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# The New Group Pleading Doctrine

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# NOTE

## THE NEW GROUP PLEADING DOCTRINE

*Matthew Agliatoro*†

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### INTRODUCTION

In typical civil lawsuits, plaintiffs' first step toward recovery is determining who is responsible for their harm. Although identifying a defendant may seem like a trivial task, in a cause of action brought under the federal securities laws, determining who is responsible for a plaintiff's harm is not always easy.<sup>1</sup> A corporation acts through a num-

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† B.A., Baruch College–The City University of New York, 2009; Candidate for J.D., Cornell Law School, 2014; Senior Articles Editor, *Cornell Law Review*, Volume 99. I would like to thank Professors Kevin Clermont and Charles Whitehead for their insight and helpful comments. I am also extremely grateful for the hard work and dedication of the associates and editors of the *Cornell Law Review*, especially Notes Editors Steven Ma and Stefanie Williams, as well as Managing Editors Conor McCormick, Catherine Eisenhut, and T.J. Vita. Finally, I would like to thank Jade Harry and the rest of my friends and family, whose unwavering love and support has made it all possible.

<sup>1</sup> See, e.g., Enzo Incandela, Note, *Recourse Under § 10(b) on Life Support: The Displacement of Liability and Private Securities Fraud Action After Janus v. First Derivative*, 43 Loy. U.

ber of different agents, including its directors and executives. Through their corporation, those agents release a number of unsigned, yet publicly available documents, such as press releases and SEC-required disclosures. When those documents contain material misstatements or omissions, plaintiffs must determine which agents are responsible for creating those documents in order to recover.<sup>2</sup>

In addition to difficulties associated with identifying a responsible agent, the Private Securities Litigation Reform Act (PSLRA) and the Federal Rules of Civil Procedure have instituted heightened pleading standards in cases of corporate fraud.<sup>3</sup> One can see the problem that arises when plaintiffs are unsure of which corporate agent is ultimately responsible for their harm but nevertheless must plead each element of fraud with particularity.

Recognizing this burden, courts crafted the group pleading doctrine. The group pleading doctrine creates a presumption “that certain group-published documents [such as SEC filings and press releases] . . . are attributable to corporate insiders involved in the everyday affairs of the company.”<sup>4</sup> The presumption allows a plaintiff to “circumvent the general pleading rule that fraudulent statements must be linked directly to the party accused of the fraudulent intent.”<sup>5</sup> For example, where a corporation issues an unsigned press release containing a false or misleading statement of material fact, a court employing the group pleading doctrine would presume that certain directors and officers collectively took part in creating the press release.<sup>6</sup>

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CHI. L.J. 935, 975 (2012) (noting the difficulty of determining nonspeaking defendants who have no duty to disclose).

<sup>2</sup> See *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 157 (2008).

<sup>3</sup> See Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified as amended at 15 U.S.C. §§ 77z-1, 77z-2, 78j-1, 78u-4, 78u-5 (2012)); FED. R. Civ. P. 9(b). Both the PSLRA and the Federal Rules of Civil Procedure require plaintiffs to plead each element of fraud with particularity.

<sup>4</sup> *In re UBS AG Sec. Litig.*, No. 07 Civ. 11225(RJS), 2012 WL 4471265, at \*9 (S.D.N.Y. Sept. 28, 2012) (quoting *In re Take-Two Interactive Sec. Litig.*, 551 F. Supp. 2d 247, 266 (S.D.N.Y. 2008)).

<sup>5</sup> *Id.* (quoting *In re Am. Int'l Grp., Inc.* 2008 Sec. Litig., 741 F. Supp. 2d 511, 529–30 (S.D.N.Y. 2010)); see also *Wool v. Tandem Computers Inc.*, 818 F.2d 1433, 1441–42 (9th Cir. 1987) (noting that it is permissible to presume that corporate officers involved in the day-to-day activity of a corporation have the power to control transactions giving rise to securities violations). Many circuit courts have applied the presumption differently. For example, the Ninth Circuit has found that the presumption may not necessarily extend to outside directors. See *In re Stac Elecs. Sec. Litig.*, 89 F.3d 1399, 1410–11 (9th Cir. 1996).

<sup>6</sup> This assumes the press release is unsigned. Where attribution is clear, the particular defendants are liable for material misstatements and group pleading does not apply. See *Howard v. Everex Sys., Inc.*, 228 F.3d 1057, 1061–62 (9th Cir. 2000) (discussing the importance of holding signers of SEC documents responsible for the statements they sign).

