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P R O C E E D I N G S

(11:00 a.m.)

CHIEF JUSTICE ROBERTS: We'll hear argument next in Case 06-43, Stoneridge Investment Partners v. Scientific-Atlanta et al.

Mr. Grossman.

ORAL ARGUMENT OF STANLEY GROSSMAN
ON BEHALF OF THE PETITIONER

MR. GROSSMAN: Thank you, Mr. Chief Justice, and may it please the Court:

The text of Section 10(b) as well as the Rule 10b-5 promulgated by the Securities and Exchange Commission prohibit the use of any deceptive device by any person, indirectly or indirectly, in connection with the purchase or sale of a security. The various deceptive devices used by the Respondents in this case is conduct that is squarely covered by the text of the statute and by the rule.

Respondents here were not passive bystanders facilitating a fraud by Charter. Their deceptive conduct was integral to the scheme to create fictitious advertising revenues for Charter to report to investors.

Respondents agreed to overcharge Charter so that they could receive the money from Charter to then return to it for the advertising, using Charter's very

1 same money for the purchase of the advertising.
2 Respondent Scientific-Atlantic created a document
3 falsely claiming that the reason for the increased
4 payments from Charter were because of increased
5 manufacturing expenses.

6 JUSTICE KENNEDY: The transaction was not
7 wholly without benefit to Scientific-Atlantic. They got
8 some advertising. And it was not wholly without benefit
9 to Charter. They were able to show that advertising
10 works. Now, that puts aside the fact that they were
11 using misleading accounting principles.

12 MR. GROSSMAN: Well, I would agree, Your
13 Honor, that they received free advertising. But the
14 problem was that they were creating the illusion that it
15 wasn't free advertising, but rather that they were
16 purchasing the advertising.

17 JUSTICE GINSBURG: And was the price four to
18 five times higher than the normal rates for advertising?

19 MR. GROSSMAN: That is correct, Justice
20 Ginsburg.

21 And the obvious purpose for creating the
22 illusion that they were purchasing the advertising
23 rather than receiving free advertising was so that
24 Charter can incorporate these increased revenues in
25 their financial statements. And Respondents understood,

1 they understood that in order to, for Charter to pass
2 this by their accountants, to deceive the accountants --
3 and this is reflected in the indictment -- in order to
4 deceive the accountants for Charter, the Respondents
5 were told that there had to be separate agreements for
6 both the advertising agreements and the purchase
7 agreements.

8 JUSTICE SCALIA: Mr. Grossman, is there any
9 reason why, in principle, the elements for a cause of
10 action under 10b-5 have to be the same as the elements
11 for a cause of action by the agency under 10b? I mean,
12 we, we created this, this cause of action. It's not set
13 forth in the statute, although other private causes of
14 action are.

15 If it's our creation, couldn't we sensibly
16 limit it so that, for example, schemes can be attacked
17 by the SEC, but schemes do not form the basis for
18 private attorney general's actions? You need actual
19 conveyance of a misrepresentation to the injured party.
20 Is there any reason why we couldn't do that?

21 MR. GROSSMAN: Well, I think there are two
22 reasons, Your Honor. The first is that at this point in
23 time -- I think as the Court recognizes in *Dura* fairly
24 recently, that when Congress enacted the Private
25 Security Law Reform Act, that at that time they accepted

1 the private right of action that this Court had
2 previously inferred. And this Court had previously
3 inferred the private right of action not only for the
4 section but each of the rules in Section 10(b).

5 CHIEF JUSTICE ROBERTS: But it's not like
6 under the Sherman Act, where we have reason to think
7 Congress intended the Court to go about the business of
8 construing and developing antitrust law. In fact, they
9 are kind of taken over for us. They are imposing
10 certain limits on when actions can be brought, proposing
11 specific elements. In one of the provision, 20(e),
12 specifying SEC can bring an action but private investors
13 can't.

14 I mean, we don't get in this business of
15 implying private rights of action any more. And isn't
16 the effort by Congress to legislate a good signal that
17 they have kind of picked up the ball and they are
18 running with it and we shouldn't?

19 MR. GROSSMAN: Well, this Court, Your Honor,
20 as recently as 2002 in Wharf (Holdings) said there is a
21 private right of action for violation of any of the
22 subdivisions of Rule 10b-5: A, B, or C. That would
23 have to be reversed.

24 Going back to the Superintendent of
25 Insurance case in, in -- that would be in 1971, Your

1 Honor, the Court held there was a private right of
2 action for violation of --

3 CHIEF JUSTICE ROBERTS: Well, that's kind of
4 my point. We did that sort of thing in 1971. We
5 haven't done it for quite sometime.

6 MR. GROSSMAN: Well, when Congress enacted
7 the Private Security Law Reform Act, everything it did
8 in connection with that statute was directed to the
9 private right of action that this Court had previously
10 implied under 10(b). Nothing that Congress did was
11 intended in any way --

12 CHIEF JUSTICE ROBERTS: I'm not -- my
13 suggestion is not that we should go back and say that
14 there is no private right of action. My suggestion is
15 that we should get out of the business of expanding it,
16 because Congress has taken over and is legislating in
17 the area in the way they weren't back when we implied
18 the right of action under 10(b).

19 MR. GROSSMAN: I would agree, Congress has
20 taken over. When they enacted the Private Security Law
21 Reform Act, they recognized this private right of
22 action. Everything they did recognized the private
23 right of action. It recognized that there would be
24 multiple primary violators of 10(b). It did that in
25 connection with proportionate liability provisions. It

1 recognized that there would be multiple players.

2 So certainly, Congress had an understanding
3 of what this Court had done up until that time. And
4 this Court up until that time had implied the private
5 right of action for every subset of Rule 10b-5.

6 CHIEF JUSTICE ROBERTS: Is it -- is it a
7 necessary part of your theory that the deceptive
8 practice that Scientific-Atlantic went in, that they
9 knew that that was also -- that Charter would carry that
10 forward? I mean, let's suppose that there were benefits
11 to this deceptive practice to Scientific-Atlantic, that
12 it looked like it had more money to spend on advertising
13 than it really did, but they didn't care what Charter
14 did with it. In fact, they didn't know that Charter was
15 going to carry it on its books the way they did. Would
16 there still be liability for Scientific-Atlantic?

17 MR. GROSSMAN: No. No, not under the test
18 that we have proposed, which is very similar to the test
19 proposed by the Ninth Circuit or applied in the Ninth
20 Circuit in the Simpson case, and the test proposed by
21 the Securities and Exchange Commission in their amicus
22 brief submitted in the Simpson case. It's not enough
23 just to have the deceptive act. The deceptive act for
24 scheme liability has to be with the purpose of
25 furthering a scheme to defraud its investors.

1 So if Scientific-Atlanta or Motorola had
2 engaged in deceptive conduct, but that deceptive conduct
3 was not intended to further a scheme to defraud the
4 shareholders, no, Your Honor, there would be no action
5 under the theory that we are pursuing here.

6 JUSTICE SCALIA: Intended or known? I mean,
7 I don't see -- what's in it for Scientific-Atlantic to
8 defraud the shareholders? Is it enough that they just
9 knew it would be used for that purpose?

10 MR. GROSSMAN: Oh, it would be enough if
11 they committed a deceptive act and they knew it was in
12 furtherance of a scheme.

13 JUSTICE SCALIA: Well, when you say "in
14 furtherance of," you -- you import intent. They didn't
15 care what Charter was going to do with it, but they
16 pretty well knew that what Charter was going to do was
17 to make its books look better.

18 Would that be enough?

19 MR. GROSSMAN: I think that would be
20 reckless.

21 JUSTICE SCALIA: That's what I thought your
22 position was.

23 MR. GROSSMAN: Yes, but my position is also
24 --

25 JUSTICE SCALIA: Not an intent necessarily.

1 It's just knowledge.

2 MR. GROSSMAN: You certainly needs scienter.
3 You certainly need scienter.

4 JUSTICE SOUTER: It's more than knowledge.
5 You mentioned recklessness. It's got to have either
6 knowledge of or a willingness to maintain indifference
7 to the consequence.

