

# Weissmann v. National Association of Securities Dealers: A Dangerously Narrow Interpretation of Absolute Immunity for Self-Regulatory Organizations

Andrew J. Cavo

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## NOTE

# WEISSMAN V. NATIONAL ASSOCIATION OF SECURITIES DEALERS: A DANGEROUSLY NARROW INTERPRETATION OF ABSOLUTE IMMUNITY FOR SELF- REGULATORY ORGANIZATIONS

Andrew J. Cavo†

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## INTRODUCTION

Stock market investments are risky, even when based on reliable information. But when such investments are based on downright fraudulent information, the investments can be ruinous. Around the turn of the century, investor confidence in the securities exchanges waned amidst reports of corporate fraud.<sup>1</sup> In one instance, investors lost billions because they relied on the fraudulent public statements of a single company—WorldCom, Inc.<sup>2</sup>

A corporation's fraudulent public statements, which are made to induce investment, can expose corporations to liability from both private investors and the Securities and Exchange Commission (SEC).<sup>3</sup> But what happens when the corporation that made those statements is bankrupt and piercing the corporate veil is not a viable option?<sup>4</sup> Do private investors have recourse against any other entities such as the securities exchanges through which the investors purchased the stock? In other words, may public statements made by a securities exchange<sup>5</sup> expose the exchange to liability?

Usually, when private investors lose their shirts because of bad stock-market information and look for someone to sue, self-regulatory organizations (SROs)<sup>6</sup> are not an option. SROs are entities designated by the SEC either as national securities exchanges, such as the National Association of Securities Dealers Automated Quotations

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<sup>1</sup> See, e.g., Adam C. Pritchard, *Self-Regulation and Securities Markets*, REGULATION, Spring 2003, at 32 ("Today, many investors are rethinking the wisdom of entrusting their financial futures to the stock market. Absent trust in the integrity of the securities markets, individuals will hoard their money under the proverbial mattress.").

<sup>2</sup> See Daniel Kadlec, *Next: WorldCom's \$11 Billion Case*, TIME, Mar. 15, 2004, at 66 (noting that WorldCom's former chief, Bernard Ebbers, masterminded an accounting fraud estimated near \$11 billion, and caused investors to lose \$180 billion—"three times the amount of wealth destroyed at Enron").

<sup>3</sup> See, e.g., *STONERIDGE INV. PARTNERS V. SCIENTIFIC-ATLANTA, Inc.*, No. 06-43, slip op. at 5-6 (U.S. Jan. 15, 2008) (discussing liability under § 10(b) of the Securities Exchange Act of 1934 and noting that such liability does not extend to aiders and abettors).

<sup>4</sup> The "corporate veil" refers to the separation, for liability purposes, of the corporation from the shareholders who own it: the shareholders may not be held liable in their personal capacity unless the veil is pierced, which may occur in exceptional circumstances of fraud. See, e.g., *DOLE FOOD CO. V. PATRICKSON*, 538 U.S. 468, 474-76 (2003).

<sup>5</sup> See 15 U.S.C. § 78c(a)(1) (2006) ("The term 'exchange' means any organization, association, or group of persons, whether incorporated or unincorporated, which constitutes, maintains, or provides a market place or facilities for bringing together purchasers and sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a stock exchange as that term is generally understood, and includes the market place and the market facilities maintained by such exchange."). For further elaboration on the definition, see 17 C.F.R. § 240.3b-16 (2008).

<sup>6</sup> See 15 U.S.C. § 78c(a)(26) ("The term 'self-regulatory organization' means any national securities exchange, registered securities association, or registered clearing agency . . .").

(NASDAQ) and the New York Stock Exchange<sup>7</sup> (NYSE), or as registered securities associations, such as the National Association of Securities Dealers<sup>8</sup> (NASD). SROs are self-regulating, self-disciplining,<sup>9</sup> quasi-governmental entities that serve the important governmental purpose of providing a fair market for securities trading.<sup>10</sup> These organizations are granted absolute immunity from private lawsuits because of these characteristics, so long as the activity in question is within the quasi-governmental authority delegated by the SEC.<sup>11</sup> But the scope of that authority may be shrinking in a way that makes it possible for private investors to sue the SROs for investments gone awry.

On September 18, 2007, the Eleventh Circuit, sitting en banc, handed down a decision that severely limits the scope of absolute immunity for SROs. In *Weissman v. National Association of Securities Dealers*, the court found that a private investor could sue the NASD and NASDAQ to recover from a disastrous investment in WorldCom because the investor allegedly relied on the SROs' public statements—in particular, two advertisements that had purportedly touted WorldCom as a sound investment.<sup>12</sup> The court denied NASD and NASDAQ's motion to dismiss based on absolute immunity because the defendants issued the advertisements in their private, for-profit capacity—not in their quasi-governmental capacity—and were thus subject to liability.<sup>13</sup> Two strong dissents shredded the majority opinion: one dissent argued in part that one of the two advertisements was indeed part of the SROs' quasi-governmental authority to regulate because NASDAQ was simply disseminating its listing requirements,<sup>14</sup> while

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<sup>7</sup> Ernest E. Badway & Jonathan M. Busch, *Ending Securities Industry Self-Regulation as We Know It*, 57 *RUTGERS L. REV.* 1351, 1352 (2005).

<sup>8</sup> See generally Onnig H. Dombalagian, *Self and Self-Regulation: Resolving the SRO Identity Crisis*, 1 *BROOK. J. CORP. FIN. & COM. L.* 317 (2007) (suggesting alternative ways to regulate the securities exchanges, including a product-oriented system of self-regulation with a consolidated enforcement function).

<sup>9</sup> Badway & Busch, *supra* note 7, at 1352.

<sup>10</sup> See Andreas M. Fleckner, *Stock Exchanges at the Crossroads*, 74 *FORDHAM L. REV.* 2541, 2547–48 (2006) (“[S]tock exchanges perform an important role to provide for fair trading and accurate price discovery, both critical components in fostering investor confidence.”).

<sup>11</sup> See, e.g., *D'Alessio v. NYSE*, 258 F.3d 93, 105 (2d. Cir. 2001) (“The NYSE, as a SRO, stands in the shoes of the SEC in interpreting the securities laws for its members and in monitoring compliance with those laws. It follows that the NYSE should be entitled to the same immunity enjoyed by the SEC when it is performing functions delegated to it under the SEC's broad oversight authority.”).

<sup>12</sup> 500 F.3d 1293, 1294–99 (11th Cir. 2007).

<sup>13</sup> *Id.* at 1299.

<sup>14</sup> *Id.* at 1301–02 (Pryor, J., concurring in part and dissenting in part) (arguing that a particular *Wall Street Journal* advertisement should be covered by absolute immunity but that a particular television ad should not). For a description of the advertisements in question, see *infra* Part II.

the other dissent argued in part that the majority fell victim to artful pleading.<sup>15</sup>

This Note analyzes *Weissman* and its implications, particularly for two other cases in which SROs made public statements that threatened to expose them to liability. First, in *In re NYSE Specialists Securities Litigation* (a case the Second Circuit decided on the same day that the Eleventh Circuit decided *Weissman*), the NYSE made statements attesting to the quality of its oversight while allegedly simultaneously ignoring and encouraging fraudulent activities on its trading floors.<sup>16</sup> Although the Second Circuit upheld the NYSE's absolute immunity for its regulatory actions,<sup>17</sup> the court remanded to determine whether the NYSE could be liable in a private capacity if investors relied on NYSE's public misstatements.<sup>18</sup> The Eleventh Circuit's *Weissman* analysis is likely to play a role in the decision on remand.

The second absolute immunity case that *Weissman* affects is *Opulent Fund v. NASDAQ Stock Market*,<sup>19</sup> in which the Northern District of California denied NASDAQ absolute immunity for public statements that announced the price of its NASDAQ-100 Index. The plaintiff, Opulent, claimed that a particular price announcement was in error, resulting in significant losses on Opulent's options portfolios.<sup>20</sup> The court quoted heavily from *Weissman* in denying NASDAQ absolute immunity for announcing the price of its Index, an activity the court characterized as facilitating the trading of derivatives.<sup>21</sup> Such a characterization meant that announcing that day's price was not considered one of NASDAQ's regulatory activities, but rather one of its private, for-profit activities, and thus was not immune from private suit.<sup>22</sup> Building on *Weissman*, the *Opulent Fund* decision further limits what activities are considered "regulatory."

In this Note I argue that an SRO's regulatory authority should be viewed broadly at the pleadings' stage so as not to unduly narrow the scope of SRO absolute immunity; that an SRO's public statements should normally fall under its regulatory authority; and that an unduly narrow view of that authority will chill SRO media communications. Part I provides a brief history of SROs in the United States and describes how the self-regulatory authority that the SEC grants SROs leads to absolute immunity. Part II summarizes *Weissman* and the two

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<sup>15</sup> *Id.* at 1304, 1311–12 (Tjoflat, J., dissenting).

<sup>16</sup> 503 F.3d 89, 93–94 (2d. Cir. 2007).

<sup>17</sup> *Id.* at 99–101.

<sup>18</sup> *Id.* at 102–03.

<sup>19</sup> No. C-07-03683 RMW, 2007 WL 3010573 (N.D. Cal. Oct. 12, 2007).

<sup>20</sup> *Id.* at \*1–2.

<sup>21</sup> *Id.* at \*5 ("The Eleventh Circuit has also suggested that actions taken to 'increase trading volume' are non-regulatory.")

