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Securities Law Alert

In This Edition:

- Supreme Court: Considers Whether Unnamed Class Members With Tolled and Timely Claims Can Bring a New Class Action After Expiration of the Otherwise Applicable Limitations Period
- Supreme Court: Considers Whether SEC Administrative Law Judges Are Subject to the Appointments Clause
- First Circuit: Failure to Disclose the Details of Adverse Regulatory Guidance Cannot Alone Support an Inference of Scienter Where Defendants Provided Warnings in Broader Terms
- Second Circuit: Aspirational Statements Concerning a Company's Values Are Not Actionable
- Ninth Circuit: Misstatement Claims Under Section 14(e) of the Exchange Act Require Only Proof of Negligence, Not Scienter
- Southern District of New York: Companies Have No Duty to Admit "Uncharged, Unadjudicated Wrongdoing"

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Simpson Thacher is "a go-to for underwriters on a range of high-value matters, with particular strength in connection with the class actions and derivative suits that follow high-profile public offerings."

–*Chambers USA* 2018

Supreme Court: Considers Whether Unnamed Class Members With Tolled and Timely Claims Can Bring a New Class Action After Expiration of the Otherwise Applicable Limitations Period

On March 26, 2018, the Supreme Court heard oral arguments in *China Agritech, Inc. v. Resh*, No. 17-432. At issue is whether an absent class member whose individual claims are timely as a result of the tolling doctrine established in *American Pipe & Construction Co. v. Utah*, 414 U.S. 538 (1974), may file a new class action after the expiration of the otherwise applicable limitations period.

Background

Under existing *American Pipe* Supreme Court doctrine, a pending class action tolls the applicable statute of limitations, allowing absent would-be class members to intervene in a pending case or file new *individual* suits after the denial of class certification when the statute of limitations period would have otherwise expired. The moment class certification is denied or vacated, or the case is dismissed without a class being certified, the statute resumes running as to the previously asserted members of the class and they have whatever time remained to them when the prior class suit was filed within which to pursue an individual claim.

In *Resh v. China Agritech*, 857 F.3d 994 (9th Cir. 2017), the Ninth Circuit held that

the *American Pipe* tolling doctrine permits plaintiffs to bring a new *class* action after the expiration of the statute of limitations if they were unnamed plaintiffs in a timely-filed putative class action, even if class certification was denied in the prior action on substantive grounds and the new action asserts similar class claims.[1] In so holding, the Ninth Circuit joined with the Sixth and Seventh Circuits in finding that the *American Pipe* tolling doctrine applies to subsequent class actions. In contrast, the First, Second, Fifth, and Eleventh Circuits limit the *American Pipe* tolling doctrine to claims by individual plaintiffs. The Third and Eighth Circuits have taken an intermediate position, only allowing subsequent class actions when class certification was denied for reasons that were unrelated to the validity of the class, such as where the denial was based solely on lead plaintiffs' deficiencies as class representatives.

In *China Agritech*, the Court will determine whether the *American Pipe* tolling doctrine extends to subsequent class action suits, permitting so-called "stacking" of successive class actions in order to continue the toll otherwise ended by denial of class certification in a prior class action.

Oral Argument Highlights

The oral argument focused heavily on the traditional requirements of tolling as an equitable remedy, which include that plaintiffs must demonstrate "diligence," meaning that they have taken action to defend their own legal rights, and some extraordinary circumstance. Counsel for China Agritech ("Petitioner") argued that the Court permitted equitable tolling for individual plaintiffs in *American Pipe* because: (1) after the denial of class certification, plaintiffs show the diligence required for tolling when they bring their own individual claims in court; and (2) the enforcement of the statute of limitations would undermine the point of Rule 23 by encouraging plaintiffs to bring duplicative independent claims during a pending class action litigation instead of relying on the class action to represent their interests. Petitioner's counsel argued that neither of those reasons are applicable to the tolling of class action claims because: (1) the absent class action members have not shown the diligence required by equity as they are still absent and are not taking action to protect their individual rights even after class certification is denied; and (2) after the denial of class certification, there is no "extraordinary circumstance," as the concern about plaintiffs filing redundant protective individual claims that detract from the value of a pending class action is no longer relevant.

Chief Justice Roberts questioned Petitioner's counsel on how his approach was consistent with Rule 23, noting that it seemed like he was "creating an exception to the rule. If you just read [Rule 23] on its face, the statute of limitations hasn't run because of *American Pipe* . . . so why shouldn't that rule be available . . . ?"