8 MR. GROSSMAN: Exactly right, Justice
9 Souter. And I think it's important -- and there is,
10 there is a very good discussion of this in the Simpson
11 case by the Ninth Circuit, that the purpose of the test
12 is such that it will not ensnare someone who does engage
13 in a deceptive act but doesn't understand that the
14 reason for it is to further a scheme.

15 JUSTICE SCALIA: Sure. After trial -- you
16 know, after trial which causes your stock to tank, you
17 may indeed be able to show that you didn't know it was
18 going to be used for that purpose. I mean, that's what
19 this is all about, isn't it, getting it -- getting it by
20 the summary judgment stage?

21 MR. GROSSMAN: No. I think, Your Honor,
22 that this Court answered this last term in the Tellabs
23 case. And Congress answered that question that you pose
24 in the PSLRA, the Private Security Law Reform Act, so
25 that you cannot just bring a case and hope to get it by

1 the summary judgment stage. You have to have
2 particularized facts alleged under the heightened
3 pleading standards of the PSLRA and this Court's
4 decision in Tellabs showing that not only the deceptive
5 act, but that the purpose of that deceptive act was to
6 further a scheme. So, no, you can't~--

7 JUSTICE SCALIA: What facts -- what has to
8 be alleged short of -- on information and belief the
9 Defendant knew that -- that this information would
10 appear on the balance sheets and be used to improve the
11 status of the stock?

12 MR. GROSSMAN: Well, of course if you just
13 -- if you just allege it on information and belief,
14 you're out of court. No doubt about that. That doesn't
15 pass the heightened pleading standard in Tellabs and the
16 PSLRA. What you do need is what we have here. Here you
17 have allegations -- and we didn't make these allegations
18 from whole court -- these allegations were derived
19 principally from the grand jury -- the Federal grand
20 jury indictment against Charter executives. That
21 indictment says that Respondents were informed and
22 ordered to deceive Charter's accountants. They had to
23 have --

24 CHIEF JUSTICE ROBERTS: Why shouldn't we be
25 guided by what Congress did in the action to the Central

1 Bank case? There we said there's no aiding and abetting
2 liability, Congress amended the statute in 20(e) to say
3 yes, there is, but private plaintiffs can't sue on that
4 basis. Why shouldn't that inform how we further develop
5 the private action under 10b-5?

6 MR. GROSSMAN: Well, I think if Congress
7 intended under 20(e) -- certainly the private action is
8 similar to this -- it would have said that only the SEC
9 has the authority to bring a claim for substantial
10 assistance whether or not it involves deceptive conduct.
11 They could have very easily said any deceptive conduct,
12 and that would have barred these claims. They chose not
13 to do that.

14 CHIEF JUSTICE ROBERTS: But they were --
15 they were addressing a very specific decision from this
16 Court, the Central Bank decision. And the one thing
17 they did not do was say that that decision was wrong
18 with respect to private -- or going forward they weren't
19 going to overrule that decision with respect to private
20 rights of action. You're asking us to extend to non --
21 I know you call it a primary violator, but not the
22 person who --

23 MR. GROSSMAN: Secondary actors.

24 CHIEF JUSTICE ROBERTS: -- who put the
25 deceptive conduct into the market. You're asking us to

1 extend that liability to, them which seems inconsistent
2 with Congress' approach in 20(e).

3 MR. GROSSMAN: We are not asking any
4 extension. Quite the contrary, Your Honor. I think
5 that's the Respondents who are asking for narrowing.
6 When Congress addressed the PSLRA it addressed all of
7 the arguments that we are hearing today from Respondents
8 and their amici.

9 JUSTICE ALITO: Is your theory dependent on
10 the proposition that Scientific-Atlanta and Motorola
11 deceived Arthur Andersen?

12 MR. GROSSMAN: That certainly is a large
13 part of it. Yes, Your Honor.

14 JUSTICE ALITO: But didn't you allege
15 exactly the opposite in your complaint?

16 MR. GROSSMAN: No. We -- I think what
17 you're referring to is that -- is that the accountants
18 should have conducted a more diligent audit than they
19 did. I mean these people clearly were trying to deceive
20 the auditors. Why else would you wish you would
21 document falsely stating a reason for a price increase?

22 JUSTICE ALITO: Well, I'm looking at
23 paragraph 218 of your amended complaint, 109 (a) of the
24 joint appendix, subsection 4. It says, speaking of
25 Arthur Andersen, "though aware that Charter was seeking

1 to boost its revenues by paying vendors higher prices at
2 the same time it received additional advertising from
3 the same vendors, Andersen failed to properly audit
4 these transactions by confirming them with the vendors."
5 You alleged that they weren't deceived. You alleged
6 that they knew exactly what was going on.

7 MR. GROSSMAN: No -- no, Your Honor, they
8 knew that they were paying the vendors higher prices,
9 but they didn't know why. The contract -- the contract
10 for the higher prices was followed by this misstatement
11 saying the reason for the higher prices is because of
12 increased manufacturing expenses, when in fact that
13 wasn't the reason. The reason was to take money --

14 JUSTICE GINSBURG: Who told -- who told
15 Charter that it was necessary for them to have a time
16 spread between the contract -- the \$20 above the
17 contract price and the advertising payment?

18 MR. GROSSMAN: Arthur Andersen.

19 JUSTICE GINSBURG: Well, if it told them
20 that, didn't it have -- it sounds to me from that if the
21 accountant says, look, if you want to make this appear
22 on the balance sheet as though the advertising revenues
23 were just ordinary advertising revenues, you better
24 separate these two. I suggest that Arthur Andersen knew
25 all along what was going on.

1 MR. GROSSMAN: No. Justice Ginsburg, what
2 Arthur Andersen did not know -- and this is very clear.
3 They did not know that it was Charter's own money that
4 was being used by the Respondent to purchase the
5 advertising. They were deceived by that document that
6 said, we are increasing the price on the set-top boxes
7 because of increased manufacturing expense. That was
8 false. The reason they were increasing it is because
9 Charter was delivering the money to them.

10 JUSTICE SCALIA: But that's exactly the
11 thing they told them to separate.

12 MR. GROSSMAN: Well, not for that reason,
13 Your Honor.

14 JUSTICE SCALIA: What other reason?

15 MR. GROSSMAN: The reason is as follows.
16 This is what they refer to as barter contracts, two
17 companies exchanging things, which is perfectly
18 legitimate, nothing wrong with that. And there are
19 certain ways to account for it properly, and what Arthur
20 Andersen was telling Charter was in order to be able to
21 have revenues included, gross revenues, you have to have
22 unrelated -- unrelated contracts. They couldn't be a
23 barter transaction. But there is no way -- no way that
24 you could recognize the advertising revenues if you're
25 using Charter's own money, and that's what Arthur

1 Andersen did not do. It would be no different, Justice
2 Scalia, if Charter delivered a suitcase filled with cash
3 and gave it to them and said okay, buy the advertising
4 from us.

5 JUSTICE SCALIA: I understand what you're
6 saying. It seems to me that when you say that they
7 can't be connected, you're saying precisely, you can't
8 be bartering the advertising revenue for the increased
9 money that you're paying.

10 MR. GROSSMAN: No. You can barter. You can
11 barter, it's just a question of how you account for it.
12 But the bartering is one thing. I mean, that's one
13 accounting principle relating to bartering, but there is
14 no accounting principle that permits the recording of
15 revenue if you're using the money from the seller. And
16 that's why they discussed --

17 JUSTICE ALITO: All right, just to be clear
18 on this -- just to be clear on this -- if Charter and
19 Arthur Andersen and Scientific-Atlanta and Motorola all
20 sat down and cooked up this scheme together and they all
21 knew exactly what was going on, would you have a claim
22 against the Respondents here?

23 MR. GROSSMAN: Yes. And the reason for
24 that, Your Honor, is because the advertising contract
25 was a sham, and the advertising contract was a sham

1 because Charter was giving the Respondents money to buy
2 the advertising.