<sup>22</sup> *Id.* at \*5–6.

cases it immediately affected. Part III examines several of *Weissman's* negative implications, particularly how the decision defeats the very purpose of absolute immunity—to shield officials performing governmental functions from the distractions of recriminatory litigation—by allowing plaintiffs to plead reliance solely on the SRO's for-profit capacity. Part III also offers a way to limit *Weissman's* negative implications by suggesting a tentative solution: when SROs make public statements, absolute immunity should only be withheld if the SRO has recommended a particular course of investment. With this suggestion, I hope to encourage courts to adopt a test for whether an SRO has implicitly recommended an investment; I also offer factors as a starting point for courts to apply such a test.

## I

### BACKGROUND

#### A. Early Self-Regulatory Organizations

SRO self-regulation is almost what it sounds like: SROs regulate themselves by enforcing rules and disciplining members<sup>23</sup> that violate them. The notable caveat to self-regulation is SEC oversight of the entire process.<sup>24</sup> SROs are non-governmental entities that have quasi-governmental authority to enforce the federal securities laws.<sup>25</sup> As such, SROs serve a number of functions.<sup>26</sup> First (and most importantly), they provide a marketplace for transactions where securities can easily be bought and sold.<sup>27</sup> This ease of transfer means that the

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<sup>23</sup> In the SRO context, a “member” essentially means anyone permitted to directly make transactions on the trading floor and any broker or dealer. See 15 U.S.C. § 78c(a)(3)(A) (2006) (“The term ‘member’ when used with respect to a national securities exchange means (i) any natural person permitted to effect transactions on the floor of the exchange without the services of another person acting as broker, (ii) any registered broker or dealer with which such a natural person is associated, (iii) any registered broker or dealer permitted to designate as a representative such a natural person, and (iv) any other registered broker or dealer which agrees to be regulated by such exchange . . .”).

<sup>24</sup> See Toni Anne Puz, Note, *Private Actions for Violations of Securities Exchange Rules: Liability for Nonenforcement and Noncompliance*, 88 COLUM. L. REV. 610, 610–11 (1988). Puz argues for a private cause of action against securities exchanges with liability based on a bad-faith standard for “nonenforcement of [or] noncompliance with exchange rules.” *Id.* at 610, 624–28.

<sup>25</sup> Badway & Busch, *supra* note 7, at 1352.

<sup>26</sup> See John W. Carson, *Conflicts of Interest in Self-Regulation: Can Demutualized Exchanges Successfully Manage Them?* 2 (The World Bank, Policy Research Working Paper No. 3183, 2003) (explaining that the dual roles of the SROs are to “bring buyers and sellers of capital together . . . [and to provide] sources of standards and safeguards that are designed to facilitate efficient markets and promote market integrity”). For a discussion of the implications of demutualization, see *id.*

<sup>27</sup> Fleckner, *supra* note 10, at 2546; see also Roberta S. Karmel, *SRO Immunity in New Era of For-Profit Exchanges*, N.Y.L.J., Dec. 20, 2007, at 3 (explaining that the government has at times exploited SRO scandals to impose government reform and oversight, converting SROs from “private clubs” to public bodies).

SROs provide liquidity to investors in three ways: (1) they bring willing investors together with corporations in need of investment capital; (2) they allow investors to reduce their risk by diversifying their portfolios; and (3) they allow investors to move in and out of an investment efficiently enough that the price does not fluctuate significantly.<sup>28</sup>

The second function that SROs perform is to regulate both their own markets and their members.<sup>29</sup> This regulatory function consists of promulgating and enforcing the SROs' own rules and also enforcing the SEC-created federal securities laws.<sup>30</sup> Thus, all who trade on an SRO's exchange are subject to the SRO's rules and the federal laws that SROs are entrusted to enforce.<sup>31</sup> The SROs have broad authority to discipline violations of rule or law, including the power to fine or ban the violating member.<sup>32</sup>

Self-regulation of the securities industry is not a new phenomenon; American securities exchanges have been regulating their own markets and members since their advent.<sup>33</sup> The NYSE was founded in 1792 as one of the earliest securities exchanges.<sup>34</sup> By the mid-1930s, up to twenty-one different exchanges existed in the United States with little or no governmental oversight<sup>35</sup>—interestingly, this lack of governmental regulation is sometimes said to have been a primary cause of the Great Depression.<sup>36</sup> Nevertheless, the exchanges maintained

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<sup>28</sup> Fleckner, *supra* note 10, at 2546. For a discussion of how the dual nature of SROs—that of regulator and market competitor—creates an inherent conflict of interest, and will inevitably lead to problems of under- and overregulation, see *id.* at 2579–80, 2593–97.

<sup>29</sup> *Id.* at 2547–48.

<sup>30</sup> Badway & Busch, *supra* note 7, at 1352.

<sup>31</sup> Fleckner, *supra* note 10, at 2547 (“All market participants and affiliates, particularly the broker-dealers that trade on the market and the issuers of the traded shares, are subject to rules that stock exchanges enact particularly for their marketplace. Moreover, stock exchanges are empowered to monitor the participants' compliance with the regulatory regime, not only with respect to their own rules but also with federal and state law and rules promulgated thereunder, most importantly by the SEC.”).

<sup>32</sup> *Id.* at 2548.

<sup>33</sup> Badway & Busch, *supra* note 7, at 1352.

<sup>34</sup> *Id.*

<sup>35</sup> *Id.* at 1352–53.

<sup>36</sup> See Pritchard, *supra* note 1, at 35. A key factor in the 1929 crash was the public's reliance on the information that the exchange disseminated; since the exchanges disseminated the information that traders relied on for their next investment, opportunities for fraud abounded. Onnig H. Dombalagian, *Demythologizing the Stock Exchange: Reconciling Self-Regulation and the National Market System*, 39 U. RICH. L. REV. 1069, 1074 n.22 (2005). For example, exchange members would agree to pre-arranged trades to create the appearance of a stock's having a higher trading volume. When the stock price inevitably rose, the conspirators would sell for a quick profit. *Id.*

The problems inherent in the exchanges having superior information over the average investor have not been left in the past. The economic value of the kind of data that stock exchanges offer often leads to securities fraud, such as insider trading and market manipulation. As a primary example, information on recently executed trades, such as volume and parties involved, is critical to analyzing the market and deciding whether to

that they should remain private and that the vast infrastructure they used to self-regulate was superior to a bureaucratic regime.<sup>37</sup> This tension resulted in the Securities Exchange Act of 1934, which was, at bottom, a compromise between Congress and the exchanges.<sup>38</sup>

## B. The Securities Exchange Act of 1934

The Securities Exchange Act of 1934 (the Exchange Act) was largely a result of Congress's increased awareness of "unchecked speculator fraud" and the importance of securities exchanges to the nation's economy.<sup>39</sup> The Exchange Act sought primarily to protect investors from then-common abuses by reining in the exchanges' ability to manipulate stock quotes and trading information.<sup>40</sup> In essence, it codified the self-regulatory regime that the exchanges sought to maintain but provided for SEC oversight.<sup>41</sup> Each SRO would be independently responsible for enforcing its own rules as well as the federal securities laws,<sup>42</sup> but the SEC would serve as a "watch-dog government agency" to ensure such enforcement was done properly.<sup>43</sup>

Under the Exchange Act, the securities exchanges are self-regulatory.<sup>44</sup> This means that they are responsible for promulgating rules, monitoring their members' conduct, and disciplining their own members.<sup>45</sup> SROs are thus legally obligated to regulate themselves,<sup>46</sup> but the rules that the SROs set forth are subject to SEC approval.<sup>47</sup> Though the SEC retains oversight, SROs maintain their quasi-governmental status because they perform the kind of regulatory tasks that the SEC would otherwise have to undertake.<sup>48</sup>

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buy or sell. See Fleckner, *supra* note 10, at 2547. Also, for the derivatives market—a market for financial instruments such as stock options, whose value depends on the price of the stock—sound business decisions require up-to-the-minute stock prices. See *id.* Another example is information on stock quotes—offers to buy and sell at a particular price—which provide a means for predicting future stock price. See *id.* Both information on past trades and stock quotes serve essential regulatory functions as well, because the same information is needed to detect the fraud as is needed to commit it. See *id.*

<sup>37</sup> Cf. Badway & Busch, *supra* note 7, at 1352 (noting that, by 1934, each exchange relied "on the premise that markets are best left to regulate themselves").

<sup>38</sup> See *id.* at 1352–53.

<sup>39</sup> See Puz, *supra* note 24, at 611 (quoting Comment, *Exchange Liability for Improper Enforcement of its Constitution and Rules: The Investor's Right of Action Under the Securities Exchange Act of 1934*, 24 EMORY L.J. 865, 867 (1975)).

<sup>40</sup> See Dombalagian, *supra* note 36, at 1074–75.

<sup>41</sup> See 15 U.S.C. § 78o-3(b) (2006); Badway & Busch, *supra* note 7, at 1353.

<sup>42</sup> Badway & Busch, *supra* note 7, at 1352; Puz, *supra* note 24, at 611.

<sup>43</sup> Badway & Busch, *supra* note 7, at 1353.

<sup>44</sup> 15 U.S.C. § 78c(a)(26).

<sup>45</sup> *Id.* §§ 78f(b), 78s(g)(1).

<sup>46</sup> See SILVER v. NYSE, 373 U.S. 341, 353 (1963); see also 15 U.S.C. § 78f(b) (describing the self-regulatory obligations of SROs).

<sup>47</sup> 15 U.S.C. § 78s(b).

<sup>48</sup> Badway & Busch, *supra* note 7, at 1353.