By any account, the breadth of the group pleading doctrine has been congressionally and judicially limited over the last two decades.<sup>7</sup> When Congress passed the PSLRA, which specifically enacted heightened pleading standards for securities fraud, many courts insisted that Congress intended to abrogate the group pleading doctrine.<sup>8</sup> Those courts reasoned that the heightened pleading standards were passed to deter unmeritorious litigation, and the use of group pleading subverted those goals.<sup>9</sup> At the same time, a line of Supreme Court cases narrowly defined the implied right of action under Rule 10b-5,<sup>10</sup> promulgated under section 10(b) of the Securities Exchange Act of 1934 (1934 Act).<sup>11</sup> Nevertheless, despite the congressional and judicial decisions, some courts persisted in allowing plaintiffs to rely on the group pleading doctrine.<sup>12</sup>

In June 2011, the Supreme Court decided *Janus Capital Group, Inc. v. First Derivative Traders*.<sup>13</sup> The Court held that “[f]or purposes of Rule 10b-5, the maker of a statement is the person or entity *with ultimate authority over the statement*, including its content and whether and how to communicate it.”<sup>14</sup> In doing so, the Court effectively absolved parties from primary liability under section 10(b) for statements they may have been responsible for if they were not the ones who ultimately made the statement.<sup>15</sup>

In a general sense, *Janus* was troubling because it further reduced access to federal courts for violations of federal securities laws.<sup>16</sup> In particular, though, some courts interpreted *Janus* as abrogating the group pleading doctrine, which could undermine plaintiffs’ ability to bring claims against corporate insiders.<sup>17</sup> Even though the Court did not specifically mention the group pleading doctrine, many argue that the presumption of attribution to corporate insiders may no

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<sup>7</sup> See, e.g., Incandela, *supra* note 1, at 945-49 (highlighting changes after the PSLRA’s passage and the Supreme Court’s response that further weakened private rights of action).

<sup>8</sup> See *infra* note 40.

<sup>9</sup> See *In re New Century*, 588 F. Supp. 2d 1206, 1224 (C.D. Cal. 2008).

<sup>10</sup> 17 C.F.R. § 240.10b-5 (2013).

<sup>11</sup> 15 U.S.C. § 78j(b) (2012). In 1994, the Court held that Rule 10b-5’s private right of action does not apply to aiders and abettors who may contribute to making a misstatement but who do not ultimately make the statement. *Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 180 (1994). The Court went further in *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 165 (2008), which held that courts will give “narrow dimensions . . . to a right . . . Congress did not authorize when it first enacted the statute and did not expand when it revisited the law.”

<sup>12</sup> See *infra* note 40.

<sup>13</sup> 131 S. Ct. 2296 (2011).

<sup>14</sup> *Id.* at 2302 (emphasis added).

<sup>15</sup> *Id.* at 2303 (noting that construing Rule 10b-5(b) to mean “to create” “fails to capture its meaning when directed at an object expressing the action of a verb”).

<sup>16</sup> See Incandela, *supra* note 1, at 949.

<sup>17</sup> See Howard Schiffman, *The Relationship Between the Investment Adviser and the Mutual Fund: Too Close for Comfort*, 45 *FORDHAM L. REV.* 183, 183 (1976).

longer be viable because, “[w]ithout control, a person or entity can merely suggest what to say, not ‘make’ a statement in its own right. One who prepares or publishes a statement on behalf of another is not its maker.”<sup>18</sup> However, interpreting the majority’s decision in *Janus* as abrogating the group pleading doctrine is incorrect. Such an interpretation is contrary to the purpose of the federal securities laws, as well as the PSLRA, and would ultimately make bad public policy. As Justice Stephen Breyer points out in his dissent, this can cause gaps in liability when a company’s board of directors has guilty intent but the same company’s executives carry out the actions.<sup>19</sup> Even assuming that Congress and the Supreme Court intended to give Rule 10b-5 claims narrow construction, the application of the group pleading doctrine to corporate insiders involved in the day-to-day activities of a corporation is not contradictory to that intent.

Part I of this Note explores the history of the group pleading doctrine, including its application before and after Congress enacted the PSLRA, as well as the different approaches the circuit courts have taken in determining whether it survives. Part II recounts the Supreme Court’s decision in *Janus* and explores the modest body of case law that has since arisen. Part III argues that there is a place for the group pleading doctrine post-*Janus*. There is no doubt that the group pleading doctrine’s application is narrower than it was prior to the passage of the PSLRA.<sup>20</sup> After *Janus*, though, the group pleading doctrine can still play an important role in holding corporate insiders liable. Such a rule is consistent with *Janus*, the PSLRA, and public policy.

## I

### THE HISTORY OF GROUP PLEADING

The group pleading doctrine has encountered judicial and congressional hurdles since its inception. The following subparts explore those hurdles and examine the development of the doctrine in the federal courts.

#### A. Before the PSLRA

The group pleading doctrine was created by the judiciary, initially arising in the Ninth and Second Circuits.<sup>21</sup> Even though each circuit

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<sup>18</sup> *Janus*, 131 S. Ct. at 2302.

<sup>19</sup> See *infra* note 102 and accompanying text.

<sup>20</sup> See William O. Fisher, *Don't Call Me a Securities Law Groupie: The Rise and Possible Demise of the "Group Pleading" Protocol in 10b-5 Cases*, 56 BUS. LAW. 991, 1046 (2001).