3 JUSTICE ALITO: Then I see absolutely no
4 difference between your test and the elements of aiding
5 and abetting.

6 MR. GROSSMAN: The difference is conceptual.

7 JUSTICE ALITO: Because you said it's not
8 necessary for there to be an actual deceptive act on the
9 part of the Respondents.

10 MR. GROSSMAN: There has to be a deception
11 -- there is deception. The deception is you're entering
12 into an advertising contract that presents the illusion
13 that you were purchasing advertising, when in fact you
14 were not purchasing advertising.

15 CHIEF JUSTICE ROBERTS: But that's -- but
16 that's not the fraud that was imposed upon the market.
17 The fraud imposed upon the market was Charter's
18 accounting for the transaction on its books. Nobody
19 bought or sold stocks in the reliance upon the way that
20 Scientific-Atlanta and Charter structured their deal.
21 They did so in reliance upon the way Charter
22 communicated its accounting to the marketplace.

23 MR. GROSSMAN: There was no way -- no way
24 that that could properly be accounted for, and the
25 Respondents understood that. And that's why they did

1 what they did, that's what --

2 JUSTICE KENNEDY: But there are -- there are
3 any number of kickbacks and mismanagements and petty
4 frauds that go on in the business, and business people
5 know that any publicly held company's shares are going
6 to be affected by its profits, so I see no limitation to
7 your -- to your proposal for validly.

8 MR. GROSSMAN: Well, I think the limitations
9 are as follows, Your Honor. Number one, there has to be
10 the purpose of furthering a scheme to defraud
11 shareholders. Number two, the test has an element of
12 materiality, that it cannot be --

13 JUSTICE KENNEDY: Well, I agree with Justice
14 Scalia's earlier comment, I don't think that
15 Scientific-Atlanta or Motorola really cared anything of
16 -- one way or the other about the investors. For them
17 the scheme made a certain amount of sense, they didn't
18 really care.

19 MR. GROSSMAN: They may not have cared, but
20 that would be reckless because they certainly understood
21 --

22 JUSTICE KENNEDY: But that's far different
23 from having a purpose. You said they have to have a
24 purpose.

25 MR. GROSSMAN: That's correct. If you just

1 close your eyes -- if somebody comes to you and says,
2 look, we want you to enter into this transaction, it's a
3 phony transaction and we don't care -- do whatever you
4 want with that, and they know it's a publicly held
5 corporation and they have every reason to understand
6 that this information --

7 JUSTICE KENNEDY: Which goes back to my
8 earlier question -- that most people that engage in
9 frauds on business know that if it's a publicly held
10 corporation, it's going to hurt the price of the shares
11 or affect the price of the shares.

12 MR. GROSSMAN: Well, they shouldn't engage
13 in schemes to defraud, that's what Congress intended by
14 Section 10.

15 JUSTICE SOUTER: But as I understand your
16 argument, it is the difference between the aiding and
17 abetting liability on the part of the Respondents and
18 liability is, in effect, as first line principles, is
19 their intent, or at the very least in knowledge that
20 they were committing a deceptive act as part of this
21 scheme. Is that correct?

22 MR. GROSSMAN: That they have to commit the
23 deceptive act --

24 JUSTICE SOUTER: Yes.

25 MR. GROSSMAN: That's correct.

1 JUSTICE SOUTER: Now, how many times are
2 parties in the position of Respondents ever going to
3 engage in those acts except with exactly the state of
4 mind that on your judgment makes them principals, rather
5 than aiders and abettors.

6 MR. GROSSMAN: It is not on my judgment. It
7 has to be pled with the particularity required by the
8 PSLRA.

9 JUSTICE SOUTER: No. No, I realize that you
10 have to plead it. What I'm getting at is: Are you
11 making a distinction that in the real world is not a
12 distinction? That, in reality, no one is going to do
13 what these Respondents did without the kind of knowledge
14 or intent that makes them, on your theory, principals
15 rather than aiders or abettors?

16 MR. GROSSMAN: There are cases, I think,
17 Your Honor, where they can engage in deceptive conduct,
18 and there would not be the purpose to defraud
19 shareholders. For instance, Charter may have come to
20 them and said look, do me a favor, says the sales
21 manager. I want to make my numbers for this period so I
22 can take my wife on a trip to Hawaii that the company
23 will give me.

24 So the company gives him a phony order,
25 thinking that's the purpose of it. That's the purpose

1 of this phony order to help this guy along.

2 Well, you've engaged in a deceptive act. It
3 may be deceptive under 10(b), but you wouldn't satisfy
4 the "purpose" test, because the purpose --

5 JUSTICE SOUTER: In other words, it's
6 deceptive but not deceptive in relation to, or for the
7 purpose of, deceiving the -- the petitioner.

8 MR. GROSSMAN: Right.

9 JUSTICE SCALIA: But don't aiders and
10 abettors have to have that purpose as well? What
11 distinguishes -- what distinguishes the liability that
12 you propose from aider and abettor liability?

13 MR. GROSSMAN: You have to engage in a
14 deceptive act under 10(b). 10(b) prohibits any deceptive
15 act.

16 JUSTICE SOUTER: I thought you were telling
17 me that in each case there may be a deceptive act but
18 not a deceptive act in relation to somebody like the
19 Petitioner here.

20 MR. GROSSMAN: Exactly.

21 JUSTICE SOUTER: But that's a different
22 answer, I think, from the one you were just giving
23 Justice Scalia.

24 MR. GROSSMAN: No. I -- I understood,
25 perhaps mistakenly, from Justice Scalia that there

1 wasn't a deceptive act in your hypothetical. If there
2 is a deceptive act, then it's prohibited by 10(b), and
3 we move to the next statute --

4 JUSTICE SCALIA: So any aiding and abetting
5 through a deceptive act makes you a principal? Is that
6 it? You can't be an aider and abetter by committing or
7 enabling a deceptive act without becoming a principal.

8 MR. GROSSMAN: No. Not At all.

9 JUSTICE SCALIA: You cannot --

10 MR. GROSSMAN: You, yourself -- you,
11 yourself, have to engage in the deceptive act.

12 JUSTICE SCALIA: Yes.

13 MR. GROSSMAN: Your own deceptive act.

14 JUSTICE SCALIA: Yes, but -- but if you do,
15 or if you should have known, you are not an aider and
16 abetter. You are automatically a principal.

17 MR. GROSSMAN: You may be a principal if you
18 satisfy the other elements of our test, which are
19 serious elements that you have to plead with
20 particularity, with the heightened pleading standards,
21 that they have the purpose to further a scheme to
22 defraud. That's very different --

23 JUSTICE SCALIA: Is it fair to say that all
24 aiders and abettors who commit deceptive acts are
25 principals?

1 MR. GROSSMAN: No.

2 JUSTICE SCALIA: What's the difference?
3 What separates the two?

4 MR. GROSSMAN: You have to take it the next
5 step further, whether or not that deceptive act had the
6 purpose and effect for furthering a scheme of an
7 investor.

8 JUSTICE SCALIA: Don't you need that to be
9 an aider or abetter?

10 MR. GROSSMAN: An aider and abetter? You
11 have to have --

12 JUSTICE SCALIA: What if -- if I'm entirely
13 innocent, and I don't --

14 MR. GROSSMAN: An aider -- certainly --
15 certainly, the primary violator in the situation that we
16 are discussing where there are deceptive acts is aiding
17 and abetting.

18 If an accountant comes in and deliberately
19 falsifies a financial statement, he is giving
20 substantial assistance to the company's statement
21 through the company who is issuing those false
22 statements. He would be an aider and abetter in that
23 sense. He is also a primary --

24 JUSTICE SCALIA: You see, I really thought
25 the difference was that the principal is the one who

1 makes the deceptive representation and obtains money
2 from it. The aider and abetter is the person who
3 facilitates or enables that deceptive representation,
4 which is what we have here.

5 And you say if you facilitate knowingly and
6 intentionally or even grossly negligently, you are not
7 an aider and abetter, but you're a principal. I really
8 don't understand what's the line between the two.