One of the biggest changes that the Exchange Act effected was to require all national exchanges to register with the SEC and abide by the obligations that it imposed.<sup>49</sup> The SEC has the authority to deny an SRO's registration if the SEC finds that the SRO's rules do not sufficiently guard against fraud, promote equitable trading, or provide for discipline in the event of a violation.<sup>50</sup> Moreover, the SEC has the ability to enforce compliance with the Exchange Act<sup>51</sup> and prevent fraudulent and manipulative practices among the SRO's members.<sup>52</sup>

### C. The Advantages of Self-Regulation

Congress's rationale for permitting SROs to continue to regulate themselves (and the SROs' willingness to regulate themselves) stems from a number of perceived benefits of minimal government regulation. First, self-regulation may provide a cost-effective and efficient method of supervising the markets that the government simply could not provide.<sup>53</sup> The bureaucratic redundancies inherent in complete government supervision would stifle the fast-paced securities industry,<sup>54</sup> which responds minute-by-minute to fluctuations in the market. Second, SROs may be better equipped than a government agency to respond quickly to the highly technical regulatory problems in today's market.<sup>55</sup> Third, SRO self-regulation means that taxpayers do not bear the additional burden that government regulation of the securities markets would entail.<sup>56</sup> Similarly, SROs can use the industry's own funding to regulate,<sup>57</sup> which may be more robust and better focused than government funding. Finally (and perhaps most importantly), self-regulating SROs are not subject to the same legal constraints that a government agency would be—namely the Consti-

<sup>49</sup> *Id.*

<sup>50</sup> *Id.* at 1353–54.

<sup>51</sup> 15 U.S.C. § 78f(b)(1).

<sup>52</sup> *Id.* § 78f(b), (b)(5) (“An exchange shall not be registered as a national securities exchange unless the Commission determines that . . . [t]he rules of the exchange are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, . . . to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest . . .”).

<sup>53</sup> Badway & Busch, *supra* note 7, at 1362.

<sup>54</sup> *See id.*

<sup>55</sup> *See id.*; *see also* Lori Richards, Dir., Office of Compliance Inspections & Examinations, U.S. Sec. & Exch. Comm'n, Remarks at the NRS Fall 2000 Compliance Conference: Self-Regulation in the New Era (Sept. 11, 2000), <http://www.sec.gov/news/speech/spch398.htm> (“Employing self-regulation . . . provides the securities industry with professionals who are more knowledgeable about the intricacies involved in the marketplace and the technical aspects of regulation. This results in a more precise regulatory function.”).

<sup>56</sup> Badway & Busch, *supra* note 7, at 1362–63; Richards, *supra* note 55 (explaining that the securities industry's financing of its own regulation reduces the cost to all taxpayers).

<sup>57</sup> *Cf.* Fleckner, *supra* note 10, at 2586 (stating that the NYSE employs over seven hundred people for regulatory issues).

tution.<sup>58</sup> Thus, SROs are able to hold their members to a higher standard than the government could.<sup>59</sup>

#### D. The Disadvantages of Self-Regulation

Despite the above-mentioned arguments, self-regulation has also been significantly criticized. First, although SROs have traditionally been created as not-for-profit organizations, increasing economic pressures have forced them to move toward demutualization—the process of restructuring an organization to become publicly traded, for-profit entities.<sup>60</sup> As SROs moved closer to for-profit status, many commentators called for changes to the self-regulatory regime.<sup>61</sup> The conflicts of interest inherent in an entity's attempts to maximize profits while regulating itself are undeniable.<sup>62</sup> Incentives to under-regulate abound and may lead to problems such as underfunding the SRO's regulatory arm in favor of a more impressive income statement, or a reluctance to discipline a violating member for fear of losing that

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<sup>58</sup> See William I. Friedman, *The Fourteenth Amendment's Public/Private Distinction Among Securities Regulators in the U.S. Marketplace—Revisited*, 23 ANN. REV. BANKING & FIN. L. 727, 730–31 (2004) (noting that this dichotomy has led to allegations that the SEC has exploited the SROs' investigations in order to bypass constitutional constraints on the SEC's own prosecution of parallel offenses); see also Badway & Busch, *supra* note 7, at 1363.

<sup>59</sup> See Badway & Busch, *supra* note 7, at 1363; Richards, *supra* note 55.

<sup>60</sup> Fleckner, *supra* note 10, at 2541–42 (explaining that demutualization is largely the product of domestic and international competition). Several other factors also brought on this trend. First, technology improvements now allow for more efficient trades that eliminate the middleman dealer. See Dombalagian, *supra* note 8, at 331–33. Second, recent SEC requirements—that the SRO's regulatory function be separate from its operational function—have allowed SROs to operate as for-profit subsidiaries. See *id.* at 333. Further, for-profit structures have allowed SROs to raise money for technology advances through public offerings instead of raising regulatory and trading fees, which would have drawn increased SEC scrutiny. See *id.* at 334.

<sup>61</sup> Cf. Fleckner, *supra* note 10, at 2579–2618 (identifying conflicts of interest created by demutualization and proposing amendments that would mitigate the conflicts of interest that stem from going public). See generally Badway & Busch, *supra* note 7 (suggesting that a “new and improved” SEC should undertake all investigative, policing, and enforcement matters); Dombalagian, *supra* note 36, at 1146–48 (proposing a modified framework that reallocates some self-regulatory responsibilities from exchanges to a representative set of market participants).

<sup>62</sup> See Badway & Busch, *supra* note 7, at 1352 (“SROs are charged with the responsibility of protecting investors and fairness in the capital markets. However, the component parts of SROs—member firms—have quite divergent interests from the public.”).

Member firms—or “Specialist Firms”—are the entities on the stock exchange floors that actually execute sales and purchases of securities for investors. The NYSE has seven member firms through which all securities on the exchange are bought and sold. The member firms are for-profit entities that are allowed to keep an inventory of stock for themselves to sell when a purchase order lacks a ready seller. See *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89, 91–92 (2d Cir. 2007). The facts of *In re NYSE Specialists Securities Litigation* demonstrate the intricate ways that member firms have manipulated the market to their own advantage. See *infra* Part II.

For a historical perspective of SRO scandals that have led to heightened SEC regulation, see Friedman, *supra* note 58, at 746–50.

member's business.<sup>63</sup> Conversely, an SRO's for-profit status may create an incentive to over-regulate because the fines SROs levy against their members go directly into their coffers, providing immediate revenue.<sup>64</sup>

#### E. The 1975 Amendment to the Exchange Act

These inherent deficiencies in the self-regulatory system led Congress to strengthen the SEC's authority over the SROs via the 1975 amendments to the Exchange Act.<sup>65</sup> The amendments allowed the SEC to enforce the SROs' own rules in situations where the SROs were reluctant or unable to do so.<sup>66</sup> The result was a more powerful SEC with authority over SRO rulemaking and SRO disciplinary action—and an SEC that, perhaps most importantly, can discipline the SROs themselves for their actions or failures to act.<sup>67</sup>

In 2007, two of the most prominent SROs—the NASD and the NYSE—decided to change their regulatory structure.<sup>68</sup> They combined many of their member-regulation functions into a new entity called the Financial Industry Regulatory Authority (FINRA).<sup>69</sup> FINRA now oversees the SROs' broker-dealer regulatory functions, though the SROs maintain regulatory control of their own markets.<sup>70</sup> With this move, the SROs essentially separated their market function from

<sup>63</sup> Fleckner, *supra* note 10, at 2593–94.

<sup>64</sup> *Id.* at 2594–95 (noting that this type of overregulation would be problematic because it would not be driven by the SRO's regulatory standards, but rather its financial goals). John Carson discusses proposed strategies to manage these conflicts of interest:

Exchanges and regulators have employed a range of responses in order to manage conflicts of interest. While the specific mechanisms vary widely, responses fall into the following general categories:

- Enhance corporate governance requirements
- Impose ownership restrictions
- Reinforce exchange's public interest mandate
- Upgrade supervision by regulator
- Strengthen exchange internal controls and management processes
- Transfer regulatory functions to an independent SRO
- Transfer regulatory functions to the Public Regulator.

See Carson, *supra* note 26, at 3.

<sup>65</sup> Puz, *supra* note 24, at 612.

<sup>66</sup> Badway & Busch, *supra* note 7, at 1354.

<sup>67</sup> See *id.*; see also Roberta S. Karmel, *Should the New York Stock Exchange Be Reorganized?*, N.Y.L.J., Oct. 16, 2003, at 3 (“The Securities Acts Amendments of 1975 further strengthened the SEC's oversight role over the stock exchanges and the NASD by, among other things, giving the SEC the power to initiate as well as approve SRO rulemaking, expanding the SEC's role in SRO enforcement and discipline, and by allowing the SEC to play an active role in structuring the market.”).

<sup>68</sup> Karmel, *supra* note 27, at 3.

<sup>69</sup> *Id.* The new regulatory entity was initially to be named the Securities Industry Regulatory Authority, or SIRA, but was renamed for fear of confusion with the Arabic word “Sirah,” which refers to biographies of the prophet Muhammad. *Broker Watchdog to Get New Name*, L.A. TIMES, July 13, 2007, at C4.

<sup>70</sup> Karmel, *supra* note 27, at 3.

most of their regulatory functions,<sup>71</sup> making their status as for-profit entities even clearer.