Justice Kagan acknowledged that she was "a little bit skeptical" of Petitioner's arguments. She noted that the Court reached its decision in *American Pipe* for two reasons: (1) plaintiffs are sufficiently diligent when they rely on a pending class action to represent their interests; and (2) the policies behind Rule 23 indicate that the Court should encourage class actions over individual actions in general. She noted that, in this case, "the exact same thing is true. Diligence is shown in the same way by reliance on the class, and, once again, even after the denial of a single motion for class certification, Rule 23 would indicate that we don't want to have a million individual suits but instead want to encourage a class."

Counsel for William Schoenke, Heroca Holding, and Ninella Beheer ("Respondents") agreed with Justice Kagan, claiming that: (1) class members in this case had shown diligence by relying on the tolling doctrine in *American Pipe*; and (2) the purpose of Rule 23 would be best served by allowing class actions to toll the statute of limitations for

1. Please click here to read our discussion of the Ninth Circuit's decision in *Resh*.

other class action claims because it avoids the potential of having an overabundance of individual claims filed by plaintiffs after the denial of class certification and before the expiration of the statute of limitations. He argued that the "extraordinary circumstance" here is the desire to enforce the principles behind Rule 23 and to "incentivize people not to bring duplicative claims."

Justice Sotomayor pressed the parties on their view of the Third and Eighth Circuits' approach, under which the application of the tolling doctrine depends on the reason for the denial of class certification. Both parties distanced themselves from this rule.

The Justices considered small value claims that would not be worthwhile to bring as individual actions. Justice Kagan observed that the reason for Rule 23 "is that we understand that with respect to some category of claims, we're not going to have them individually or it will be so ridiculous if we have them individually that we would prefer the class action device." Justice Gorsuch commented that "encourag[ing] more protective filings . . . would solve the problem, wouldn't it? We wouldn't have to create these extraordinary rules in extending *American Pipe* in new ways; we'd just create a new incentive structure that would ensure that there are backup class actions available. . . . [W]hat's wrong with that?"

Justice Gorsuch showed concern about the perpetual filing of class actions, asking if plaintiffs could "stack them forever, so that try, try again, and the statute of limitations never really has any force in these cases." Respondents' counsel responded that comity will be a "powerful mechanism" to limit serial motions for class certification.

The Court will issue its decision in *China Agritech* later this term.

Supreme Court: Considers Whether SEC Administrative Law Judges Are Subject to the Appointments Clause

On April 23, 2018, the Supreme Court heard oral arguments in [*Lucia v. SEC*, No. 17-130](). The question before the Court is whether the administrative law judges ("ALJs") for the SEC's in-house courts qualify as either "Officers of the United States" or "inferior officers" subject to the Appointments Clause of the United States Constitution, or employees not subject to the Appointments Clause.

Background

The Appointments Clause states that the President "shall nominate, and by and with the Advice and Consent of the Senate, shall appoint . . . Officers of the United States." U.S. Const. art. II, § 2, cl. 2. The Appointments Clause further provides that "Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments."

In *Raymond J. Lucia Cos. v. SEC*, 832 F.3d 277 (D.C. Cir. 2016), the D.C. Circuit held that SEC ALJs are not "Officers of the United States" or "inferior officers" within the meaning of the Appointments Clause. The court held that the key inquiry for determining the applicability of the Appointments Clause is whether SEC ALJs "issue final decisions" of the SEC. The D.C. Circuit found it significant that the SEC has a discretionary right to review the action of any ALJ as it sees fit.[2]

However, in *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016), the Tenth Circuit relied on the Supreme Court's decision in *Freytag v. Commissioner of Internal Revenue*, 501 U.S. 868 (1991), to hold that SEC ALJs are "inferior officers" who must be appointed in conformity with the Appointments Clause. The Tenth Circuit rejected final decision-making power as the key criterion for assessing whether the Appointments Clause applies. The Tenth Circuit determined that

2. Pursuant to 17 C.F.R. § 201.411, the SEC has the authority to review an ALJ's decision de novo. If no review is sought or ordered, the SEC will issue an order directing enforcement of the ALJ's decision. 17 C.F.R. § 201.360(d). The ALJ's initial decision becomes final only upon issuance of the SEC's order.

"SEC ALJs exercise significant discretion in performing 'important functions' commensurate with" the functions performed by the special trial judges of the federal Tax Court deemed to be "inferior officers" in *Freytag*.