<sup>21</sup> See *Schwartz v. Celestial Seasonings, Inc.*, 124 F.3d 1246, 1254 (10th Cir. 1997); *Wool v. Tandem Computers Inc.*, 818 F.2d 1433, 1440 (9th Cir. 1987). For a brief summary of the three principal cases that gave rise to the group pleading doctrine in the Second Circuit, see Fisher, *supra* note 20, at 1010–14.

has applied a slightly different version of the doctrine, the Ninth Circuit's enunciation is the best example of the general rule:

In cases of corporate fraud where the false or misleading information is conveyed in prospectuses, registration statements, annual reports, press releases, or other "group-published information," it is reasonable to presume that these are the collective actions of the officers. Under such circumstances, a plaintiff fulfills the particularity requirement of Rule 9(b) by pleading the misrepresentations with particularity and where possible the roles of the individual defendants in the misrepresentations.<sup>22</sup>

Both the Second and Ninth Circuits extended the application of the group pleading doctrine to representatives other than corporate officers. The Ninth Circuit, for example, applied the doctrine to all inside directors,<sup>23</sup> as well as outside directors that participated in day-to-day corporate activities or had a special relationship with the corporation.<sup>24</sup> However, relying on the "day-to-day involvement" standard, the court refused to extend the group pleading doctrine to include outside advisers, underwriters, or large shareholders.<sup>25</sup>

Other circuits also recognized the application of the group pleading doctrine. In *Schwartz v. Celestial Seasonings, Inc.*, the Tenth Circuit held that "[i]dentifying the individual sources of statements is unnecessary when the fraud allegations arise from misstatements or omissions in group-published documents such as annual reports, which presumably involve collective actions of corporate directors or officers."<sup>26</sup> Other courts, although never directly addressing the issue, implicitly applied the group pleading doctrine.<sup>27</sup> Despite differences in the exact breadth of the group pleading doctrine, such as to which

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<sup>22</sup> *Wool*, 818 F.2d at 1440 (citations omitted).

<sup>23</sup> See *Blake v. Dierdorff*, 856 F.2d 1365, 1369 (9th Cir. 1988) ("[P]resumption of collective action when there is misleading 'group published information' is equally applicable to members of a board of directors . . .").

<sup>24</sup> See *In re GlenFed, Inc. Sec. Litig.*, 60 F.3d 591, 593 (9th Cir. 1995).

<sup>25</sup> See *Moore v. Kayport Package Express, Inc.*, 885 F.2d 531, 539-41 (9th Cir. 1989) (outside advisors); *Fisher*, *supra* note 20, at 1000 n.35 (underwriters); *id.* at 1001 n.36 (large shareholders and venture capitalists). Rather than looking at a defendant's day-to-day activity to determine liability, the Second Circuit relied on a defendant's status as an "insider." See, e.g., *Friedman v. Treasure Island N.V.*, No. 90 Civ. 2882 (PKL), 1992 WL 111371, at \*6 (S.D.N.Y. May 4, 1992) (stating that plaintiffs did not need to show a connection between defendants and alleged misstatements because almost all defendants were insiders or affiliates); *Pellman v. Cinerama, Inc.*, 503 F. Supp. 107, 108, 111 (S.D.N.Y. 1980) (noting that all defendants were insiders).

<sup>26</sup> 124 F.3d 1246, 1254 (10th Cir. 1997). Although the decision date of this case is after the passage of the PSLRA, the case was brought prior to enactment. The Tenth Circuit has not decided the viability of the group pleading doctrine post-PSLRA.

<sup>27</sup> See, e.g., *Ballan v. Upjohn Co.*, 814 F. Supp. 1375, 1387 (W.D. Mich. 1992) (holding that defendants were properly named in the securities fraud claim because they all signed internal company documents, reports, and other information and attended management and board meetings).

corporate figures or documents it applied,<sup>28</sup> the general rule remained the same: where a representative was directly involved in the management of a corporation, that representative's involvement in the creation of a corporate document was presumed.<sup>29</sup>

The Supreme Court's decision in *Central Bank v. First Interstate Bank*<sup>30</sup> was the first in a line of cases to raise doubts about the viability of the group pleading doctrine.<sup>31</sup> In *Central Bank*, the Court held that there could be no aiding and abetting liability in Rule 10b-5 actions.<sup>32</sup> The Court's holding raised doubts about group pleading because it clouded the divide between corporate insiders who made material misstatements, as required under Rule 10b-5, and corporate insiders who merely aided in the creation of material misstatements. The holding in *Central Bank* and its impact on the group pleading doctrine has been thoroughly analyzed,<sup>33</sup> and subsequent judicial decisions failed to come to a consensus with respect to *Central Bank's* impact on group pleading. Some courts firmly held that group pleading survived *Central Bank*.<sup>34</sup>

Other courts emphasized the important distinction between primary and secondary liability.<sup>35</sup> Prior to *Central Bank*, plaintiffs could

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<sup>28</sup> The district courts are all over the map on this point. *Wool* itself specifically referenced "prospectuses, registration statements, annual reports, [and] press releases." *Wool v. Tandem Computers Inc.*, 818 F.2d 1433, 1440 (9th Cir. 1987); see also *Cosmas v. Hassett*, 886 F.2d 8, 11-13 (2d Cir. 1989) (extending Second Circuit's group pleading rule to cover press releases and SEC filings, as well). Courts went on to find other corporate documents to qualify as group published. See, e.g., *Polar Int'l Brokerage Corp. v. Reeve*, 108 F. Supp. 2d 225, 238 (S.D.N.Y. 2000) (tender offer documents); *Walsh v. Emerson*, No. 88-952-DA, 1989 U.S. Dist. LEXIS 18289, at \*9 (D. Or. Oct. 3, 1989) (offer sheets given to retiring employees).