9 MR. GROSSMAN: If you facilitate with a
10 deceptive act, then you're a primary violator. That's
11 what Section 10(b) prohibits. If you facilitate without
12 a deceptive act, then you are an aider and abetter.

13 JUSTICE GINSBURG: Mr. Grossman, before you
14 finish, there is one statement made by the other side
15 that you are trying to use this -- small in comparison
16 to all the fraud that was involved here in order to
17 collect on the entire loss. That is, you are asserting
18 that the vendors are liable for the entire loss when
19 they were just a bit player.

20 MR. GROSSMAN: Yes. We are not seeking that
21 at all, Your Honor. We -- the PSLRA proportionate
22 liability provisions govern this with respect to --

23 JUSTICE GINSBURG: So what are you seeking?
24 How would you measure your damages?

25 MR. GROSSMAN: We would measure the damages,

1 number one, that flow from this particular scheme. We
2 would have to first subtract the settlements that we've
3 achieved already, and then the proportionate liability
4 provisions of the PSLRA provide how you make this
5 determination.

6 You look at the particular nature of their
7 conduct, and you look at the extent to which their
8 particular conduct had a causal relationship with the
9 damages.

10 CHIEF JUSTICE ROBERTS: Mr. Grossman, I'm
11 conscious of eating into your time but a question -- how
12 many chains of this connection can you have? Let's say
13 Charter was not a publicly traded company, but same
14 thing happened with respect to Scientific-Atlanta, and
15 that made it look valuable to a company that is publicly
16 traded. So they decided to buy Charter and then that
17 made their profits look better to investors. Can you --
18 how many chains in the link can you go?

19 MR. GROSSMAN: Well, I -- I think you can go
20 so long as the person's deceptive conduct has the
21 purpose for furthering a scheme to defraud. If they
22 engage in some deceptive conduct that was not in
23 furtherance of the scheme to defraud, that's another
24 thing. I --

25 CHIEF JUSTICE ROBERTS: Thank you,

1 Mr. Grossman.

2 MR. GROSSMAN: Thank you, Your Honor.

3 CHIEF JUSTICE ROBERTS: Mr. Shapiro.

4 ORAL ARGUMENT BY STEPHEN M. SHAPIRO.

5 ON BEHALF OF THE RESPONDENTS

6 MR. SHAPIRO: Thank you, Mr. Chief Justice,
7 and may it please the Court:

8 My friend has just asked the Court to expand
9 an implied cause of action by diluting traditional
10 requirements such as the reliance requirement and by
11 eroding this Court's precedent in the Central Bank case.

12 The Court has said in the past that it must
13 be very cautious about expanding implied causes of
14 action, but here there are special reasons for caution.
15 Expanding the implied cause of action would give
16 plaintiff the very thing that Congress said it should
17 not get in Section 20(e) of the Exchange Act.

18 Congress wanted cases like this one to be
19 handled by an expert and disinterested administrative
20 agency.

21 JUSTICE GINSBURG: That's if you equate this
22 with aiding and abetting, and I think the question is --
23 is there a middle category between Charter, who is
24 clearly primarily liable, and Central Bank, that didn't
25 do anything deceptive?

1 MR. SHAPIRO: The Central Bank case, I
2 believe, answers that by saying to be a primary violator
3 you have to satisfy all the prerequisites of 10(b)
4 liability, including reliance, loss causation, the
5 "in-connection-with" standard. And here plaintiffs fail
6 to meet these tests. And Congress in 20(e) --

7 JUSTICE GINSBURG: But you are saying -- I
8 thought your argument, unlike the government's argument,
9 is that there was no deceptive device. There was no
10 deceptive device. They simply aided and abetted.

11 MR. SHAPIRO: Yes. That's one of the
12 arguments we make. It is that this case is governed by
13 Central Bank because the defendant did not use or employ
14 deception in connection with a securities transaction.
15 That exactly describes what Charter did.

16 Now, what exactly describes what the vendors
17 are alleged to do is what is said in 20(e) -- to
18 knowingly give substantial assistance to someone else
19 that is misleading an investor. That fits this case
20 like a glove where --

21 JUSTICE KENNEDY: I agree with Justice
22 Ginsburg. I thought the "in-connection-with" argument
23 is actually in addition to or separate from an
24 additional argument you made that there was no deceptive
25 statement made here. I thought that's what you were

1 arguing, and I have problems with that argument because
2 the statute doesn't require a statement. It requires
3 government conduct to suffice.

4 MR. SHAPIRO: We don't make these arguments
5 without reference to each other. We think all of these
6 statutory terms have to be viewed together. You have to
7 use deception in connection with securities trading,
8 which these vendors did not do. That's what Charter
9 did. And we --

10 JUSTICE KENNEDY: Would you say there was
11 deception, standing alone?

12 MR. SHAPIRO: Well, we have -- we have
13 suggested that that is not true when you're speaking
14 with somebody that knows the facts such as Charter.
15 Charter understood all these facts. Charter could have
16 accounted for these transactions correctly, itself. The
17 vendors did that. They didn't recognize any revenues
18 here. It was up to Charter to account for these
19 transactions properly. Congress required it to do that,
20 so it is the speaker here.

21 JUSTICE GINSBURG: But Charter said --
22 vendors, I need you to consummate this fraud on the
23 public. I can't do it without you. I've got to have
24 those revenues that you're going to give me through
25 these phony advertising payments at four or five times

1 the usual rate.

2 MR. SHAPIRO: Well, we believe even placing
3 that most pejorative characterization on these facts,
4 which we don't agree are the true facts, that still --

5 JUSTICE GINSBURG: But you must assume that
6 they are now.

7 MR. SHAPIRO: Assuming that they are, that
8 this is a 20(e) situation where it is alleged that the
9 vendors gave substantial, knowing assistance to somebody
10 who was committing a fraud. And Congress said that an
11 expert and disinterested administrative agency should
12 decide whether to proceed, because it is so slippery to
13 apply these characterizations.

14 JUSTICE GINSBURG: That's if they are --
15 that's if they are aiders and if there are only two
16 categories and everyone who is not Charter is an aider
17 and abettor, then you're right. But if there's a middle
18 category of people who, while not the benefited company
19 -- the company that's trying to achieve the deception --
20 but made it possible for that -- for that deception to
21 happen.

22 MR. SHAPIRO: Well, you know that's an exact
23 description of Central Bank because there it was alleged
24 that the trustee entered --

25 JUSTICE GINSBURG: No --

1 MR. SHAPIRO: -- into a secret agreement.

2 JUSTICE GINSBURG: In Central Bank, it was
3 conceded that the bank engaged in no deceptive act.

4 MR. SHAPIRO: Well, the --

5 JUSTICE GINSBURG: Here there is the charge
6 that it did engage in deceptive acts.

7 MR. SHAPIRO: What was conceded was that the
8 bank made a misstatement to investors, but what was
9 alleged in the complaint and argued in the briefs was
10 that the bank entered into a secret side agreement that
11 enabled the use of a fraudulent prospectus that
12 unleashed securities that were worthless on investors,
13 and investors said, we were depending on our trustee to
14 prevent that from happening.

15 JUSTICE SOUTER: Now, I take it, though, you
16 do not defend the position that there must -- for 10(b)
17 liability, that there must have been a statement
18 addressed to investors.

19 MR. SHAPIRO: Well, we -- we think that for
20 reliance purposes, there --

21 JUSTICE SOUTER: Well, do you --

22 MR. SHAPIRO: -- the defendant has to
23 communicate with investors.

24 JUSTICE SOUTER: Would you answer my
25 question first? Do you take the position that there can

1 be no 10(b) liability without a statement addressed to
2 investors?

3 MR. SHAPIRO: It has to be communicated to
4 the investors and it has to be attributed under the case
5 law to the --

6 JUSTICE SOUTER: You mean the statement as
7 such or a statement which could not have been made but
8 for the statements of the Respondents must be
9 communicated to the investors? Which one?