Oral Argument Highlights

Counsel for Raymond J. Lucia and Raymond J. Lucia Companies ("Petitioners") began by arguing that SEC ALJs are "inferior officers" for purposes of the Appointments Clause because they "have been invested with the sovereign power to preside over formal adjudications" and they have "independence in their decisional functions, their hearing functions, and their evidentiary functions." Chief Justice Roberts countered that "any decisions of the ALJs in every case aren't operative until the Commission issues an order of finality." Justice Sotomayor joined in, emphasizing that an SEC ALJ's decision "doesn't become final except by the actions of the SEC officers." She later questioned, "why isn't that the line? Whether the ALJ's word is final or not?"

Justice Kagan questioned whether the problem of the SEC ALJ's alleged bias in the case involving the Petitioner would be solved by "the greater political accountability that comes from the Appointments Clause." She asked, "wouldn't putting those decision-makers even closer to the political body only exacerbate the problem that you're complaining of?" She later observed that "[t]here are different ways to interfere with decisional independence," and one way is to be "the person who gets to decide who gets the job or not." She explained that holding SEC ALJs subject to the Appointments Clause would "in some manner tie the adjudicator more closely to the political system."

Counsel for the SEC ("Respondent"), arguing in support of Petitioners' position,[3] asserted that SEC ALJs "adjudicate disputes that impose liability and sanctions on private individuals, and they can and do issue binding decisions." Counsel for Respondent contended that there is "no meaningful difference between this case and *Freytag*." Justice Breyer stated that he was "fairly certain . . . that the Constitution does not inhibit the creation of . . . an adjudicatorily merit-based system of hearing examiners."

Court-appointed amicus curiae argued, in support of the D.C. Circuit's decision and the SEC's original position, that "an officer of the United States is someone with the power to bind the government or private parties in the name of his own office." He further stated that "someone whose acts have no binding effect without the sanction of an officer is not himself an officer of the United States."

Chief Justice Roberts asked how the case before the Court was different than *Freytag*. Court-appointed amicus curiae explained that the special trial judges in *Freytag* also had contempt power. Justice Kagan took issue with this distinction, and noted that the *Freytag* Court did not even mention the special trial judges' contempt power until the second half of the opinion. She noted that it was "hard to get around" the "commonalities" between SEC ALJs and the tax judges in *Freytag*.

Chief Justice Roberts expressed concern that the process for appointing SEC ALJs "operates as insulation from the political accountability that the drafters of the Constitution intended." He observed that the SEC could disclaim responsibility for the decisions of its ALJs. Court-appointed amicus curiae disagreed, and stated that the SEC "is going to be held 100 percent accountable for every single decision, whether it's initially made by an ALJ or not" because the statutory structure "makes clear that the decision is always the decision of the Commission."

Court-appointed amicus curiae emphasized that the test he proposed "turns on a legal authority to either bind the government, make the government do particular things, or bind private parties." Justice Alito noted that this test is "potentially very broad and also quite vague." He observed that "an enormous number of executive branch officials have the power to bind the government in one way or another."

Justice Kagan found that there was "a good deal to be said" for this proposed test, but she questioned the basis for the proposed test.

3. Under the Obama administration, the federal government took the position that SEC ALJs are only employees, rather than "Officers" or "inferior officers" subject to the Appointments Clause. But in November 2017, the federal government reversed course and took the view that ALJs exercise significant authority and are subject to the Appointments Clause. Counsel for Respondent therefore argued in favor of the position advanced by the Petitioners. The Court appointed counsel to argue in support of the D.C. Circuit's decision and the original position advanced by the SEC.

She noted, "I don't really see what the source of this test is." Court-appointed amicus curiae responded that the test was based in part on the long-established distinction between whether the holder of an office is "authorized to act in the name of their own office" or "only in the name of somebody else's office." He explained that without his test, "every AUSA is going to be considered an officer, even though the U.S. Attorney is going to be held 100 percent accountable for every decision in his or her office."

In response to the arguments advanced by Court-appointed amicus curiae, counsel for Petitioners stated that the "binding authority" test applies only to principal officers, but not to inferior officers. Moreover, he emphasized that the SEC has only a discretionary right to review SEC ALJ decisions that is frequently not exercised.

The Court will issue a decision in the *Lucia* case later this term.