<sup>29</sup> See, e.g., *Wool*, 818 F.2d at 1440 (discussing instances where it is reasonable to presume actions are the collective actions of a company's officers).

<sup>30</sup> 511 U.S. 164 (1994).

<sup>31</sup> *Id.* at 191-92.

<sup>32</sup> *Id.* at 180.

<sup>33</sup> See Fisher, *supra* note 20, at 1030-47 ("Because *Central Bank* seems to contract the circle of possible securities law defendants and because 'group pleading' permits plaintiffs to place defendants within the circle at least for purposes of a complaint, it is important to consider whether *Central Bank* affects the 'group pleading' authorities."); see also S. Scott Luton, *The Ebb and Flow of Section 10(b) Jurisprudence: An Analysis of Central Bank*, 17 U. ARK. LITTLE ROCK L.J. 45, 46 (1994) (noting the congressional response to *Central Bank* leading to the passage of the PSLRA).

<sup>34</sup> See, e.g., *In re Sunbeam Sec. Litig.*, 89 F. Supp. 2d 1326, 1342 (S.D. Fla. 1999) ("In no way does [*Central Bank*] restrict the ability of a plaintiff to allege primary violations of Section 10(b) against groups of defendants."); *In re Health Mgmt., Inc. Sec. Litig.*, 970 F. Supp. 192, 207-10 (E.D.N.Y. 1997) (holding that group pleading is alive and well post-*Central Bank*); *McDaid v. Sanders*, No. C-95-20750-JW, 1996 WL 241605, at \*2 (N.D. Cal. May 3, 1996) ("The Court does not read *Central Bank* as abolishing group pleading. Rather, *Central Bank* prohibits a private right of action for 'aiding and abetting' liability, a theory not alleged in this case.").

<sup>35</sup> See, e.g., *Shapiro v. Cantor*, 123 F.3d 717, 720-21 & n.2 (2d Cir. 1997) ("In pre-*Central Bank* cases, some courts did not distinguish precisely between primary liability and

include any and all corporate agents in their complaint on the theory that “[i]f the defendant was not a primary violator, he or she might well be an aider and abettor or a co-conspirator.”<sup>36</sup> Because *Central Bank* did not allow for secondary liability under Rule 10b-5 actions, representatives that were not primarily liable could no longer be held secondarily liable and thus were not proper defendants.<sup>37</sup>

Needless to say, the wide range of decisions following *Central Bank* represented the lower courts’ confusion. Indeed, the Court itself appeared to invite legislative action to rectify its holding: “To be sure, aiding and abetting a wrongdoer ought to be actionable in certain instances. The issue, however, is not whether imposing private civil liability on aiders and abettors is good policy but whether aiding and abetting is covered by the statute.”<sup>38</sup> Congress took the Court’s advice and enacted the PSLRA less than a year after the *Central Bank* decision.<sup>39</sup>

## B. After the PSLRA

In the midst of Newt Gingrich’s Contract with America, the Private Securities Litigation and Reform Act of 1995 was passed over Presidential veto.<sup>40</sup> What started out as a bipartisan comprehensive overhaul of liability for securities class actions<sup>41</sup> evolved into legislation that, among other things, raised the pleading standard for plaintiffs to bring securities class actions in federal court.<sup>42</sup> Specifically, the PSLRA required plaintiffs’ complaints to “specify each statement alleged to have been misleading . . . and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with *particularity all facts* on which that belief is formed.”<sup>43</sup>

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aiding and abetting liability.”); *see also* Fisher, *supra* note 20, at 1030–32 (describing the importance of the definition of primary liability after *Central Bank*).

<sup>36</sup> Fisher, *supra* note 20, at 1032.

<sup>37</sup> *Id.*

<sup>38</sup> *Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 177 (1994) (citations omitted).

<sup>39</sup> *See* John W. Avery, *Securities Litigation Reform: The Long and Winding Road to the Private Securities Litigation Reform Act of 1995*, 51 BUS. LAW. 335, 335–36 (1996).

<sup>40</sup> For a history of the passage of the PSLRA, *see generally id.* at 335–53.