Although FINRA now controls much of the SROs' regulatory function, the discussion that follows—on SROs' absolute immunity for activities that take place within their regulatory authority—is still highly relevant for two reasons. First, *Weissman* and the other cases discussed above predate FINRA. Second, these cases address the scope of the absolute immunity that SROs are granted as regulators of their own *markets* (rather than regulators of their *members*)—a role that both NASDAQ and the NYSE maintain.<sup>72</sup>

## F. Absolute Immunity

By regulating their own markets, SROs perform the quasi-governmental function that affords them absolute immunity from private lawsuits (so long as their activities fall within that regulatory function).<sup>73</sup> Through self-regulation, SROs act for the SEC, which would otherwise regulate the securities markets—and would be afforded sovereign immunity for doing so.<sup>74</sup> Because SROs are private entities, they do not enjoy sovereign immunity; rather, they enjoy what is (somewhat misleadingly) termed “absolute immunity,” an idea that stems from sovereign immunity.<sup>75</sup> The SRO

stands in the shoes of the SEC in interpreting the securities laws for its members and in monitoring compliance with those laws. It follows that the [SRO] should be entitled to the same immunity enjoyed by the SEC when it is performing functions delegated to it under the SEC's broad oversight authority.<sup>76</sup>

The term “absolute immunity” is a bit misleading because SROs “do not enjoy complete immunity from suits; it is only when they are acting under the aegis of the Exchange Act's delegated authority that

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<sup>71</sup> *Id.*

<sup>72</sup> *Id.*

<sup>73</sup> *D'Alessio v. NYSE*, 258 F.3d 93, 106 (2d Cir. 2001) (“[T]he NYSE, when acting in its capacity as a SRO, is entitled to immunity from suit when it engages in conduct consistent with the quasi-governmental powers delegated to it pursuant to the Exchange Act . . .”). Such immunity from private suit is not specific to securities exchanges. Sovereign immunity (from which absolute immunity for SROs derives) protects the federal government against civil suit or criminal prosecution; judicial immunity is granted to judges when acting in their official capacity; and prosecutorial immunity allows prosecutors to grant witnesses immunity from prosecution of their crimes in exchange for their testimony. See *Clinton v. Jones*, 520 U.S. 681, 693 (1997) (“In cases involving prosecutors, legislators, and judges we have repeatedly explained that the immunity serves the public interest in enabling such officials to perform their designated functions effectively without fear that a particular decision may give rise to personal liability.”).

<sup>74</sup> *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89, 96 (2d Cir. 2007); *Barbara v. NYSE*, 99 F.3d 49, 59 (2d Cir. 1996).

<sup>75</sup> *Barbara*, 99 F.3d at 59.

<sup>76</sup> *D'Alessio*, 258 F.3d at 105.

they so qualify. When conducting private business, they remain subject to liability.”<sup>77</sup>

The Exchange Act explicitly delegates authority to the SROs for, among other things, implementing and enforcing federal securities laws,<sup>78</sup> creating and imposing rules to govern exchange members,<sup>79</sup> and disciplining members.<sup>80</sup> Courts have also found that SROs act under their quasi-governmental authority (and are thus immune from private suit) in situations where the SRO temporarily de-lists securities and suspends trading;<sup>81</sup> disciplines exchange members;<sup>82</sup> interprets the application of federal securities laws to the exchange and its members;<sup>83</sup> turns over exchange members that were in violation of federal securities laws to the SEC for civil liability or criminal prosecution;<sup>84</sup> and publicly announces regulatory decisions.<sup>85</sup> A common theme is that absolute immunity attaches in cases that involve the “proper functioning of the regulatory system.”<sup>86</sup>

The million dollar question thus becomes, “What specific SRO functions fall within the regulatory authority delegated by the SEC, such that a private investor may not sue the SRO directly?” The Eleventh Circuit answered this question very narrowly in *Weissman*.

## II

### WEISSMAN V. NATIONAL ASSOCIATION OF SECURITIES DEALERS

*Weissman v. National Association of Securities Dealers* tells the story of Steven Weissman, who purchased 82,800 shares of WorldCom stock between December 2000 and June 2002.<sup>87</sup> When WorldCom collapsed,<sup>88</sup> it took Mr. Weissman’s investment down with it.<sup>89</sup> Seeking recourse for his losses—and having no viable target in the now-bankrupt WorldCom—Mr. Weissman turned on NASDAQ, the market where he bought the securities, and NASDAQ’s oversight body, the

<sup>77</sup> *Sparta Surgical Corp. v. Nat’l Ass’n of Sec. Dealers, Inc.*, 159 F.3d 1209, 1214 (9th Cir. 1998).

<sup>78</sup> 15 U.S.C. § 78s(g) (2006).

<sup>79</sup> *Id.*

<sup>80</sup> *Id.* § 78f(b)(6), (7).

<sup>81</sup> *Sparta Surgical*, 159 F.3d at 1214–15.

<sup>82</sup> *Barbara v. NYSE*, 99 F.3d 49, 58–59 (2d Cir. 1996); *Austin Mun. Sec., Inc. v. Nat’l Ass’n of Sec. Dealers, Inc.*, 757 F.2d 676, 692, 697 (5th Cir. 1985).

<sup>83</sup> *D’Alessio v. NYSE*, 258 F.3d 93, 106 (2d Cir. 2001).

<sup>84</sup> *Id.*

<sup>85</sup> *DL Capital Group v. NASDAQ Stock Mkt.*, 409 F.3d 93, 97–98 (2d Cir. 2005).

<sup>86</sup> *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89, 96 (2d Cir. 2007) (quoting *D’Alessio*, 258 F.3d at 106).

<sup>87</sup> 500 F.3d 1293, 1294 (11th Cir. 2007).

<sup>88</sup> See Kadlec, *supra* note 2, at 66.

<sup>89</sup> *Weissman*, 500 F.3d at 1294.

NASD. Mr. Weissman's complaint alleged that NASDAQ<sup>90</sup> partnered with WorldCom in an effort to promote WorldCom securities and increase trading volume; that NASDAQ assisted in the largest corporate fraud in American history by failing to review WorldCom's fraudulent financial statements; that NASDAQ directly and indirectly profited from Mr. Weissman's purchase of WorldCom stock; and that WorldCom was not in compliance with NASDAQ listing requirements.<sup>91</sup>

Mr. Weissman's specific legal theories for recovery were threefold. First, he alleged that NASDAQ's advertisement promoted and marketed WorldCom without disclosing that NASDAQ profited from increased trading in WorldCom stock, in violation of Florida statutory law.<sup>92</sup> Second, he alleged that NASDAQ offered to sell WorldCom shares without registering as a broker, again in violation of Florida statutory law.<sup>93</sup> Third, he alleged that NASDAQ's use of advertisements to induce purchases of WorldCom shares constituted either common law fraud, negligent misrepresentation, or both.<sup>94</sup> Aware of NASDAQ's absolute immunity for action taken under its regulatory authority, Mr. Weissman carefully crafted his complaint: he stated that he did not rely at all upon NASDAQ's regulatory actions when making his decision to purchase WorldCom shares, but rather relied "solely on the for-profit commercial business activity of [NASDAQ and NASD] . . . includ[ing] [their] approximately \$100 million dollar marketing and advertising campaign during the years 2000, 2001 and 2002 to promote and sell . . . the shares of WorldCom, Inc."<sup>95</sup>

Mr. Weissman allegedly relied on two public statements in making his purchases of WorldCom stock.<sup>96</sup> The first was a television advertisement for NASDAQ's 100 Index Trust product that aired during *The West Wing* and *MSNBC News with Brian Williams*<sup>97</sup> and depicted a group of companies in the 100 Index Trust, including WorldCom.<sup>98</sup> The complaint alleged that the point of the advertisement was to promote those companies as the world's most successful and sought af-

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<sup>90</sup> Throughout the complaint, Weissman referred to NASDAQ as "The For Profit," *id.* at 1298 n.5, presumably to drive home the point that NASDAQ sought monetary gain for the benefit of its shareholders from its promotion of WorldCom and was thus outside its quasi-governmental regulatory authority.

<sup>91</sup> Complaint ¶ 12, *Weissman v. Nat'l Ass'n of Sec. Dealers*, 500 F.3d 1293 (11th Cir. 2007) (No. 03-61107).

<sup>92</sup> *Weissman*, 500 F.3d at 1294.

<sup>93</sup> *Id.*

<sup>94</sup> *Id.* at 1294-95.

<sup>95</sup> Complaint, *supra* note 91, ¶ 6.

<sup>96</sup> *Weissman*, 500 F.3d at 1298-99.

<sup>97</sup> *Id.* at 1298.

<sup>98</sup> *Id.* at 1298-99.

ter,<sup>99</sup> yet the ad did not communicate—nor did Mr. Weissman allege that it communicated—that WorldCom specifically was a good investment.<sup>100</sup>

NASDAQ's second public statement upon which Mr. Weissman claimed reliance was a two-page *Wall Street Journal* spread, whose purpose (according to Mr. Weissman) was to "calm the markets in the wake of [the] Enron fraud."<sup>101</sup> The spread publicly communicated some of NASDAQ's financial disclosure standards established by the SEC—particularly, that NASDAQ-listed companies should follow Generally Accepted Accounting Principles (GAAP).<sup>102</sup> It also included a section with the slogans "The Responsibilities We All Share," "Keeping Our Markets True—It Is All About Character," and "Our Beliefs Stand In Good Company," under which appeared a list of chief executives whose companies traded on the NASDAQ exchange, including Bernard Ebbers of WorldCom.<sup>103</sup> The ad did not mention WorldCom specifically, other than to say that it was among those companies that met the listing criteria.<sup>104</sup> Mr. Weissman claimed that he relied on this advertisement—specifically, that it was evidence of NASDAQ's endorsement of WorldCom as a company of good character and responsible accounting—when he purchased additional shares the day after the ad ran in the *Wall Street Journal*.<sup>105</sup>

The Eleventh Circuit convened en banc "to address the question of whether [an SRO] . . . enjoys absolute immunity for the advertisements described in the complaint in this case."<sup>106</sup> In a notably short majority opinion, the court held that because SROs may claim absolute immunity only when performing functions delegated by the Exchange Act, and because the advertisements upon which Mr. Weissman allegedly relied "were in no sense coterminous" with those regulatory functions, the district court appropriately denied absolute immunity.<sup>107</sup>

#### A. *In re NYSE Specialists Securities Litigation*

On the very same day that *Weissman* was decided, the Second Circuit upheld the NYSE's absolute immunity against allegations that it failed to properly regulate its Specialist Firms, through whom all buy-

<sup>99</sup> *Id.* at 1299.