10 MR. SHAPIRO: That -- that kind of but-for
11 causation is not sufficient. That is not reliance.
12 That kind of --

13 JUSTICE SOUTER: So are you -- so you are
14 saying that there can be no causation and hence, you
15 know -- and I think you're going further. You're saying
16 there can be no liability within the description of
17 10(b) unless there is a statement directly addressed to
18 the investors, is that correct?

19 MR. SHAPIRO: That is one of our
20 submissions, but we also say that the substance of these
21 statements was never communicated to investors. Only
22 Charter --

23 JUSTICE GINSBURG: Because the whole purpose
24 of it --

25 MR. SHAPIRO: -- spoke to the investors and

1 never summarized these.

2 JUSTICE GINSBURG: Mr. Shapiro, if --

3 MR. SHAPIRO: Yes?

4 JUSTICE GINSBURG: If it was communicated to
5 investors that there had been \$20 per set box over the
6 regular price, if there had been advertising that was
7 paid for by the very money that Charter gave, then the
8 whole thing would have failed. So this can work only if
9 the vendors are silent. Silence and not speech is what
10 counts. If the vendors communicate anything at all, the
11 whole thing fails.

12 MR. SHAPIRO: But the -- the communication,
13 Your Honor, has to be to the market and to investors.
14 There was no duty to disclose to investors here. The
15 only communications the vendors made were we're raising
16 our prices 6 percent, the date of our contract is August
17 31st, for the simple reason that it started the very
18 next day --

19 JUSTICE GINSBURG: Was there any --

20 MR. SHAPIRO: -- on September 1st.

21 JUSTICE GINSBURG: Was there any economic
22 substance to this?

23 MR. SHAPIRO: Oh, of course. There was
24 economic substance from the vendors' perspective. They
25 were selling their products at exactly the price that

1 they wanted to receive for those products and they were
2 getting some free cooperative advertising thrown in at
3 the same time.

4 JUSTICE GINSBURG: Is it true that the price
5 that they were charging, they did not charge to other
6 customers -- the \$20 hike?

7 MR. SHAPIRO: Well, it's true because they
8 weren't concerned with that because they weren't paying
9 for it. Charter was paying for this cooperative --
10 cooperative advertising, the reason being --

11 JUSTICE GINSBURG: But it was --

12 MR. SHAPIRO: -- that Charter had a big
13 interest.

14 JUSTICE GINSBURG: -- a sham then, because
15 they said the reason they upped the price \$20 a box was
16 they -- the inflationary conditions, so they had to
17 renegotiate the contract, but didn't renegotiate with
18 any of their other customers.

19 MR. SHAPIRO: Well, Your Honor, from the
20 vendors' perspective, this was a transaction that
21 appeared to be a way to increase cooperative
22 advertising. It cost the vendors no money. They were
23 told by Charter that Arthur Andersen had approved the
24 transaction. That's alleged in the Barford indictment.
25 Then they went home and talked to their own auditors --

1 how could you account for this transaction? The
2 auditors said, you cannot record any revenues from the
3 transaction. They didn't record any revenues. They
4 expected Charter to do the same thing, to not record
5 revenues --

6 JUSTICE KENNEDY: But that's --

7 MR. SHAPIRO: -- of that sort of thing as
8 required.

9 JUSTICE KENNEDY: That's not the allegation
10 of the complaint. I -- I thought the allegation of the
11 complaint was that they -- they knew that this was a
12 fraud and they participated in the fraud.

13 MR. SHAPIRO: Yes, they -- they do allege.
14 I'm merely pointing out that in the --

15 JUSTICE KENNEDY: But I mean that -- so that
16 your answer doesn't seem to be at -- on a legal point.

17 MR. SHAPIRO: Well, we say that if you take
18 the complaint at face value and you don't even consider
19 the Barford indictment that they cite, that it still is
20 a classic example of knowingly giving substantial
21 assistance to someone else that is making misstatements
22 to investors, because these vendors didn't make any
23 misstatement to investors. Nobody relied on their sales
24 correspondence. It sat in a file drawer until long
25 after the stock had gone all the way up and come all the

1 way down.

2 JUSTICE GINSBURG: That's the essence of the
3 scheme. You said that they -- they are home free
4 because they didn't themselves make any statement to
5 investors. But they set up Charter to make those
6 statements, to swell its revenues -- revenues that it in
7 fact didn't have.

8 MR. SHAPIRO: But Congress's policy judgment
9 here is that the SEC, an expert agency that is
10 impartial, should evaluate a claim of that sort and
11 decide whether to proceed.

12 JUSTICE GINSBURG: That's if they are aiders
13 and abettors, which is what Congress covered. And I
14 again go back to, is there another category or is
15 everyone -- either Charter, the person whose stock is at
16 stake, the company whose stock is at stake and everyone
17 else is an aider? I take it that that's your position.

18 MR. SHAPIRO: Well --

19 JUSTICE GINSBURG: It's either the company
20 whose stock is in question or you're an aider and
21 abettor.

22 MR. SHAPIRO: You are only a primary
23 violator under -- under Central Bank if each and every
24 element of 10b-5 liability is satisfied, including
25 reliance on your statement, including the

1 "in-connection-with" test, and including loss causation.
2 None of those tests are satisfied here, but what is
3 satisfied is Section 20(e), which says, did they
4 knowingly give substantial assistance to somebody who is
5 committing a fraud? And that -- that fits this case
6 like a glove --

7 JUSTICE KENNEDY: If we accept --

8 MR. SHAPIRO: -- if Congress wanted the SEC
9 to address --

10 JUSTICE KENNEDY: If we accept your theory
11 of the case and we then get another case in which an
12 accountant or an attorney who prepares the statement for
13 publication to the investors and then gives it to
14 Charter, and they are before us, could we find liability
15 under 10b-5 as to the accountants and still rule -- and
16 still keep our ruling in favor of your client here?

17 MR. SHAPIRO: It really depends on --

18 JUSTICE KENNEDY: And if so, what would --

19 MR. SHAPIRO: -- on the circumstances.

20 JUSTICE KENNEDY: And if so, what would be
21 the rationale?

22 MR. SHAPIRO: Some attorneys are control
23 persons within corporations, and in-house counsel that
24 drafts the disclosure statement which contains a
25 falsehood may be liable as in the Macondua case, which

1 the Court recently considered. Individuals may be
2 liable --

3 JUSTICE KENNEDY: How about outside
4 accountants and attorneys who deliberately and directly
5 participate in negotiating -- or in drafting the false
6 disclosure statements?

7 MR. SHAPIRO: I --

8 JUSTICE KENNEDY: Could they be liable and
9 under your theory of the case, but your client not
10 liable?

11 MR. SHAPIRO: It -- it's possible. Your
12 Honor, at the end of your --

13 JUSTICE SOUTER: Well what about in this
14 case? Let's be specific. As I understood an earlier
15 answer of yours, the answer was that Arthur Andersen
16 knew what was going on. If I've -- if you are -- as I
17 understand it, that's not what was charged, but if
18 that's correct, Arthur Andersen did know what was going
19 on. Can Arthur Andersen be held liable under 10b-5 --

20 MR. SHAPIRO: Absolutely --

21 JUSTICE SOUTER: -- whereas your client
22 cannot?

23 MR. SHAPIRO: Yes, sir. The reason --

24 JUSTICE SOUTER: And the difference is?

25 MR. SHAPIRO: The reason is they issued

1 opinions that were circulated to investors, that were
2 attributed to them and which were authorized by them,
3 and if a lawyer does the same thing, if Steve Shapiro
4 writes an opinion letter and circulates it to investors
5 and it's full of falsehoods --

6 JUSTICE SOUTER: But --

7 MR. SHAPIRO: -- I can be held liable for
8 that --

9 JUSTICE SOUTER: What if Arthur Andersen --

10 MR. SHAPIRO: -- as a speaker.

11 JUSTICE SOUTER: What if Arthur Andersen has
12 a footnote in there saying, this is okay because we have
13 this -- this letter from I forget which one of the two
14 Respondents it was, saying there's been inflation and
15 therefore we've got to renegotiate the prices and jack
16 them up 20 percent, Arthur Anderson knows that that is
17 false and the Respondent who made it knows that it is
18 false, can the Respondent who made it then be held
19 liable?