<sup>41</sup> *See* Luton, *supra* note 33, at 83–86. Senators Chris Dodd (Democrat) and Pete V. Domenici (Republican) introduced the Private Securities Litigation Reform Act in 1994, prior to the decision in *Central Bank*. *Id.* However, “the Senate Subcommittee on Securities, a subcommittee of the Senate Committee on Banking, Housing, and Urban Affairs, held a hearing concerning the *Central Bank* decision.” *Id.* at 84.

<sup>42</sup> *See* Avery, *supra* note 39, at 357–59 (describing the heightened pleading standards required by the PSLRA); Incandela, *supra* note 1, at 935.

<sup>43</sup> 15 U.S.C. § 78u-4(b)(1)(B) (2012) (emphasis added). The heightened pleading requirement is one of the three specific reasons that President Clinton pointed to when vetoing the legislation: “I am returning herewith without my approval H.R. 1058, the ‘Private Securities Litigation Reform Act of 1995 . . . . I am not . . . willing to sign legislation



While Congress debated the PSLRA, commentators were already predicting the end of the group pleading doctrine because of the particularity pleading requirement.<sup>44</sup> The judicial response reflected those commentators' predictions. Courts that refused to reject the group pleading doctrine in light of the Supreme Court's decision in *Central Bank*<sup>45</sup> showed no such reluctance after the passage of the PSLRA.

The Fifth Circuit was the first circuit to explicitly to reject the group pleading doctrine after the PSLRA.<sup>46</sup> The Third and the Seventh Circuits followed, relying predominantly on the Fifth Circuit's reasoning.<sup>47</sup> The Fifth Circuit found it irrelevant that Congress did not explicitly overrule the group pleading doctrine "because Congress never made this judicial creation law to begin with."<sup>48</sup> The court continued, adding that group pleading doctrine "cannot withstand the PSLRA's specific requirement that the untrue statements or omissions be set forth with particularity as to 'the defendant.'"<sup>49</sup> Because the PSLRA specifically references "*the* defendant," the court concluded that Congress could only have meant for particularity to be required for each and every defendant in a multiple-defendant action.<sup>50</sup> The Fifth Circuit's holding created a very high burden, requiring "specific factual allegations" linking a corporate insider to misstatements in "corporate documents that have no stated author or statements within documents not attributed to any individual."<sup>51</sup>

Two years later in *Makor Issues & Rights, Ltd. v. Tellabs, Inc.*, the Seventh Circuit relied on the Fifth Circuit's decision to abrogate the group pleading doctrine.<sup>52</sup> Finding the Fifth Circuit's reasoning per-

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that will have the effect of closing the courthouse door on investors who have legitimate claims. Those who are the victims of fraud should have recourse in our courts. Unfortunately, changes made in this bill during conference could well prevent that." William J. Clinton, Veto Message for Securities Litigation Reform Act (Dec. 20, 1995), 1995 WL 752715, at \*1.

<sup>44</sup> Luton, *supra* note 33, at 92 ("The Act would impose much stricter pleading standards and would directly overrule Rule 9(b) and the 'group pleading doctrine.'").

<sup>45</sup> See Fisher, *supra* note 20, at 1031-32.

<sup>46</sup> See *Southland Sec. Corp. v. INSpire Ins. Solutions Inc.*, 365 F.3d 353, 365 (5th Cir. 2004) ("[T]he PSLRA requires the plaintiffs to 'distinguish among those they sue and enlighten *each defendant* as to his or her particular part in the alleged fraud.' As such, corporate officers may not be held responsible for unattributed corporate statements solely on the basis of their titles, even if their general level of day-to-day involvement in the corporation's affairs is pleaded.").

<sup>47</sup> See *Winer Family Trust v. Queen*, 503 F.3d 319, 336-37 (3d Cir. 2007); *Makor Issues & Rights, Ltd. v. Tellabs, Inc.*, 437 F.3d 588, 603 (7th Cir. 2006), *rev'd on other grounds*, 551 U.S. 308 (2007).

<sup>48</sup> *Southland*, 365 F.3d at 364.

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

<sup>50</sup> See *id.* at 364-65.

<sup>51</sup> See *id.* at 365.

<sup>52</sup> 437 F.3d 588 (7th Cir. 2006), *rev'd on other grounds*, 551 U.S. 308 (2007).

suasive, the court in *Tellabs* contended that plaintiffs would have to prove each element of securities fraud “with respect to each individual defendant in multiple defendant cases.”<sup>53</sup> One year later, citing the Fifth and the Seventh Circuits, the Third Circuit also rejected the application of the group pleading doctrine.<sup>54</sup> And although the Eleventh Circuit has never explicitly rejected the group pleading doctrine, dicta suggests that it would adopt the Fifth Circuit’s reasoning.<sup>55</sup>

Still, a few circuits either implicitly recognized the continued existence of the group pleading doctrine or explicitly refused to reject its application. The Sixth Circuit, for example, conceded that it had never officially recognized the group pleading doctrine but nevertheless refused to foreclose the possibility of it surviving the PSLRA.<sup>56</sup> Meanwhile, the Second Circuit refused to abrogate the group pleading doctrine, once assuming its continued existence<sup>57</sup> and once vacating the lower court’s dismissal for failure to consider its application.<sup>58</sup>

Other courts had the opportunity to address the viability of the group pleading doctrine after the PSLRA but equivocated on the issue. The First Circuit spoke at great length about the advantages and disadvantages of the group pleading doctrine, but it ultimately decided the case on other grounds.<sup>59</sup> Similarly, the Eight Circuit had an opportunity to address the viability of the group pleading doctrine,

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<sup>53</sup> See *id.* at 603.