<sup>100</sup> *Id.* at 1313 (Tjoflat, J., dissenting).

<sup>101</sup> *Id.* at 1299 (majority opinion) (citing Complaint, *supra* note 91, ¶ 62).

<sup>102</sup> *Id.* at 1299.

<sup>103</sup> *Id.*

<sup>104</sup> *Id.* at 1313 (Tjoflat, J., dissenting).

<sup>105</sup> *Id.* at 1299 (majority opinion).

<sup>106</sup> *Id.* at 1295.

<sup>107</sup> *Id.* at 1299.

ers and sellers must transact.<sup>108</sup> In *In re NYSE Specialists Securities Litigation*, lead plaintiffs California Public Employees' Retirement System and Empire Programs, Inc. (Lead Plaintiffs) alleged that over several years, the Specialist Firms actively and systematically used their unique position<sup>109</sup> to their advantage by self-dealing and that the NYSE neglected its regulatory duties by ignoring and, at times, even encouraging this practice.<sup>110</sup>

As in *Weissman*, the Lead Plaintiffs further alleged that they relied on the NYSE's fraudulent misrepresentations—the NYSE's public statements and advertisements—in purchasing NYSE-traded securities.<sup>111</sup> Some advertisements featured Warren Buffet attesting to the virtues that the NYSE has provided for Berkshire Hathaway shareholders,<sup>112</sup> while others portrayed high-level NYSE executives praising the

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<sup>108</sup> *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89, 91–92, 102 (2d. Cir. 2007). Prior to the Lead Plaintiffs' class action suit, the SEC invoked its own regulatory authority against the Specialist Firms. This resulted in settlement agreements under which the firms admitted that they had failed to maintain a fair and orderly market but did not admit to specific Exchange Act violations. The SEC also simultaneously filed and settled an enforcement action against the NYSE, whereby the NYSE did not admit to specific violations but agreed to an order that imposed a censure and prevented the NYSE from committing future federal securities violations. *Id.* at 94.

<sup>109</sup> To grasp the full breadth of the Second Circuit's interpretation of the NYSE's regulatory authority, one must first understand the procedure that NYSE members must follow to buy and sell stocks. Each security traded on the exchange is assigned to a particular Specialist Firm, through which buyers present offers to buy and sellers present offers to sell that security. Each Specialist Firm has an electronic "display book," which allows them to execute orders received from the market to buy and sell. The Specialist Firms act as agents for buyers and sellers by executing orders to buy and sell at the same price. Buyers and sellers are not allowed to conduct trades on the trading floor without the Specialist Firms. *Id.* at 92.

The Specialist Firms are also permitted to act as principals, in a limited fashion. For instance, when there are no orders to buy and sell at the same price, the Specialist Firms may execute an order to buy by selling from the Firm's own inventory of such stock, or execute an order to sell by buying the stock and adding it to the Firm's inventory. *See id.* The complaint points out that the Specialist Firms are in a unique position as potential buyers and sellers that not only control trade but have superior, non-public information about the supply and demand of a given stock. *Id.* at 93–94.

<sup>110</sup> *Id.* at 93–94. Specifically, the Lead Plaintiffs accused NYSE of ignoring, concealing, and encouraging the Specialist Firms' following violations: (1) "interpositioning"—preventing a trade between a normal buyer and seller, to its own benefit; (2) "trading ahead"—using its information to execute trades for its own account ahead of public investors in order to benefit from the gain or loss that the public investors' subsequent trades would create in the market; (3) "freezing the book"—halting the display book for a certain stock to trade from its own inventory before public investors could make any orders; and (4) "manipulating the tick"—changing the price of a stock to affect trading. *Id.* at 93.

<sup>111</sup> *Id.* at 93–95. For example, on January 8, 2001, a NYSE press release allegedly stated, "Our agency-auction model joins the greatest liquidity and transparency with the most efficient method of price discovery, leading to the lowest execution costs and best prices for consumers." *Id.* at 94.

<sup>112</sup> *Id.*



NYSE's reliability and integrity.<sup>113</sup> In describing the fraudulent misrepresentation section of the complaint, the court states that

Lead Plaintiffs claim that these statements deliberately created "the false impression that [the Exchange] was overseeing and operating its auction market in accordance with laws, rules and regulations, and l[ed] investors to believe that the NYSE was an honest and fair market," and that they relied on these misstatements in trading stocks listed on the NYSE's exchange during the Class Period.<sup>114</sup>

The Southern District of New York granted the NYSE's motion to dismiss for failure to state a claim because the NYSE is an SRO and, as such, enjoys absolute immunity as the allegations arose out of the NYSE's quasi-governmental regulatory authority.<sup>115</sup> Alternatively, the district court granted the NYSE's motion to dismiss because the Lead Plaintiffs lacked standing to pursue their fraudulent misrepresentation claim.<sup>116</sup> The Second Circuit affirmed the district court's grant of absolute immunity but vacated the denial of Lead Plaintiffs' standing.<sup>117</sup> The court did not address whether the alleged misrepresentations related to the NYSE's for-profit or regulatory function<sup>118</sup> but specifically directed the district court to consider whether the Lead Plaintiffs' reliance on the statements caused their losses.<sup>119</sup>

By affirming the district court's ruling that the Lead Plaintiffs' claims were barred by absolute immunity, the Second Circuit explicitly interpreted the NYSE's regulatory authority to include the announcement of the SEC investigation and the approval of regulatory reports on its exchange floor.<sup>120</sup> Perhaps most importantly, however, the court unambiguously declined to carve out a fraud exception from the doctrine of absolute immunity, noting that even an exception for the most egregious instance of fraud would undermine the

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113 One such advertisement included then-Chairman of the NYSE, Richard Grasso. *Id.*

114 *Id.* at 94-95.

115 *Id.* at 90-91, 99.

116 *Id.* at 91.

117 *Id.* at 102. The district court dismissed the case in part because it interpreted Rule 10b-5 to say that an action for false statements about a security applies only to the issuer of the security. *Id.* The Second Circuit disagreed, and remanded for further argument on the misrepresentation claims. *Id.* at 102-3. However, the Second Circuit tipped its hand by noting that at least one potential theory of reliance—the fraud-on-the-market theory, under which "the misrepresentation itself affects the market price of the security purchased"—would probably not apply. *Id.* at 103.

118 *Id.* at 103; Karmel, *supra* note 27, at 8.

119 *In re NYSE Specialists*, 503 F.3d at 102-3.

120 *Id.* at 100 ("The gravamen of the Lead Plaintiffs' claims, however, centers on the functions performed by NYSE in its supervisory and regulatory role: announcing investigations, signing off on regulatory reports on the stock exchange floor, and examining the Form 81s for content and legality. While these actions may not appear to form the heart of the regulatory functions delegated to the NYSE as an SRO, they are nonetheless central to effectuating the NYSE's regulatory decisionmaking.").

purpose of the doctrine—to free SROs' quasi-governmental function from disruptive litigation.<sup>121</sup>

The remand sets up an emerging circuit split should the Second Circuit rehear the fraudulent misrepresentation argument on appeal and hold fast to their grant of absolute immunity to the NYSE. But even without the fraudulent misrepresentation analysis, the Second Circuit has clearly adopted a broader view of absolute immunity for SROs than the Eleventh Circuit. The Eleventh Circuit withheld NASDAQ's absolute immunity for what was arguably a regulatory function—publicly communicating its capabilities and regulations.<sup>122</sup> Meanwhile, the Second Circuit declined to carve out a fraud exception to absolute immunity for a highly publicized,<sup>123</sup> SEC-investigated<sup>124</sup> fraud that allegedly went on at a high level inside the NYSE for a number of years,<sup>125</sup> simply because the fraud occurred within the SRO's regulatory function.<sup>126</sup>

The difference in the analyses of the two cases lies in the way each court views the scope of an SRO's regulatory function. The Second Circuit, although reserving judgment on the public statement aspect of the complaint, views SRO regulatory authority broadly, so as to include all of the NYSE's other alleged misconduct.<sup>127</sup> On the other hand, the Eleventh Circuit views that regulatory function narrowly, so as to not even include a public statement intended to communicate the SRO's standards if that statement in any way mentions a company that trades on its exchange.<sup>128</sup> *Weissman's* narrow approach to an SRO's regulatory authority (and thus absolute immunity) may make *Weissman* an untenable precedent.

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<sup>121</sup> *Id.* at 101.

<sup>122</sup> *Weissman v. Nat'l Ass'n of Sec. Dealers*, 500 F.3d 1293, 1299 (11th Cir. 2007).

<sup>123</sup> *In re NYSE Specialists*, 503 F.3d at 93–94 (describing a November 3, 2003 *Wall Street Journal* article that summarizes the contents of a confidential SEC report on the NYSE's regulatory failures).

<sup>124</sup> *Id.* at 94; see also Press Release, Sec. & Exch. Comm'n, SEC Charges the New York Stock Exchange with Failing to Police Specialists (Apr. 12, 2005), <http://www.sec.gov/news/press/2005-53.htm> (“The Securities and Exchange Commission today instituted and simultaneously settled an enforcement action against the New York Stock Exchange, Inc., finding that the NYSE, over the course of nearly four years, failed to police specialists, who engaged in widespread and unlawful proprietary trading on the floor of the NYSE.”).

<sup>125</sup> *In re NYSE Specialists*, 503 F.3d at 94.

<sup>126</sup> *Id.* at 97 (“[T]o the extent that this concept was unclear in our prior precedent, we make the assertion plain: If an SRO's exercise of a governmental power delegated to it deserves absolute immunity, the SRO's nonexercise of that power also entitles it to immunity.”).

<sup>127</sup> *Id.* at 102.

<sup>128</sup> *Weissman v. Nat'l Ass'n of Sec. Dealers*, 500 F.3d 1293, 1299 (11th Cir. 2007).