20 MR. SHAPIRO: Only people who speak to the
21 market --

22 JUSTICE SOUTER: Yes, but doesn't --

23 MR. SHAPIRO: -- and induce investor
24 reliance.

25 JUSTICE SOUTER: Yes, but doesn't -- doesn't

1 the Respondent in that case know that it is likely that
2 the auditor is going to indicate the basis for its
3 statement, that the transaction is okay --

4 MR. SHAPIRO: Well --

5 JUSTICE SOUTER: -- and, therefore, isn't it
6 reasonable to suppose that they anticipated that their
7 statement would be communicated to the market?

8 MR. SHAPIRO: That is just aiding and
9 abetting, and in fact Congress dealt with that squarely
10 in Section 303 --

11 JUSTICE SOUTER: But there's a communication
12 to the market --

13 MR. SHAPIRO: Oh, yes --

14 JUSTICE SOUTER: -- and there's a reason to
15 expect that communication.

16 MR. SHAPIRO: Yes.

17 JUSTICE SOUTER: Doesn't that make any
18 difference?

19 MR. SHAPIRO: That's not sufficient.
20 Congress addressed that in Section 303 of
21 Sarbanes-Oxley, and it held that any person -- said any
22 person including a vendor that misleads an auditor can
23 be held liable in an SEC proceeding only, not in a
24 private suit. It excluded private actions.

25 JUSTICE SOUTER: Is the word "only" in

1 there?

2 MR. SHAPIRO: Pardon me?

3 JUSTICE SOUTER: Is the word "only" in
4 there?

5 MR. SHAPIRO: The word "exclusively" is in
6 there --

7 JUSTICE SOUTER: In the statute?

8 MR. SHAPIRO: -- and my --

9 JUSTICE SOUTER: So you have an independent
10 defense quite apart from -- from the construction of
11 10b-5?

12 MR. SHAPIRO: We rely on 20(e) and 303 of
13 Sarbanes-Oxley, and my friend has made the argument --

14 JUSTICE GINSBURG: Which I thought speak
15 about aiders and abettors.

16 MR. SHAPIRO: It's talking about an aider
17 and abettor that misleads an auditor and then --

18 JUSTICE GINSBURG: But they usually --

19 MR. SHAPIRO: -- the auditor issues a false
20 certification.

21 JUSTICE GINSBURG: -- aider and abettor --
22 then again we get back to the question: If there's
23 nothing in this world other than the company that puts
24 out the false statement and the aider and abettor --

25 MR. SHAPIRO: Well -- oh, no --

1 JUSTICE GINSBURG: -- and is there something
2 in between?

3 MR. SHAPIRO: Your Honor, there are other
4 persons that are control persons within a company who
5 are liable.

6 JUSTICE GINSBURG: We're taking those out.
7 We're taking about independent actors.

8 MR. SHAPIRO: Independent actors that don't
9 speak to the markets and cause direct reliance on their
10 statement are aiders and abetors. And they are supposed
11 to be dealt with by the SEC, an expert agency.

12 Now, my friend made the argument about
13 Sarbanes-Oxley that there's a savings clause in that
14 provision that preserves other remedies. But if you
15 look at the legislative history, it says explicitly we
16 are preserving SEC remedies. We want the SEC to pursue
17 these suits. And Congress refused in 2002 in
18 Sarbanes-Oxley to reinstate the aiding and abetting
19 private liability clause.

20 JUSTICE KENNEDY: Do you know, Mr. Shapiro,
21 if in the law of torts and the restatement of torts or
22 in other areas of the law there is some third
23 classification that's between aider and abettor in
24 principle?

25 MR. SHAPIRO: I don't know the answer.

1 Although in these statutes themselves there are such
2 provisions not included in Section 10(b). For example
3 in Section 18(a), if you cause some other person to make
4 a false statement in a financial statement, you can be
5 held liable, but they are not invoking it in Section 18.
6 Same thing under Section 17. If you engage in a scheme
7 to cause some falsehood, you can be prosecuted by the
8 government.

9 But nowhere has Congress said that an
10 individual litigant can bring a claim like that without
11 regard for reliance and in connection with in the loss
12 causation test.

13 JUSTICE SOUTER: Let's assume there is
14 reliance and loss causation. Let me ask a question very
15 similar to what Justice Ginsburg has posed a couple of
16 times. She has said is there a third category. My
17 question is, is there an overlap? Can there be an
18 overlap?

19 MR. SHAPIRO: No, I don't there can be.

20 JUSTICE SOUTER: Why?

21 MR. SHAPIRO: Because Congress intended in
22 Section 20(e) to have an expert agency to address these
23 cases and not to have the trial --

24 JUSTICE SOUTER: Congress intended an expert
25 agency to address solely aiding and abetting cases. My

1 question is if there is an overlap -- A, can there be an
2 overlap? And if so, I don't see why Congress' intent to
3 reserve aiding and abetting alone to the agency affects
4 the determination of this case.

5 MR. SHAPIRO: We believe they are separate
6 categories and that Central Bank tells us exactly who
7 the primary violator is. He is somebody who makes a
8 statement that investors rely on in connection with
9 securities transactions, and that is not these vendors.
10 That is exactly what Section 20(e) addresses and commits
11 --

12 JUSTICE SCALIA: Could you amend that to
13 say -- you don't insist that he make a statement that
14 invest -- he could engage in a deceptive practice
15 directed at investments?

16 MR. SHAPIRO: Absolutely. Absolutely. We
17 don't quarrel over that, Justice Scalia.

18 JUSTICE SOUTER: For example, for example,
19 let's assume in this case that Charter said we've, we've
20 got to let the investors know that our cost of doing
21 business is going up, and we want to you make an
22 announcement that you're jacking up your price 20
23 percent. In that case there would be primary liability.

24 MR. SHAPIRO: Absolutely.

25 JUSTICE SOUTER: Why in that case is there

1 not also aiding and abetting? We know perfectly why
2 they are doing it, and they are doing it solely to aid
3 and abet Charter in its scheme themselves enjoying a
4 wash transaction. Why isn't that both primary and
5 aiding and abetting?

6 MR. SHAPIRO: Well, it's primary because
7 there is communication of the market that's missing
8 here.

9 JUSTICE SOUTER: We know it's primary. Why
10 isn't it also aiding and abetting?

11 MR. SHAPIRO: You can call it --

12 JUSTICE SOUTER: If you can call it, why
13 isn't there the kind of overlap which raises the
14 question that Justice Ginsburg has raised?

15 MR. SHAPIRO: You can't have primary
16 liability, which they are asserting here, without the
17 statement to the market. And it can be a statement by
18 conduct, and it can be by nodding of the head.

19 JUSTICE SOUTER: So you are saying there can
20 be an overlap but there is no overlap that helps the
21 Petitioner in this case?

22 MR. SHAPIRO: Oh, yes. Nodding the head is
23 the same thing as saying yes. But it has to be made
24 directly to an investor and cause reliance by that
25 investor. That's what's missing here.

1 So there is nothing wrong with the Eighth
2 Circuit's decision. It didn't address that refinement,
3 because it has no bearing on this case. So there is no
4 point in reversing the decision. It has to be affirmed
5 in our view for want of reliance, for want of loss
6 causation, for lack of in connection with, and because
7 most importantly, Congress intended to remove this
8 category of case and commit it to an expert agency as
9 part of its very important reform effort to deal with
10 excessive litigation that was harming our economy.

11 This is an important concept for Congress.
12 And it said it twice: First in the PSLRA in 1995, then
13 in 2002, in the Sarbanes-Oxley law. And it removed even
14 claims that you mislead an auditor under Section 303 of
15 Sarbanes-Oxley. And there is no savings clause there
16 for private actions. Congress refused to permit the
17 private actions.