<sup>54</sup> See *Winer Family Trust v. Queen*, 503 F.3d 319, 337 (3d Cir. 2007) (“We agree [with the Fifth Circuit] and hold the group pleading doctrine is no longer viable in private securities actions after the enactment of the PSLRA.”).

<sup>55</sup> See *Phillips v. Scientific-Atlanta, Inc.*, 374 F.3d 1015, 1018 (11th Cir. 2004) (“[T]he most plausible reading in light of congressional intent is that a plaintiff, to proceed beyond the pleading stage, must allege facts sufficiently demonstrating each defendant’s state of mind regarding his or her alleged violations.”).

<sup>56</sup> See *City of Monroe Emps. Ret. Sys. v. Bridgestone Corp.*, 399 F.3d 651, 690 (6th Cir. 2005) (“We need not decide here the current viability of the group-published doctrine because resolution of that question is not required to decide this case.”). The Sixth Circuit also recognized that even its own districts disagreed upon the applicability of the group pleading doctrine, with some of them continuing to apply it. *Id.*

<sup>57</sup> See *Yung v. Lee*, 160 F. App’x 37, 42 (2d Cir. 2005) (“Assuming *arguendo* that the group pleading doctrine survives the strict pleading requirements [of the PSLRA] . . .”).

<sup>58</sup> See *Ill. State Bd. of Inv. v. Authentidate Holding Corp.*, 369 F. App’x 260, 266 (2d Cir. 2010) (“Because the district court did not address the individual defendants’ liability under . . . the group pleading doctrine, we vacate and remand . . .”).

<sup>59</sup> See *Miss. Pub. Emps.’ Ret. Sys. v. Bos. Scientific Corp.*, 523 F.3d 75, 93 (1st Cir. 2008) (declining to decide in the first instance whether the group pleading doctrine survived the PSLRA and holding that the “questions should be resolved in the first instance by the district court”); *In re Cabletron Sys., Inc.*, 311 F.3d 11, 40 (1st Cir. 2002) (“For purposes of this opinion, we will set the issue aside without deciding it, because we determine without reference to the group pleading presumption whether the complaint states a claim against each defendant.”).

but also chose to decide the case on other grounds.<sup>60</sup> Meanwhile, the Tenth Circuit has yet to address the issue.<sup>61</sup>

The indecision and conflicting rulings by the several circuits led to inconsistent results below. Many lower courts continued to allow plaintiffs to circumvent the strict requirements of the PSLRA via the group pleading doctrine.<sup>62</sup> Conversely, there were a number of lower courts within undecided circuits that rejected the application of the group pleading doctrine.<sup>63</sup> Needless to say, courts had trouble interpreting the pleading standards of the PSLRA<sup>64</sup> and determining whether those standards signaled the demise of the group pleading doctrine.

One of the Supreme Court's last words on the scope of Rule 10b-5 claims was in *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*<sup>65</sup> There, the Court made it clear that lower courts should give "narrow dimensions . . . to a right . . . Congress did not authorize when it first enacted the [1934 Act] and did not expand when it revisited the law."<sup>66</sup> Taken literally, courts may have found it even more difficult to argue that the group pleading doctrine was viable. Never-

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<sup>60</sup> *In re Hutchinson Tech., Inc. Sec. Litig.*, 536 F.3d 952, 961 n.6 (8th Cir. 2008) ("[B]ecause we have held that NECA's complaint is insufficient under the PSLRA we need not consider the issue of whether this doctrine survived the PSLRA or whether the doctrine applies here.").

<sup>61</sup> *In Schwartz v. Celestial Seasonings, Inc.*, 124 F.3d 1246, 1254 (10th Cir. 1997), the court held that "[i]dentifying the individual sources of statements is unnecessary when the fraud allegations arise from misstatements or omissions in group-published documents such as annual reports, which presumably involve collective actions of corporate directors or officers." This lawsuit predated the PSLRA, however, and the Tenth Circuit has yet to revisit the issue. *See supra* note 26.

