Fund retained JCM as an investment advisor and administrator. Plaintiffs alleged that JCG and JCM had violated Rule 10b-5 by making false statements concerning market timing policies in mutual fund prospectuses issued by Janus Investment Fund, including statements suggesting that JCM would act to curb market timing in the funds.

The District Court dismissed the plaintiffs' complaint for failure to state a claim. The Fourth Circuit reversed holding that plaintiffs' allegations of JCG and JCM's participation in "writing and disseminating" the Janus mutual fund prospectuses sufficiently pled that JCG and JCM "made" the statements within the meaning of Rule 10b-5. It also held that claims against JCG could only be sustained on a theory of "control person" liability. Thus, the narrow question before the Supreme Court was whether plaintiffs sufficiently alleged that JCM had "made" the statements at issue.

## The Supreme Court's decision

In a 5-4 opinion by Justice Thomas, the Supreme Court adopted a bright line definition of the maker of a statement for purposes of Rule 10b-5: a statement is "made" by the person or entity with the authority to control "the content of the statement and whether and how to communicate it." In reaching this decision, the Court analyzed the term "to make" and concluded that "one 'makes' a statement by stating it." Accordingly, attribution of a statement to a particular individual is strong evidence that the individual made the statement. The Court analogized to a speechwriter and a speaker, stating that while the speechwriter might write the speech it is ultimately the speaker who makes the statement. In reaching this conclusion, the Court rejected the position of the Government, that had submitted an *amicus* brief in support of plaintiffs' position, that the term "make" should be defined as "create" and thus allow plaintiffs to sue entities that participate in the drafting of a false statement issued by a separate entity.

The Court then examined the entities involved in the case to determine who made the statements at issue. The statements at issue were made in Janus Investment Fund's prospectus. Because Janus Investment Fund was a legally independent entity with its own board of trustees, separate and distinct from JCM, the Court concluded that it alone had control over the statements in its mutual fund prospectuses. Further, the prospectuses did not attribute any statements it contained to JCM rather than Janus Investment Fund.

The Court was clear that so long as "the corporate formalities are observed," the Court will not disregard the

corporate form in determining the scope of Rule 10b-5 liability. While the Court was persuaded that investment advisers exercise significant influence over the funds they advise, it declined to expand liability on that basis stating "[a]ny reapportionment of liability in the securities industry in light of the close relationship between the investment advisors and mutual funds is properly the responsibility of Congress and not the Courts."

#### Notes

1 The SEC still has the authority to enforce anti-fraud provisions against secondary actors if they aid and abet a primary violator.

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