18 Instead, it permitted the SEC to bring
19 intentional misconduct cases under Section 20(e) or
20 negligent misconduct cases under Section 303 or under
21 Section 13. And the SEC has a broad panoply of
22 remedies. It doesn't have to just allege intentional --

23 JUSTICE GINSBURG: Does the SEC distinguish
24 this kind of situation where silence is the essence of
25 the thing for the deceiver, silence not speech? Does

1 the SEC distinguish this from aiding and abetting?

2 MR. SHAPIRO: Well, the SEC's view is the
3 one rejected by the Solicitor General, and that's this
4 purpose and effect standard that's been advocated, which
5 we think is hopelessly vague. And it overrides the
6 reliance requirement. It overrides in connection with
7 requirement. And it overrides loss causation.

8 JUSTICE STEVENS: Mr. Shapiro, what is your
9 strongest case, in your view, for the reliance
10 requirement?

11 MR. SHAPIRO: Central Bank itself.

12 JUSTICE STEVENS: Central Bank itself?

13 MR. SHAPIRO: Yes. Because the court there
14 said that even though the bank did something that was a
15 secret agreement that facilitated the issuer's
16 distribution of a false prospectus and caused all the
17 harm to the shareholders, it was the direct sine qua non
18 cause of all of that harm. That that was aiding and
19 abetting, because there was no reliance on anything that
20 the bank stated or anything that the bank had a duty to
21 state because of a fiduciary relationship.

22 Now, the vendors here are even far more
23 removed from investors than the bank was in Central
24 Bank. The investors knew about the bank in Central
25 Bank, and they were relying on it to do its job. But

1 that was not sufficient because it made no statement
2 that the investors relied on it. There is no
3 communication here between these vendors and investors.
4 There is no way you could --

5 JUSTICE STEVENS: In your judgment, is the
6 reliance private requirement an element of the violation
7 or of the private cause of action?

8 MR. SHAPIRO: It's the private cause of
9 action. An important point, Justice Stevens, because
10 the SEC is not burdened with any of these elusive
11 inquiries into but for causation, speculative questions
12 of indirect reliance; none of that burdens the SEC.

13 And the SEC also has power to distribute
14 funds to investors. This is the better mouse trap that
15 Congress prescribed for these kinds of cases. It didn't
16 want the trial lawyers to bring class actions that
17 always result in settlements.

18 CHIEF JUSTICE ROBERTS: Thank you,
19 Mr. Shapiro.

20 MR. SHAPIRO: We thank the Court.

21 CHIEF JUSTICE ROBERTS: Mr. Hungar.

22 ORAL ARGUMENT OF THOMAS G. HUNGAR
23 FOR UNITED STATES, AS AMICUS CURIAE,
24 SUPPORTING RESPONDENTS

25 MR. HUNGAR: Thank you, Mr. Chief Justice,

1 and may it please the Court:

2 The Court of Appeals erred to the extent it
3 held that Section 10(b) applies only to verbal
4 misrepresentations or omissions. But the Court
5 correctly held that this Court's decision in Central
6 Bank forecloses Petitioner's claim here. Like the
7 plaintiff in Central Bank, Petitioner cannot establish
8 reliance, a critical element of the Section 10(b)
9 implied right of action.

10 Neither Petitioner nor the market relied on
11 or was even aware of any deceptive conduct or statement
12 by Respondents --

13 JUSTICE STEVENS: Mr. Hungar, I want to be
14 sure I understand one part of the government's position.
15 You do take the position that there has a violation of
16 10-b-5?

17 MR. HUNGAR: We haven't taken a position on
18 that question, Your Honor. We take the position that
19 there was deceptive conduct alleged. That's one of the
20 elements of a 10-b-5 violation, but not the only
21 element.

22 JUSTICE STEVENS: Were the other elements
23 present?

24 MR. HUNGAR: As I say, we have not taken --
25 I mean, materiality, for instance, in connection with

1 requirements scienter we haven't addressed those
2 questions and have not made --

3 JUSTICE STEVENS: Do you have an opinion as
4 to whether there was a violation of 10(b) in this case?

5 MR. HUNGAR: No, Your Honor.

6 JUSTICE STEVENS: You don't have an opinion?

7 MR. HUNGAR: We haven't taken a position.

8 JUSTICE STEVENS: I know you haven't taken a
9 position, but I was just wondering if you have an
10 opinion?

11 (Laughter.)

12 MR. HUNGAR: No, Your Honor. We haven't
13 addressed the other elements and those -- questions that
14 we have -- because there is no need to resolve them in
15 this case and because they weren't resolved by the court
16 of appeals or by the district court, we have chosen to
17 focus on what we think is dispositive and what was
18 raised and decided below which is reliance --

19 JUSTICE STEVENS: You have not reached
20 opinion as to whether there was a violation of the
21 statute?

22 MR. HUNGAR: Correct.

23 JUSTICE SOUTER: Has the SEC publicly taken
24 a position on that question?

25 MR. HUNGAR: I'm not sure of the answer to

1 that question, Your Honor. Certainly individual
2 commissioners have given speeches and testified before
3 Congress to the effect that the Commission voted in this
4 case to agree with our position on deception, the
5 position that's expressed in our brief, and by three to
6 two vote to disagree with the position on reliance that
7 is expressed in our brief. But I don't know that there
8 has been any official SEC Commission statement to that
9 effect that's been publicly released.

10 As I said, the only deceptive conduct that
11 was allegedly committed by Respondents in this case
12 involves the backdating of contracts and the false
13 justifications for the price increase. That conduct was
14 never disclosed to the market at any time during the
15 class period, and therefore, could not have been relied
16 on by the market or by Petitioners.

17 And as a consequence, under this Court's
18 decisions in Central Bank and in Basic, reliance cannot
19 be established because the presumption of reliance that
20 Petitioner seeks to invoke requires as a prerequisite to
21 its invocation the existence of a publicly disseminated
22 statement from the defendant that was disseminated to
23 and, therefore, relied on by the market. That did not
24 happen here with respect to Respondents.

25 JUSTICE GINSBURG: Could SEC get any

1 monetary recovery for the investors on your theory? You
2 say yes, it's a deceptive practice, but this belongs in
3 the SEC's bailiwick, not in private suits?

4 MR. HUNGAR: Yes, Your Honor.

5 JUSTICE GINSBURG: Private suits; obviously
6 they are seeking damages for the decline in the share
7 price. What could the SEC -- suppose it should take up
8 in this case -- get by way of remedy?

9 MR. HUNGAR: The SEC is entitled to obtain
10 civil fines, as well as disgorgement remedies.

11 JUSTICE GINSBURG: But there is no
12 disgorgement here because the vendors didn't get
13 anything. For them it was a wash.

14 MR. HUNGAR: Well, I don't know -- I believe
15 in the, not in this case but in the Adelphia, case which
16 is addressed --

17 JUSTICE GINSBURG: Well this case,
18 disgorgement would not be a remedy. You say fines,
19 those would be payable to the Government, right?

20 MR. HUNGAR: If I may -- yes, yes and no, I
21 think is the answer to that question; because under the
22 fair funds provision of the Sarbanes-Oxley Act, Section
23 308 of Sarbanes-Oxley, the SEC is authorized to take
24 fines and distribute those as -- those as disgorgement
25 relief -- and distribute them to investors.

1 JUSTICE GINSBURG: But there would be no
2 disgorgement relief.

3 MR. HUNGAR: Well, I'm not sure I can agree
4 with that point. In the Adelpia matter --

5 JUSTICE GINSBURG: What profits did the
6 vendors get? For them it was a wash. They got -- what
7 did they have to disgorge?

8 MR. HUNGAR: Well, they obtained -- at least
9 it appears that they obtained advertising that
10 presumably had some value, although it didn't cost them
11 anything; and presumably the SEC could seek the value of
12 that advertising. As I said, in the Adelpia matter
13 where the SEC did pursue the vendors that assisted
14 Adelpia in a somewhat similar transaction, it obtained
15 substantial monetary recoveries from them. I think --

16 JUSTICE GINSBURG: But did they receive
17 something that they then disgorged?

18 MR. HUNGAR: I believe the allegations were
19 similar to those here. But in any event, certainly the
20 SEC has the authority to proceed in that fashion, and
21 additionally the Justice Department has the ability to
22 proceed criminally, and to obtain substantial monetary
23 sanctions, either as part of a deferred prosecution
24 agreement, as part of a restitutionary sanction and the
25 like; but the fundamental point is that for the private

1 right of action to apply, as this Court said in Central
2 Bank, all of the elements of the private cause of action
3 must be satisfied with respect to the individual
4 defendant. That is the line.