First Circuit: Failure to Disclose the Details of Adverse Regulatory Guidance Cannot Alone Support an Inference of Scienter Where Defendants Provided Warnings in Broader Terms

On April 4, 2018, the First Circuit affirmed dismissal of a securities fraud action alleging that a pharmaceutical company misled investors about the timing of its expedited application for approval of a new pharmaceutical. [*Kader v. Sarepta Therapeutics*, 887 F.3d 48 (1st Cir. 2018) (Torruella, J.)]. The court held that plaintiffs failed to allege scienter because defendants broadly disclosed the FDA's concerns, and there were no particularized facts supporting plaintiffs' allegation that the company was dependent on offerings to fund its operations.

To plead scienter, plaintiffs pointed to the company's alleged failure to disclose the FDA's request that the company obtain an independent review of its pharmaceutical data. The First Circuit found the statements at issue "severely weaken[ed] any inference of scienter" because the CEO both "reminded investors that the FDA was looking for further review" while offering "no assurance that [the company] would accede to the type of review that the FDA sought." The First Circuit explained that "providing warnings to investors, or otherwise disclosing potential risks, erodes inferences of scienter."

The First Circuit further held that it could not "reasonably infer scienter from [the CEO's] failure to elaborate . . . on any difference between a review by the FDA and" an independent review. The court reasoned that "an arguable misrepresentation provides by itself less support for an inference of scienter than does a clear falsehood."

The First Circuit also rejected plaintiffs' effort to plead scienter based on the CEO's failure to disclose that the company was not complying with the FDA's request for independent review. The court observed that the FDA did not inform the company that independent review was "a mandatory prerequisite" for expedited filing. Moreover, the First Circuit emphasized that defendants' failure to "divulge the details of interim 'regulatory back-and-forth' with the FDA . . . alone cannot support an inference of scienter . . . when the defendants do provide warnings in broader terms." The court reasoned that "[t]here must be some room for give and take between a regulated entity and its regulator."

Finally, the First Circuit found meritless plaintiffs' contention that the company was "dependent upon offerings to fund its operations" because it was "in a race for FDA approval" and was "generating no significant revenue." The court explained that it has "set a high bar for arguments of this sort." To plead scienter based on a motive to boost the company's stock price, plaintiffs must allege "something more than the ever-present desire to improve results, such as allegations that the very survival of the company was on the line."

In the case before it, the First Circuit found the complaint "bereft of allegations that [the company] was financially on the ropes, or that it would shutter its doors unless it padded earnings by deceiving investors." The court recognized that the company's initial public offering may have "generated revenue that proved useful to [the company] in its race for FDA approval, so as to secure the first-mover advantage." However, the First Circuit held that this "alone cannot bear the weight of an inference of scienter that is at least as compelling as any other."

Second Circuit: Aspirational Statements Concerning a Company's Values Are Not Actionable

On April 24, 2018, the Second Circuit affirmed dismissal of a securities fraud action alleging misstatements concerning the values of the company's online marketplace.[4] *Altayyar v. Etsy*, 2018 WL 1918519 (2d Cir. 2018) (summary order) (*Altayyar II*). The Second Circuit found "the purported misstatements" were all "vague aspirational statements" that could not give rise to a securities fraud claim.

Plaintiffs sought to recover losses that followed an analyst report indicating that certain of the items sold on the company's online marketplace were either counterfeit or infringed on existing trademarks and copyrights. Plaintiffs claimed that a number of the company's values-related statements misrepresented the company's "trustworthiness." *Altayyar v. Etsy*, 242 F. Supp. 3d 161 (E.D.N.Y. 2017). For example, plaintiffs pointed to statements describing the company as "a mindful, transparent and humane business" with "an authentic, trusted marketplace that embodies [the company's] values-based culture."

The district court found these statements were "precisely the type of puffery that the Second Circuit has held to be non-cognizable." The court reasoned that "[w]ords like 'mindful,' 'humane,' 'genuine,' and 'authentic' are not quantifiable or factual; they are subject to interpretation, within reason, and are statements of opinion." The court explained that "'a sincere statement of pure opinion is not an untrue statement of material fact, regardless whether an investor can ultimately prove the belief wrong.'" *Id.* (quoting *Omnicare v. Laborers Dist. Council Const. Indus. Pension Fund*, 135 S. Ct. 1318 (2015)). The district court determined that even if "plaintiffs' allegations might show that [the company's] compliance practices were imperfect," plaintiffs did not "establish that the challenged values statements were objectively false or disbelieved when [the company] made them."