<sup>62</sup> *See, e.g., In re Raytheon Sec. Litig.*, 157 F. Supp. 2d 131, 152-53 (D. Mass. 2001); *In re SmarTalk Teleservices, Inc. Sec. Litig.*, 124 F. Supp. 2d 527, 545 (S.D. Ohio 2000) (holding PSLRA did not abolish group published information rule); *accord In re Baan Co. Sec. Litig.*, 103 F. Supp. 2d 1, 17 (D.D.C. 2000); *In re Oxford Health Plans, Inc., Sec. Litig.*, 187 F.R.D. 133, 142 (S.D.N.Y. 1999); *In re Sunbeam Sec. Litig.*, 89 F. Supp. 2d 1326, 1340-41 (S.D. Fla. 1999); *In re Livent, Inc. Sec. Litig.*, 78 F. Supp. 2d 194, 219 (S.D.N.Y. 1999); *In re BankAmerica Corp. Sec. Litig.*, 78 F. Supp. 2d 976, 987 (E.D. Mo. 1999); *In re Miller Indus., Inc. Sec. Litig.*, 12 F. Supp. 2d 1323, 1329 (N.D. Ga. 1998); *In re Stratosphere Corp.*, 1 F. Supp. 2d 1096, 1107-08 (D. Nev. 1998); *In re Digi Int'l, Inc. Sec. Litig.*, 6 F. Supp. 2d 1089, 1101 (D. Minn. 1998), *aff'd*, 14 F. App'x 714 (8th Cir. 2001); *Powers v. Eichen*, 977 F. Supp. 1031, 1040 (S.D. Cal. 1997); *In re Health Mgmt., Inc. Sec. Litig.*, 970 F. Supp. 192, 208-09 (E.D.N.Y. 1997).

<sup>63</sup> *See, e.g., P. Schoenfeld Asset Mgmt. LLC v. Candant Corp.*, 142 F. Supp. 2d 589, 620-21 (D.N.J. 2001); *In re Miller Indus., Inc. Sec. Litig.*, 12 F. Supp. 2d at 1329-30; *Allison v. Brooktree Corp.*, 999 F. Supp. 1342, 1350 (S.D. Cal. 1998).

<sup>64</sup> *See In re Silicon Graphics Inc. Sec. Litig.*, 183 F.3d 970, 974 (9th Cir. 1999) ("There is widespread disagreement among courts as to the proper interpretation of the PSLRA's heightened pleading requirement."). The Supreme Court clarified the scienter requirements of the PSLRA in *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 323 (2007) ("[I]n determining whether the pleaded facts give rise to a 'strong' inference of scienter, the court must take into account plausible opposing inferences.").

<sup>65</sup> *See* 552 U.S. 148, 165 (2008).

<sup>66</sup> *Id.* at 167.

theless, some courts continued to allow plaintiffs to rely on the group pleading doctrine.<sup>67</sup> And as one court pointed out, “Congress did not expressly prohibit group pleading in the PSLRA.”<sup>68</sup>

## II

### THE FUTURE OF GROUP PLEADING

#### A. *Janus v. First Derivative*

The Supreme Court stepped in to settle the confusion about the interpretation of Rule 10b-5. Janus Capital Group (JCG) was a publicly traded company that created the Janus Investment Fund (JIF), a collection of mutual funds that were managed by JCG and JCG’s wholly owned subsidiary, Janus Capital Management (JCM).<sup>69</sup> Even though the officers of JIF were all officers of JCG, the two entities were sufficiently independent to qualify as separate legal entities.<sup>70</sup> As required by law, JIF periodically released public disclosure documents, including prospectuses.<sup>71</sup> In particular, the prospectuses represented that JIF, through JCM, would refrain from market timing.<sup>72</sup> However, allegations arose that JCM and JCG used market timing,<sup>73</sup> ultimately leading to investors withdrawing significant funds from JIF mutual funds.<sup>74</sup> Because JIF was a major source of revenue for JCG, JCG’s stock price plummeted.<sup>75</sup>

First Derivative Traders, representing the allegedly injured stockholders of JCG, brought a class action against JCG and JCM asserting violations of section 10(b) and Rule 10b-5.<sup>76</sup> Plaintiffs contended that

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<sup>67</sup> See, e.g., *Pa. Ave. Funds v. Inyx Inc.*, 08 CIV. 6857 (PKC), 2010 WL 743562, at \*17 n.3 (S.D.N.Y. Mar. 1, 2010) (“The majority of judges in this district who have addressed the issue have concluded that the group pleading doctrine has survived the PSLRA.”); *In re Thornburg Mortg., Inc. Sec. Litig.*, 695 F. Supp. 2d 1165, 1199 (D.N.M. 2010) (“The Court . . . is not prepared to judicially declare that the PSLRA forbids all instances of group pleading.”).

<sup>68</sup> *Thornburg Mortg.*, 695 F. Supp. 2d at 1199.

<sup>69</sup> *Janus Capital Grp., Inc. v. First Derivative Traders*, 131 S. Ct. 2296, 2299 (2011). Mutual funds are typically managed by the same people who organize their creation. See Schiffman, *supra* note 17, at 183.

<sup>70</sup> See *Janus*, 131 S. Ct. at 2299–300.

<sup>71</sup> See *id.* at 2300.

<sup>72</sup> *Id.* Market timing “involves investors buying or selling mutual fund shares (before the 4 p.m. close of stock trading) at a net asset value that is nonetheless based on stale prices.” See Stephen Choi & Marcel Kahan, *The Market Penalty for Mutual Fund Scandals*, 87 B.U. L. REV. 1021, 1028 (2007). Although market timing is not illegal, it harms the mutual fund because it generates transaction costs that those investors must bear. See *id.* at 1023 n.18, 1028.