5 CHIEF JUSTICE ROBERTS: Do you agree, do you
6 agree with Mr. Shapiro, what I understood to be his
7 argument, that 20(e), the aider and abettor statute,
8 more or less occupies the field here and there is no
9 role for additional 10b-5 liability.

10 MR. HUNGAR: Well, I wouldn't say it
11 occupies the field per se, but what it does do is --
12 given the timing of this Court's decision in Central
13 Bank in 1984 followed by Congress's considering the
14 question and whether to provide for secondary liability
15 in private acts, and its decision not to authorize such
16 secondary liability -- what it does clearly suggest is
17 that this Court ought not adopt the expansive view of
18 the implied right of action that Petitioner is urging,
19 but instead both because the Court is appropriately
20 cautious in expanding liability under implied rights of
21 action, and because Congress has now looked at this
22 question, not once but twice, and has declined to
23 provide secondary liability for secondary actors under
24 the cause of action.

25 JUSTICE SCALIA: You think that you are

1 either a principal or an aider and abettor?

2 MR. HUNGAR: You can, it's possible for
3 someone to be both but in order to be both they must
4 have -- they must have satisfied all of the elements.

5 JUSTICE SCALIA: For the same act, I'm
6 talking about -- for the same act.

7 MR. HUNGAR: Yes. For instance an auditor
8 who certifies false financial statements and allows
9 that -- its certification to be, to be publicly
10 disseminated, thereby aiding and assisting in the
11 issuer's primary fraud, but is also a -- quite likely to
12 be a primary violator, because they have spoken to the
13 market. The market is relying on their statements, and
14 is aware that they are making them; and so they would be
15 both a primary violator, but presumably could be pursued
16 as an aider and abettor. I don't think there is any
17 preclusion of liability under both, but in order to be
18 in that category you must be a primary violator. And
19 here, Petitioners have not established and cannot
20 establish the reliance element with respect to
21 Respondents, because nothing that Respondents said or
22 did was disseminated to the market during the class
23 period.

24 JUSTICE KENNEDY: And I take it in your view
25 they cannot establish the -- in connection with

1 argument. There is no reliance, but that there is in
2 connection --

3 MR. HUNGAR: Your Honor, I would hesitate to
4 say that, Your Honor, because the SEC and the United
5 States do not have to establish reliance in criminal or
6 civil enforcement proceedings, but we do have to
7 establish in connection with, and we think they are
8 different. We think reliance adds something more than
9 what in connection with requires, and so I certainly
10 would urge the Court not to suggest that merely because
11 reliance is not established, therefore in connection
12 with must not also be established; and that is one of
13 the reasons that we think that in connection with
14 question was resolved, not in this case, but in the case
15 where it's been squarely presented, and/ preferably a
16 Government enforcement action where the Government has
17 an opportunity to tailor the case in an appropriate
18 fashion.

19 The Court, as I said has been --

20 CHIEF JUSTICE ROBERTS: It's at least a
21 little awkward for you to say we should wait for a case
22 in which it's been fully presented when the argument
23 you're presenting here wasn't fully presented or at
24 least was not decided below.

25 MR. HUNGAR: I think it was, Your Honor. It

1 was certainly briefed and argued in both the district
2 court and the court of appeals. The district court
3 squarely resolved -- it's at page 41a of the Petition
4 appendix. The court of appeals addressed reliance at
5 page 10a of the Petition appendix. It did not give it a
6 fully orbited discussion.

7 CHIEF JUSTICE ROBERTS: I -- the court of
8 appeals decision would be based on its determination
9 that there was no deceptive act because there was no
10 statement or omission.

11 MR. HUNGAR: But on page 10a, they also talk
12 about reliance, Your Honor; and what's important here to
13 understand is that the Petitioner's theory of reliance
14 rests on a misstatement, because they say it's a market
15 -- it's a basic presumption of reliance based on the
16 fraud in the market theory case. That's the only
17 allegation of reliance in the complaint; that requires
18 something that was publicly disseminated. The only
19 thing that was publicly disseminated is the statement,
20 but the court of appeals said that doesn't work, and
21 there was no reliance because Respondents didn't make
22 any publicly disseminated statement. So it's actually,
23 perhaps not a complete, but certainly a perfectly
24 reasonable resolution of the reliance question; and
25 therefore it is squarely presented. Petitioners has

1 raised reliance in their petition --

2 JUSTICE GINSBURG: I don't see --

3 MR. HUNGAR: -- at page 25. In their
4 opening brief at pages 37 to 40, it's squarely presented
5 and --

6 JUSTICE GINSBURG: I'm looking at the court
7 of appeals decision which I thought just said that there
8 was no deceptive device.

9 MR. HUNGAR: Your Honor, on page 10a, the
10 second line, the first full sentence, speaking of
11 Motorola and Scientific-Atlantic, "they did not issue
12 any misstatement relied upon by the investing public,"
13 and then it goes on the next sentence: "None of the
14 alleged financial misrepresentations by Charter was made
15 by or even with the approval of the vendors," that is
16 the Respondents.

17 Again as I say, it's not as complete a
18 discussion of the reliance issue as we would have
19 thought appropriate if we had been writing the opinion,
20 but it certainly does touch on the question and we think
21 it's wholly presented.

22 CHIEF JUSTICE ROBERTS: Thank you,
23 Mr. Hungar.

24 Mr. Grossman, have you three minutes.

25 REBUTTAL ARGUMENT OF STANLEY M. GROSSMAN

1 ON BEHALF OF THE PETITIONER

2 MR. GROSSMAN: Thank you.

3 I -- excuse me, I have three quick points to
4 make.

5 One, Mr. Shapiro and Mr. Hungar both said
6 that the advertising cost the vendors no money. Well,
7 if the advertising cost them no money, why was there a
8 contract that they entered into for the purchase of
9 advertising? Clearly it was designed to give the false
10 appearance that Charter had this additional \$17 million
11 in revenue.

12 Number two, the SEC did take a position in
13 the Simpson case as it submitted an amicus brief, the
14 commissioners testified before a House committee this
15 past spring that they wanted to submit the same brief on
16 the same points supporting the position that we are
17 taking here; and the testimony of Commissioner Cox is
18 appended to the briefs of Congressmen Franks and
19 Conyers.

20 Number three, Central Bank did not turn on
21 reliance. Central Bank turned on the issue of deceptive
22 conduct. There was no deceptive conduct in that case.
23 The plaintiffs conceded there was no deceptive conduct;
24 the court of appeals and the district court said there
25 was no deceptive conduct; it was strictly an aiding and

1 abetting case.

2 With respect to the reliance issue in
3 Central Bank, what the Court did say was under
4 plaintiff's theory he wouldn't have to prove reliance.
5 He only had to prove that he, that the defendant
6 substantially assisted a defendant who engaged in a
7 primary violation, but he would not have to prove any
8 reliance by the aiding and abettor.

9 Number three, with respect to 20(e), how do
10 my friends on the other side read 20(e) in connection
11 with Section 9 and Section 18 of the Exchange Act, each
12 of which provides remedies and private rights of actions
13 against multiple parties? Under their definition, that
14 would appear to be displaced by 20(e). 20(e) was not
15 designed, it was not intended to do anything but to give
16 the SEC the right to bring the very type of aiding and
17 abetting action that this Court barred in Central Bank.

18 CHIEF JUSTICE ROBERTS: Thank you,
19 Mr. Grossman. The case is submitted.

20 (Whereupon, at 12:00 p.m., the case in the
21 above-entitled matter was submitted.)

22

23

24

25

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