On appeal, the Second Circuit found the district court "correctly dismissed" plaintiffs' claims for failure to "allege actionable misstatements or omissions." *Altayyar II*, 2018 WL 1918519.

4. Simpson Thacher represents the underwriters of Etsy's initial public offering in this matter.

Ninth Circuit: Misstatement Claims Under Section 14(e) of the Exchange Act Require Only Proof of Negligence, Not Scienter

On March 30, 2018, the Ninth Circuit held that the first clause of Rule 14(e), which prohibits material misstatements in connection with tender offers, requires only proof of negligence, rather than scienter.[5] *Varjabedian v. Emulex Corp.*, 2018 WL 1882905 (9th Cir. 2018) (Marguia, J.). Five other circuits to consider this question have relied on similarities between the first clause of Rule 14(e) and Rule 10b-5(b)[6] to hold that a scienter requirement applies to Rule 14(e) claims. The Ninth Circuit departed from these decisions based on its determination that "important distinctions exist between Rule 10b-5 and Section 14(e)" that "strongly militate against importing the scienter requirement from the context of Rule 10b-5 to Section 14(e)."

The prevailing view that the first clause of Section 14(e) requires proof of scienter dates back to the Second Circuit's decision in *Chris-Craft Industries v. Piper Aircraft Corp.*, 480 F.2d 341 (2d Cir. 1973), in which the court stated that it would "follow the principles developed under Rule 10b-5 regarding the elements of [Section 14(e)]

5. Rule 14(e), titled *Untrue statement of material fact or omission of fact with respect to tender offer*, provides:

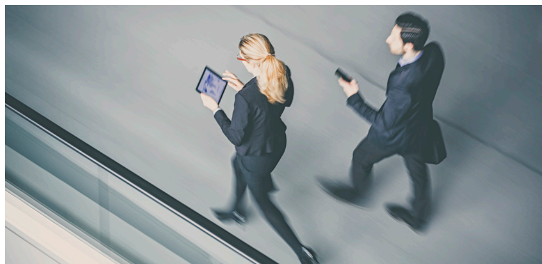
> It shall be unlawful for any person to make any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation.

15 U.S.C. §78n(e). Rule 14(e) was added as an amendment to the Securities Exchange Act of 1934 pursuant to the Williams Act.

6. Rule 10b-5(b), titled *Employment of manipulative and deceptive devices*, provides in relevant part:

> It shall be unlawful for any person, directly or indirectly . . . [t]o make any untrue statement of a material fact or 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 . . . in connection with the purchase or sale of any security.

violations." A year later, the Fifth Circuit agreed with the Second Circuit and held that the first clause of Rule 14(e), like Rule 10b-5, requires proof of scienter. *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579 (5th Cir. 1974). Three other circuits have since reached the same conclusion.[7]



The Ninth Circuit disagreed with *Chris-Craft* and *Smallwood*, and the rulings of other circuits following those decisions, for several reasons. First, the Ninth Circuit explained that Rule 10b-5(b)'s scienter requirement is based not on the text of the rule itself but on the language of Section 10(b), pursuant to which Rule 10b-5 was promulgated. The Ninth Circuit noted that in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976), the Supreme Court "acknowledged that the wording of Rule 10b-5(b) could reasonably be read as imposing a scienter *or a negligence* standard." *Varjabedian*, 2018 WL 1882905. However, as the Ninth Circuit explained, the *Ernst & Ernst* Court ultimately concluded that Rule 10b-5(b) "requires a showing of scienter because it is a regulation promulgated under Section 10(b) of the Exchange Act, which allows the SEC to regulate *only* 'manipulative or deceptive device[s].'" The Ninth Circuit found "[t]his rationale regarding Rule 10b-5 does not apply to Section 14(e), which is a statute, not an SEC Rule."

The Ninth Circuit also explained that "Section 14(e) differs fundamentally from Section 10(b)" because the SEC may regulate non-fraudulent conduct under Section 14(e). The Ninth Circuit observed that "[i]f the SEC can prohibit acts themselves not fraudulent under Section 14(e), then it would be somewhat inconsistent to conclude that Section 14(e) itself reaches only fraudulent conduct requiring scienter."

7. *See In re Digital Island Sec. Litig.*, 357 F.3d 322 (3d Cir. 2004); *SEC v. Ginsburg*, 362 F.3d 1292 (11th Cir. 2004); *Adams v. Standard Knitting Mills,* 623 F.2d 422 (6th Cir. 1980).