B. *Opulent Fund v. NASDAQ Stock Market Follows Weissman's Narrow Approach*

Another court has already followed the *Weissman* precedent to some extent. In *Opulent Fund v. NASDAQ Stock Market*—yet another case where an SRO made a public statement that threatens to expose it to liability—the Northern District of California drew heavily from *Weissman* when it denied NASDAQ's motion to dismiss for absolute immunity.<sup>129</sup>

The Plaintiffs—Opulent Fund, L.P. and Opulent Lite, L.P. (Opulent)—were private investment partnerships that profited from trading in stock index options.<sup>130</sup> The value of the NASDAQ-100 Index directly impacted the profits or losses realized on certain options that Opulent traded.<sup>131</sup> (The options were thus derivatives of the NASDAQ-100 Index.)<sup>132</sup> The value of the NASDAQ-100 Index depends on the value of the individual securities on the Index, or more precisely, the NASDAQ Official Opening Price (NOOP) of each security in the Index; thus, timely and accurate reporting of the NOOP and the NASDAQ-100 Index price was essential to Opulent's option trading.<sup>133</sup>

Opulent alleged that on May 19, 2006, NASDAQ reported a NASDAQ-100 Index price of \$1,583.45, while calculating the price based on the NOOPs of the underlying stocks should have yielded a price of \$1,589.18.<sup>134</sup> According to Opulent, the error of \$5.73 per share resulted in significant losses.<sup>135</sup> The court quoted *Weissman* in denying NASDAQ's motion to dismiss and characterized NASDAQ's statement not as regulatory, but rather as within its private, for-profit capacity: “[A]s a private corporation, NASDAQ may engage in a variety of non-governmental activities that serve its private business interests, such as its efforts to increase trading volume.”<sup>136</sup> The court found unpersuasive NASDAQ's argument that the SEC approved the very formula that generated the price later disputed by Opulent.<sup>137</sup>

<sup>129</sup> No. C-07-03683 RMW, 2007 WL 3010573, at \*4–6 (N.D. Cal. Oct. 12, 2007).

<sup>130</sup> *Id.* at \*1.

<sup>131</sup> *Id.* The NASDAQ-100 Index includes the one hundred largest non-financial securities that trade on NASDAQ's exchange. The index is weighted by the market value of the securities of the index, using an SEC-approved computational method. *Id.*

<sup>132</sup> *Id.*

<sup>133</sup> *Id.*

<sup>134</sup> *Id.*

<sup>135</sup> *Id.* That difference cost Opulent significantly on short-put option contracts when Opulent was forced to buy back the security at the strike price of \$1,590. *Id.*

<sup>136</sup> *Id.* at \*5 (quoting *Weissman v. Nat'l Ass'n of Sec. Dealers, Inc.*, 500 F.3d 1293, 1296 (11th Cir. 2007)).

<sup>137</sup> *Id.* (emphasizing that engaging in regulatory conduct, and not SEC approval, is the “*sine qua non* of SRO immunity”).

Although *Opulent Fund* does not involve an SRO's advertising through a public medium, as *Weissman* did, certain similarities between the cases indicate that *Opulent Fund* may narrow SRO immunity even further. First, *Opulent's* allegation involves an SRO making a public statement—that the NASDAQ-100 Index price was what NASDAQ said that it was.<sup>138</sup> However, in *Opulent Fund*, the public statement was not even arguably an attempt to induce investors; rather, the announcement of its NOOP was simply part of its daily operations. The court argued that because the NASDAQ-100 Index is intended to facilitate and support derivative trading—which is not something the government would do if it were performing the SRO's duties—that the NASDAQ-100 Index was not part of NASDAQ's quasi-governmental regulatory function.<sup>139</sup>

Second, the *Opulent Fund* court uses an underlying theme from *Weissman*—that an SRO's for-profit status tends to weigh against an argument that the SRO was acting within its regulatory authority<sup>140</sup>—to deny absolute immunity. That is, because NASDAQ sought to create a derivative market as a way to profit,<sup>141</sup> NASDAQ “represents no one but itself.”<sup>142</sup> Accordingly, NASDAQ should not be granted absolute immunity for an action that is not quasi-governmental.<sup>143</sup> The *Opulent Fund* court thus follows *Weissman* in weighing NASDAQ's for-profit status heavily when determining whether the activity complained of was indeed “regulatory” and whether immunity should attach.<sup>144</sup>

Third, *Opulent Fund* may undermine the doctrine of absolute immunity even further by following *Weissman's* narrow, pro-plaintiff approach to the pleadings' stage to judge whether immunity is or is not appropriate. Never is this more obvious than where the *Opulent Fund*

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<sup>138</sup> *Id.* at \*1.

<sup>139</sup> *Id.* at \*5 (distinguishing NASDAQ's actions from what the court considers an SRO's regulatory functions, such as suspending trading, banning traders, and carrying out disciplinary actions).

<sup>140</sup> *Weissman*, 500 F.3d at 1299 (“Even if NASDAQ's status as a money-making entity does not foreclose absolute immunity for any number of its activities, its television and newspaper advertisements cannot always be said to directly further its regulatory duties under the Securities Exchange Act. These advertisements—by their tone and content—were in the service of NASDAQ's own business, not the government's, and such distinctly non-governmental conduct is not protected by absolute immunity.”); *Opulent Fund*, 2007 WL 3010573, at \*5.

<sup>141</sup> NASDAQ profits by selling the market price data to investors. See *Opulent Fund*, 2007 WL 3010573, at \*5.

<sup>142</sup> *Id.* at \*5 (quoting *Weissman*, 500 F.3d at 1299).

<sup>143</sup> See *id.* at \*5.

<sup>144</sup> *Id.* (“NASDAQ's duty to accurately calculate and disseminate an index price does not function to protect investors; instead, NASDAQ's actions function to create a market and increase trading.”). But see *id.* at \*5 n.1 (“That NASDAQ happens to profit from its activities is not critical. The immunity inquiry turns on the nature of the challenged conduct.”).

court quotes *Weissman* in stating that “‘grants of immunity must be narrowly construed’ because they deprive injured parties of remedies.”<sup>145</sup>

### III

#### ANALYSIS AND IMPLICATIONS OF *WEISSMAN*

*Weissman* is problematic for several reasons. First, by allowing Mr. Weissman to plead around NASDAQ’s absolute immunity defense, the Eleventh Circuit undercuts the very purpose of the absolute immunity doctrine: to cut off a claim at the pleadings’ stage so officials performing important duties may have the peace of mind to focus on those duties.<sup>146</sup> Second, *Weissman* narrows SRO regulatory authority by overlooking an Exchange Act purpose that NASDAQ’s advertisements served: “to remove impediments to and perfect the mechanism of a free and open market.”<sup>147</sup> Third, *Weissman* chills the use of public media for SRO communications.

#### A. *Weissman* Undercuts the Purpose of Absolute Immunity for SROs

The purpose of absolute sovereign immunity is to afford government officials the discretion to perform their duties without the distraction of ongoing and recriminatory litigation.<sup>148</sup> Absolute immunity for SROs is intended to serve the same purpose when SRO officials are performing quasi-governmental functions.<sup>149</sup> Pretrial discovery is just the type of distraction that absolute immunity is meant to avoid;<sup>150</sup> so the very purpose of absolute immunity is defeated if it is not applied aggressively at the pleadings’ stage, before discovery begins.<sup>151</sup> Applying absolute immunity at the pleadings’ stage requires a

<sup>145</sup> *Id.* at \*5 n.2 (quoting *Weissman*, 500 F.3d at 1297).

<sup>146</sup> *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89, 97 (2d. Cir. 2007); *Barbara v. NYSE*, 99 F.3d 49, 59 (2d. Cir. 1996) (explaining that Congress’s purpose in enacting the Exchange Act would be hindered by suits arising out of SRO’s quasi-governmental functions).

<sup>147</sup> 15 U.S.C. § 78o-3(b)(6) (2006).

<sup>148</sup> *In re NYSE Specialists*, 503 F.3d at 97, 101; *Barbara*, 99 F.3d at 58–59 (noting that absolute immunity is particularly appropriate in the SRO context because the SEC would be afforded sovereign immunity if it were to carry out those same functions).

<sup>149</sup> *In re NYSE Specialists*, 503 F.3d at 97 (“After all, the purpose of immunity is to give governmental officials—or those acting with the express delegation of the government, as with SROs—breathing room to exercise their powers without fear that their discretionary decisions may engender endless litigation.”); *cf. Imbler v. Pachtman*, 424 U.S. 409, 424–25 (1976) (addressing absolute immunity for prosecutors).

<sup>150</sup> *See, e.g., Brown v. Crawford County*, 960 F.2d 1002, 1010 (11th Cir. 1992).

<sup>151</sup> *See Mitchell v. Forsyth*, 472 U.S. 511, 526 (1985) (“[A]bsolute immunity . . . is effectively lost if a case is erroneously permitted to go to trial.”). The purpose of absolute immunity is substantive in nature, and it seeks to bring about a particular public goal: to free government officials, or those performing the same functions, from the disruptions of a lawsuit. *See Marx v. Gumbinner*, 855 F.2d 783, 788 (11th Cir. 1988).

court to glean from the complaint the plaintiff's "precise claim."<sup>152</sup> Only after determining that "precise claim" may the court decide whether the activity complained of is one to which absolute immunity attaches.<sup>153</sup>

The *Weissman* court failed to determine Mr. Weissman's precise claim and instead allowed Mr. Weissman to artfully plead around NASDAQ's absolute immunity defense. In his complaint, Mr. Weissman alleged—and the court majority parroted—that "NASDAQ touted, marketed, advertised and promoted WorldCom, falsely representing it as a good company and worthwhile investment and disseminating its fraudulent financial statements, without revealing that, *inter alia*: . . . WorldCom was not in compliance with N[ASDAQ] listing requirements . . ."<sup>154</sup> From that statement, it appears that Mr. Weissman's precise claim is that NASDAQ's for-profit status caused it to continue listing WorldCom even after it knew or should have known that NASDAQ was acting illegally.<sup>155</sup> But such an allegation would not have evaded NASDAQ's absolute immunity because the decision to list or not list a stock clearly falls within NASDAQ's regulatory authority.<sup>156</sup> So Mr. Weissman took a different approach in his complaint, stating:

This action is based *solely* on [NASDAQ's] for-profit commercial business activity. . . . Plaintiff makes no claim based upon any failure of the Defendants to fulfill any duties as a self regulatory organization under the Exchange Act or otherwise. Likewise, Plaintiff's claims are not based upon any failure of the Defendants to properly regulate any aspects of the securities markets, publicly traded companies, or any market participants whatsoever; or, in connection with enforcement of its rules and the performance of its regulatory or adjudicatory responsibilities or functions.<sup>157</sup>

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<sup>152</sup> See, e.g., *Burns v. Reed*, 500 U.S. 478, 487 (1991); *Marrero v. City of Hialeah*, 625 F.2d 499, 505 (5th Cir. 1980) (noting a need to isolate the specific conduct complained of).

<sup>153</sup> See, e.g., *Marx*, 855 F.2d at 788–89; see also *Weissman v. Nat'l Ass'n of Sec. Dealers*, 500 F.3d 1293, 1306 (11th Cir. 2007) (Tjoflat, J., dissenting) (describing the concept of "functionality," which "examine[s] the nature of the functions with which a particular official or class of officials has been lawfully entrusted, and . . . seek[s] to evaluate the effect that exposure to particular forms of liability would likely have on the appropriate exercise of those functions" (quoting *Forrester v. White*, 484 U.S. 219, 224 (1988))).

<sup>154</sup> *Weissman*, 500 F.3d at 1298 (alteration in original) (quoting Complaint, *supra* note 91, ¶ 12).

<sup>155</sup> *Id.* at 1312 (Tjoflat, J., dissenting).

<sup>156</sup> See *Sparta Surgical Corp. v. Nat'l Ass'n of Sec. Dealers*, 159 F.3d 1209, 1213–15 (9th Cir. 1998).

<sup>157</sup> Complaint, *supra* note 91, ¶ 6.

In dissent, Judge Tjoflat pointed out that the majority accepted these conclusory statements without questioning their veracity.<sup>158</sup> How Mr. Weissman could have known exactly whether the NASDAQ regulatory or for-profit function persuaded him to purchase shares of WorldCom is perplexing, but the court appears to take Mr. Weissman at his word that his reliance was beyond NASDAQ's regulatory authority. Had the court probed more closely to determine Mr. Weissman's precise claim, the outcome would likely have been different.

Mr. Weissman's precise claim was based on the two advertisements described above. The first—the television ad for NASDAQ's 100 Index Trust—featured a group of one hundred companies that had the largest market capitalizations, including WorldCom.<sup>159</sup> But that television ad did not tout WorldCom specifically as a good investment<sup>160</sup> or distinguish it in any way from the other ninety-nine companies mentioned<sup>161</sup>—none of which were purchased by Mr. Weissman right away as a result of it. His precise claim with respect to this ad is simply that NASDAQ ran a commercial that listed WorldCom among the one hundred companies with the largest market capitalizations—hardly the aggressive marketing of WorldCom and upon which Mr. Weissman claims reliance.

The *Wall Street Journal* spread was even less suggestive. The ad expressed NASDAQ's belief that companies that list on its exchange should report their financials accurately, using GAAP.<sup>162</sup> It included a list of chief executives of companies that trade on the NASDAQ exchange,<sup>163</sup> which happened to include Bernard J. Ebbers, WorldCom's president and CEO,<sup>164</sup> along with the names of eighty-one chief executives of other companies.<sup>165</sup> The inclusion of Mr. Ebbers's name on that list, however, was apparently such an effective marketing technique that it alone—not any of WorldCom's perceived qualities—caused Mr. Weissman to purchase additional shares the very next day, even as WorldCom's share price plummeted.<sup>166</sup>

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<sup>158</sup> *Weissman*, 500 F.3d at 1312 (Tjoflat, J., dissenting) (“[T]he majority all too happily accepts Weissman’s baseless disavowal of ‘any reliance on NASDAQ’s regulatory activity as the basis for his suit,’ . . . apparently taking his word for it that NASDAQ’s actions constituted touting, marketing, advertising and promotion and that such activities fall outside the functions for which NASDAQ ought to enjoy immunity.”).

<sup>159</sup> *Id.* at 1298–99 (majority opinion).

<sup>160</sup> *Id.* at 1313 (Tjoflat, J., dissenting).

<sup>161</sup> *Id.*

<sup>162</sup> *Id.* at 1301 (Pryor, J., concurring in part and dissenting in part).

<sup>163</sup> *Id.*

<sup>164</sup> *Id.*

<sup>165</sup> Brief for Defendants-Appellants at 9, *Weissman v. Nat’l Ass’n of Sec. Dealers*, No. 04-13575-EE (11th Cir. Sept. 24, 2004).

<sup>166</sup> *Weissman*, 500 F.3d at 1299 (majority opinion); see also Complaint, *supra* note 91, ¶¶ 62, 96.

Mr. Weissman's highly unusual reaction to a rather passive advertisement led the court to again mischaracterize his precise claim. Its more accurate characterization is that NASDAQ ran an ad dispatching its regulatory information, intending to convey no more than that NASDAQ-traded companies must meet strict listing requirements, and that WorldCom was among the companies traded on NASDAQ's exchange.<sup>167</sup> The same type of information could likely be found in a NASDAQ press release or on its web site.<sup>168</sup> But by asserting that he relied only on the for-profit capacity of these two advertisements, Mr. Weissman effectively pleaded around NASDAQ's absolute immunity defense. These more exacting descriptions of the public statements in question hardly rise to the level of "touting," as Mr. Weissman alleged,<sup>169</sup> and the court's acceptance of Mr. Weissman's self-serving characterizations improperly cost NASDAQ its absolute immunity.

The *Weissman* decision weakens a doctrine intended to prevent the very distractions for SRO officials that the case caused, and the decision makes recriminatory litigation more likely. Under *Weissman*, every time an SRO mentions a company that trades on its exchange, it exposes itself to liability if an investment in that company turns out badly.

#### B. *Weissman* Limits Absolute Immunity by Viewing "Regulatory Duties" Too Narrowly

SROs are granted absolute immunity for duties delegated to them by the SEC in the Exchange Act.<sup>170</sup> These duties have long included an SRO's regulatory duties.<sup>171</sup> But what specific duties may be considered "regulatory" depends largely upon case law interpretations of an SRO's duties. *Weissman* limits absolute immunity for SROs by narrowing the scope of duties that an SRO's regulatory authority includes.

NASDAQ's *Wall Street Journal* spread—as Judge Pryor's separate opinion argued—should have been considered regulatory because it was issued under NASDAQ's SEC-delegated authority.<sup>172</sup> The SEC delegated authority to the SROs to

promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mecha-

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<sup>167</sup> *Weissman*, 500 F.3d at 1301 (Pryor J., concurring in part and dissenting in part).

<sup>168</sup> *Id.*

<sup>169</sup> Complaint, *supra* note 91, ¶ 67; see also *Weissman*, 500 F. 3d at 1302.

<sup>170</sup> See, e.g., *Weissman*, 500 F.3d at 1296 (majority opinion).

<sup>171</sup> *Id.* at 1296.

<sup>172</sup> *Id.* at 1300–02 (Pryor, J., concurring in part and dissenting in part).



*nism of a free and open market* and a national market system, and, in general, to protect investors and the public interest . . . .<sup>173</sup>

To accomplish these goals, an SRO must have authority to list and de-list the securities that trade on its exchange.<sup>174</sup> Thus, the communication of the listing requirements used to determine whether a security is listed or de-listed must also be considered a regulatory function.<sup>175</sup> Such information is essential for listed companies to know how to remain in compliance with listing requirements and for the investing public to know what standards those traded companies must meet. As such, this function properly falls under an SRO's delegated regulatory authority "to remove impediments to and perfect the mechanism of a free and open market."<sup>176</sup>

The *Weissman* court seems to have overlooked the regulatory purpose served by the *Wall Street Journal* advertisement. The result is a narrower view of an SRO's regulatory authority, which carves out a significant chunk of the doctrine of SRO absolute immunity. After *Weissman*, an SRO may be subject to liability if it publicly communicates its listing requirements alongside a list of companies that the SRO believes to meet those requirements.

### C. *Weissman* Chills SRO Media Communications

Another negative implication of *Weissman* is that SROs will now be more reluctant to use commercial media outlets to communicate their regulatory standards to the investing public. Mr. Weissman's complaint seized on the bare mention of WorldCom's CEO, Bernard Ebbers, in a newspaper spread intended to communicate NASDAQ's listing requirements.<sup>177</sup> Such a statement, which was once a permissible form of public communication from SROs to shareholders, listing companies, and potential investors, could now render SROs liable for the fraudulent actions of any and all companies that trade on their exchanges. A perception of certain types of advertisements—such as

<sup>173</sup> 15 U.S.C. § 78o-3(b)(6) (2006) (emphasis added).

<sup>174</sup> See *Sparta Surgical Corp. v. Nat'l Ass'n of Sec. Dealers*, 159 F.3d 1209, 1214–15 (9th Cir. 1998).

<sup>175</sup> See *DL Capital Group v. NASDAQ Stock Mkt.*, 409 F.3d 93, 98 (2d Cir. 2005) (finding an SRO immune after it announced the suspension of trading, which the court likened to the regulatory action of actually suspending trading).