Second, the Ninth Circuit found it significant that in *Aaron v. SEC*, 446 U.S. 680 (1980), the Supreme Court held that Section 17(a)(2) of the Securities Act of 1933—which is nearly identical to the first clause of Rule 14(e)—does not require a showing of scienter.[8] The Ninth Circuit noted that the two provisions both "govern disclosures and statements made in connection with an offer of securities, albeit in different contexts: Section 17(a) applies to initial public offerings while Section 14(e) applies to tender offers." The Ninth Circuit explained that "statutes dealing with similar subjects should be interpreted harmoniously."

Finally, the Ninth Circuit found that the legislative history of the Williams Act, pursuant to which Section 14(e) was enacted, also "supports a negligence standard." The court explained that "[t]he legislative history suggests that the Williams Act places more emphasis on the quality of information shareholders receive in a tender offer than on the state of mind harbored by those issuing a tender offer."

The Ninth Circuit concluded that "because the text of the first clause of Section 14(e) is devoid of any suggestion that scienter is required, . . . the first clause of Section 14(e) requires a showing of only negligence, not scienter."

Southern District of New York: Companies Have No Duty to Admit "Uncharged, Unadjudicated Wrongdoing"

On March 30, 2018, the Southern District of New York dismissed with prejudice a securities fraud action brought against an aerospace conglomerate following disclosures of SEC and DOJ investigations into potential Foreign Corrupt Practices Act ("FCPA") violations that predated the class period. *Emps. Ret. Sys. of the City of Providence v. Embraer S.A.*, 2018 WL 1725574 (S.D.N.Y. 2018) (Berman, J.). The court held defendants were under no obligation to admit that the

8. Section 17(a)(2) provides in relevant part:

> It shall be unlawful for any person in the offer or sale of any securities . . . to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

15 U.S.C. § 77q(a)(2).

company had violated the FCPA before the company had been charged and while the investigations were ongoing. The court emphasized that "companies do not have a duty to disclose uncharged, unadjudicated wrongdoing."

Disclosure of Pending Investigations and Their Potential Adverse Consequences Is Sufficient to Satisfy the Securities Laws

The *Embraer* court held the company had "complied with its disclosure obligations" by informing investors of pending SEC and DOJ investigations, as well as the possible penalties and fines that could result. The court rejected plaintiffs' contention that the company was "duty bound to alert investors to the certainty of the fraud" itself. The *Embraer* court underscored that "disclosure is not a rite of confession."

The court explained that in *City of Pontiac Policemen's and Firemen's Retirement System. v. UBS AG*, 752 F.3d 173 (2d Cir. 2014), the Second Circuit found that an investment bank had satisfied its disclosure requirements under the securities laws by revealing that the bank was under investigation and could face significant adverse consequences. The Second Circuit rejected plaintiffs' contention that "defendants were required to disclose that [the bank] was, in fact, [allegedly] engaged in an ongoing . . . scheme." *City of Pontiac*, 752 F.3d 173.

The *Embraer* court also found persuasive the court's recent decision in *In re Banco Bradesco S.A. Securities Litigation*, 277 F. Supp. 3d 600 (S.D.N.Y. 2017). There, the court held that a company had no obligation to inform investors that it was allegedly "engaged in an unlawful bribery scheme" where it had disclosed both the existence of legal and administrative proceedings concerning that alleged scheme, as well as the potential impact of those proceedings on the company's finances and reputation.

Plaintiffs Cannot State a Securities Fraud Claim Based on the Disclosure of Accurate Financial Data

The *Embraer* court found meritless plaintiffs' contention that the company was "obligated to disclose that some unstated portion of its sales or income was derived from contracts related to the FCPA violations." The court explained that "the allegation that a corporation properly reported income that is alleged to have been, in part, improperly obtained is insufficient to impose Section 10(b) liability." 2018 WL 1725574 (quoting *In re Sanofi Sec. Litig.*, 155 F. Supp. 3d 386 (S.D.N.Y. 2016)).

Because plaintiffs did "not dispute that [the company's] financial statements were (literally) accurate," the court held that the "the statements or omissions concerning [the company's] financial statements are not actionable." The court stated that "a violation of federal securities laws cannot be premised upon a company's disclosure of accurate historical data." *Id.* (quoting *Sanofi*, 155 F. Supp. 3d 386).