<sup>176</sup> 15 U.S.C. § 78o-3(b)(6); see *DL Capital Group*, 409 F.3d at 98 ("Without the capacity to make announcements, [SROs] would be stripped of a critical and necessary part of their regulatory powers"—namely, the power to inform the public of those actions it has undertaken in the interest of maintaining a 'fair and orderly market' or protecting 'investors and the public interest.'" (quoting NASD Rule 11890(b) (2008))); see also *Weissman*, 500 F.3d at 1301 (Pryor, J., concurring in part and dissenting in part) (describing an SRO's right to communicate to the investing public that listed companies must satisfy rigorous financial standards).

<sup>177</sup> Complaint, *supra* note 91, ¶ 62.

those in *Weissman*—as beyond the scope of an SRO’s regulatory function will foster distrust of public media as an avenue for such communication and frustrate an SRO’s ability to communicate publicly with shareholders.

One might argue that an SRO could avoid such potential liability by simply removing the names of any companies that trade on that exchange from its public statements. But the *Weissman* court did not draw a line there, or anywhere, to indicate the extent to which an SRO may tout its services through public statements without risking liability. The cursory majority opinion seems to stand for the proposition that any mention of a company by an SRO represents the SRO’s whole-hearted endorsement of that company’s professional integrity; the SRO will not be able to claim immunity if that company turns out to have acted fraudulently.

Similarly, with respect to the *forms* of public statements that will preclude an absolute immunity defense, *Weissman* leaves more questions than it answers. Does *Weissman* mean that an SRO forfeits its absolute immunity when using its website to list certain companies that trade on the exchange? May an SRO executive speak to the quality of the exchange in a speech or an interview by mentioning the specific companies that trade on it? Does the SRO expose itself when using the *Wall Street Journal* to disseminate other types of regulatory information, such as suspension or resumption of trading notices?<sup>178</sup> Must SROs find a way to demonstrate their value without mentioning those companies at all? The lack of answers to these pivotal questions will leave SROs wondering which forms of communication will cause them to forfeit their absolute immunity and which will not. The result will likely be a decrease in the use of the commercial media as an outlet for SRO communications.

#### D. A Better Approach: The “Investment Recommendation” Test

The current test for absolute immunity leaves too much room for courts to interpret whether a public statement qualifies as a quasi-governmental regulatory function.<sup>179</sup> As a result, the SROs’ ever-increasing for-profit status is swaying courts away from granting SROs absolute immunity for their public statements.

A better approach would be to categorize an SRO’s public statements as either purely regulatory, purely nonregulatory, or mixed, before determining whether absolute immunity should attach. Purely regulatory statements, such as disclosures of listing requirements that do not mention any companies specifically, should always enjoy abso-

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<sup>178</sup> *Weissman*, 500 F.3d at 1301 (arguing that such communications are regulatory in nature and therefore should be protected by the doctrine of absolute immunity).

<sup>179</sup> *Id.* at 1314.

lute immunity. Purely nonregulatory statements, such as naked promotion of companies that trade on an SRO's exchange (or naked promotion of the exchange itself), should never enjoy absolute immunity. Mixed statements, however, present a trickier question, to which the *Weissman* court neglected to respond with a clear legal standard.

Mixed statements, the broad category that would seem to include the advertisements in *Weissman*, contain some regulatory information and some other information that serves little regulatory purpose. This other information may run the gamut of everything that an SRO wishes to convey and may span the full range of an SRO's authority spectrum—from regulatory to for-profit. An SRO's immunity with regard to mixed statements should thus turn on the nature of the information and whether the information serves little regulatory purpose. The best approach to determine the nature of the information in mixed statements is an "investment recommendation" test: if the information is neutral, in that it simply provides names of companies and their CEOs, for instance, absolute immunity should attach; on the other hand, if the statement makes an explicit or implicit recommendation for a particular course of investment,<sup>180</sup> an SRO should forfeit its absolute immunity. In other words, an SRO's regulatory authority includes the broad authority to make public statements, unless the statement recommends a particular course of investment. If instead an SRO's public statement *does* recommend a particular investment, the SRO's absolute immunity should not bar a claim if an investor relies upon and is injured by the statement. Recommending a particular course of investment is clearly beyond what the SEC would do and what an SRO should do.

When determining whether an SRO's public statement recommends an investment, courts should consider the following factors: the quantity of regulatory information in proportion to the other information included in the statement; the sophistication of the investor (or potential investor) at whom the statement is targeted; the truth of the statement; the font size of the information in question in relation to the statement's regulatory information; whether the statement is made by an individual officer to a particular audience or as a generic statement from the SRO to the investing public at large; the medium through which the statement is made; and whether the information is intended to be relied upon as investment advice or should be dis-

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<sup>180</sup> I use the phrase "particular *course of investment*" here, rather than simply a "particular investment" because an SRO may recommend a series of investments, an investment strategy, or simply an investment in the SRO itself. The SEC would not perform any such duties had it not delegated its authority to the SROs, so these activities are rightly beyond an SRO's regulatory authority.

missed as puffery.<sup>181</sup> A final consideration may be the economic context in which the statement is released—during periods of financial crisis, investors may be hyper-sensitive to positive information and thus more likely to perceive mixed SRO statements as investment recommendations. No single factor will likely dominate the analysis; courts should adjust the relative weight of these factors in each particular case.

### E. Reexamining the Case Law Under the New Approach

A reexamination of *Weissman* under this standard would yield quite a different result. The following factors tend to indicate that the advertisements in *Weissman* did not recommend a particular course of investment: (1) the regulatory information in both advertisements dwarfed NASDAQ's mere mention of WorldCom; (2) the non-regulatory information in both advertisements was true—WorldCom was listed on NASDAQ and Bernard Ebbers was indeed its CEO; (3) the advertisements were targeted at the investing public at large through commercial media (rather than, say, a live speech by a corporate officer to a limited number of individuals); and (4) the slogans contained in the statements were highly generic in nature,<sup>182</sup> suggesting that a reasonable investor would likely have dismissed them as puffery. *Weissman's* interpretation of the advertisements—that NASDAQ was really saying “that the world's most successful, sought after companies, can be found on the N[ASDAQ] stock market”<sup>183</sup>—requires a major leap from what NASDAQ actually said to what Mr. Weissman alleged. Such a leap costs the SROs their immunity and undercuts the very purpose of the doctrine.

*Opulent Fund* would be even more likely to come out differently under this investment recommendation test.<sup>184</sup> NASDAQ's statement announcing the price of its index would likely fall into the purely regulatory category of SRO public statements, since NASDAQ simply announced the price of its NASDAQ-100 Index and did not include any

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<sup>181</sup> See *In re Ford Motor Co. Sec. Litig.*, 381 F.3d 563, 570–71 (6th Cir. 2004) (“Courts everywhere ‘have demonstrated a willingness to find immaterial as a matter of law a certain kind of rosy affirmation commonly heard from corporate managers and numbingly familiar to the marketplace—loosely optimistic statements that are so vague, so lacking in specificity, or so clearly constituting the opinions of the speaker, that no reasonable investor could find them important to the total mix of information available.’” (quoting *Shaw v. Digital Equip. Corp.*, 82 F.3d 1194, 1217 (1st Cir. 1996))); see also *Lasker v. N.Y. State Elec. & Gas Corp.*, 85 F.3d 55, 58 (2d Cir. 1996) (affirming the district court's assertion that a corporation's self-praise about its business strategy is “not considered seriously by the marketplace and investors in assessing a potential investment”).

<sup>182</sup> See *supra* Part II.

<sup>183</sup> Complaint, *supra* note 91, ¶ 61.

<sup>184</sup> *Opulent Fund v. NASDAQ Stock Mkt.*, No. C-07-03683 RMW, 2007 WL 3010573 (N.D. Cal. Oct. 12, 2007).

other information in the statement that could possibly be interpreted as recommending a particular investment.

It is, however, unclear whether *In re NYSE Specialists Securities Litigation* would come out differently. The Second Circuit's opinion<sup>185</sup> does not provide enough details of the NYSE's public statements concerning the quality of its oversight function to determine whether it recommended a particular course of investment.

#### CONCLUSION

In viewing an SRO's regulatory duties narrowly and allowing Steven Weissman to artfully plead reliance on NASDAQ's for-profit capacity, the Eleventh Circuit undermined the doctrine of absolute immunity for SROs. In denying NASDAQ's motion to dismiss, the court defeated the doctrine's purpose and exposed SROs to liability from individual investors. The Eleventh Circuit's narrow approach to absolute immunity is vastly dissimilar to that of the Second Circuit, which declined to carve out an exception to absolute immunity even when faced with allegations of egregious fraud that went on for years, cost investors millions, and warranted SEC action.

The negative implications of *Weissman* are as follows: the decision (1) allows investors to plead around an SRO's absolute immunity by simply claiming reliance solely on its for-profit function; (2) limits SRO's legitimate behavior because they do not know beforehand what conduct falls under their regulatory authority and what does not, making it much harder for absolute immunity to serve its essential purpose; and (3) chills SRO communications through public media.

If the Second Circuit has the opportunity to revisit the fraudulent misrepresentation claim from *In re NYSE Specialists Securities Litigation* on appeal from remand, it should expressly decline to follow any *Weissman*-like narrowing of the doctrine of absolute immunity for the reasons set forth above. Further, if the Ninth Circuit has an opportunity to hear *Opulent Fund* on appeal, it should decline to follow *Weissman* and reverse.

Perhaps a better approach to SRO absolute immunity for public statements is to ask whether the statement recommends a particular course of investment. If not, SROs should maintain their absolute immunity from private lawsuits.

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<sup>185</sup> *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89 (2d Cir. 2007).