A Code of Ethics Cannot Give Rise to a Securities Fraud Claim

The court further held that plaintiffs could not state a claim based on the company's alleged failure to comply with its code of ethics, which the court found "inherently aspirational." The court noted that "it cannot be that every time a violation of that code occurs, [the company] will be liable under federal [securities] laws."

Plaintiffs Failed to Allege the Company's Opinion Concerning Reserves Was Not Sincerely Held

Plaintiffs also challenged the company's opinion, based on advice of counsel, that there was "no basis for estimating reserves or quantifying any possible contingency" in connection with the DOJ and SEC investigations of the alleged FCPA violations. In plaintiffs' view, the company could have quantified reserves by reference to the scope of the alleged bribery scheme.

The *Embraer* court held that plaintiffs could not state a claim merely by alleging that the company's opinion was wrong. Here, plaintiffs did "not plead that this statement was (insincerely) not truthful or that management (and its outside counsel) did not believe what they were stating publicly." Plaintiffs simply "disagree[d] with the opinion." The court explained that "'[t]he securities laws do not allow investors to second-guess inherently subjective and

uncertain assessments.'" *Id.* (quoting *In re Weight Watchers Int'l Sec. Litig.*, 2016 WL 2757760 (S.D.N.Y. May 11, 2016)).

Plaintiffs' Internal Control Claims Were Deficient in Light of the "Temporal Disconnect" Between the Alleged FCPA Violations and the Class Period

Finally, the *Embraer* court found plaintiffs' claims concerning the adequacy of the company's internal controls insufficiently particularized to survive a motion to dismiss. The court explained that a plaintiff asserting an internal control-based securities fraud claim must "allege specific facts concerning the purportedly deficient internal controls, including how they were deficient, when and why."

Here, the court found plaintiffs pled only generalized allegations concerning the company's internal controls and then attempted to link those allegations to current employees' knowledge of, or participation in, alleged FCPA violations that occurred *before* the commencement of the class period. The court agreed with defendants that there was a "'temporal disconnect' between bribery events [that] occurred well before the [c]lass period and [the] alleged faulty internal controls."

The *Embraer* court distinguished *In re Petrobras Sec. Litig.*, 116 F. Supp. 3d 368 (S.D.N.Y. 2015), in which the court "apparently did not require the plaintiffs to present more detailed information about the defendant's internal controls." *Id.* The *Embraer* court explained that in *Petrobras*, "both the statements and the alleged corruption occurred during the class period." Here, however, the alleged bribery scheme "occurred five years prior to the [c]lass [p]eriod." The *Embraer* court found plaintiffs' allegations "temporally and logically insufficient" to give rise to an internal controls-based claim.

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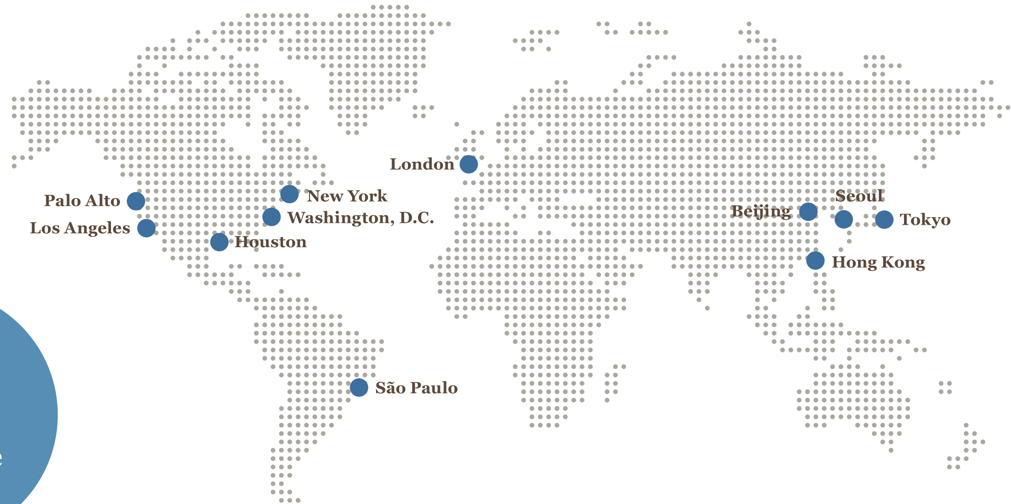

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