<sup>73</sup> The source of the allegation was a complaint that the Attorney General of New York filed against JCG and JCM that became public. See *Janus*, 131 S. Ct. at 2299–300.

<sup>74</sup> See *id.*

<sup>75</sup> See *id.*

<sup>76</sup> The SEC promulgated Rule 10b-5 in 1942 under the catchall antifraud provision, section 10(b) of the Securities Exchange Act. See Eric C. Chaffee, *Standing Under Sec-*

JCG and JCM were ultimately responsible for the misstatements in JIF's prospectuses and that plaintiffs detrimentally relied on those misstatements.<sup>77</sup> The District Court of Maryland dismissed the suit for failing to state a claim, but the Fourth Circuit reversed, holding "that First Derivative had sufficiently alleged that 'JCG and JCM, by participating in the writing and dissemination of the prospectuses, *made* the misleading statements contained in the documents.'" <sup>78</sup> The Supreme Court granted certiorari to decide "whether JCM can be held liable in a private action under Rule 10b-5 for false statements included in Janus Investment Fund's prospectuses."<sup>79</sup>

In a 5–4 decision, Justice Clarence Thomas, writing for the majority, held that JCM could not be liable for false statements in JIF's prospectuses because JCM did not *make* the material misstatement for purposes of Rule 10b-5 claims.<sup>80</sup> Relying on the contemporary dictionary definition of "to make,"<sup>81</sup> Justice Thomas held that "[w]hen 'make' is paired with a noun expressing the action of a verb, the resulting phrase is 'approximately equivalent in sense' to that verb."<sup>82</sup> Therefore, Justice Thomas reasoned, the phrase in Rule 10b-5(b), "[t]o make any . . . statement," was the equivalent of "to state."<sup>83</sup> With this statutory interpretation in hand, Justice Thomas concluded that "the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it."<sup>84</sup> Justice Thomas relied on an analogy of the relationship between a speechwriter and a speaker, stating that only the ultimate maker of the misstatement (the speaker) can be liable for

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*tion 10(b) and Rule 10b-5: The Continued Validity of the Forced Seller Exception to the Purchaser-Seller Requirement*, 11 U. PA. J. BUS. L. 843, 852 (2009). To succeed on a claim brought under Rule 10b-5, a plaintiff must prove "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation." *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 157 (2008).

<sup>77</sup> See *Janus*, 131 S. Ct. at 2300–01. Plaintiffs also contended that JCG and JCM should be liable as controlling persons under section 20(a) of the Act. *Id.*

<sup>78</sup> *Id.* at 2301 (quoting *In re Mutual Funds Inv. Litig.*, 566 F.3d 111, 121 (2009)) (emphasis in original). For a more detailed analysis of the lower court decisions, see *Incandela*, *supra* note 1, at 966–70.

<sup>79</sup> *Janus*, 131 S. Ct. at 2301.

<sup>80</sup> See *id.* at 2305.

<sup>81</sup> Justice Thomas is known to consult period dictionaries to determine the meaning of words in their original context. See Gregory E. Maggs, *Which Original Meaning of the Constitution Matters to Justice Thomas?*, 4 N.Y.U. J.L. & LIBERTY 494, 505 (2009). In this case, Justice Thomas consulted the Oxford English Dictionary published in 1933. See *Janus*, 131 S. Ct. at 2302.

<sup>82</sup> See *Janus*, 131 S. Ct. at 2302.

<sup>83</sup> *Id.*

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

what another (the speechwriter) creates.<sup>85</sup> Despite the managerial and investment services JCM and JCG provided to JIF, and their substantial aid that went into creating the prospectuses, the Court refused to extend liability because plaintiffs failed to allege that JCM was the party with ultimate authority over the statements at issue.<sup>86</sup>

Justice Thomas grounded his interpretation in preceding case law and policy. He argued that the holding was a natural successor to *Central Bank* and *Stoneridge*: that ultimate authority is required for claims of primary liability to distinguish them from claims of secondary liability under section 20(a) of the 1934 Act.<sup>87</sup> Furthermore, holding JCM liable for statements by JIF would inappropriately disregard the corporate formalities observed by the two legal entities.<sup>88</sup> Because JIF and JCM met the minimum statutory requirements to ensure separateness, to hold one liable for the other's actions would render the laws allowing separateness meaningless.<sup>89</sup> In particular, Justice Thomas pointed to the statutory obligation to file a prospectus, a task that was required of JIF, not JCM.<sup>90</sup> Even if JCM assisted in preparing JIF's prospectus, Justice Thomas stated, such assistance "does not mean that JCM 'made' any statements in the prospectuses."<sup>91</sup>

Writing for a four-Justice dissent, Justice Stephen Breyer argued that JCM could be responsible for having made the false misstatements, even if JIF ultimately made the misstatements.<sup>92</sup> Justice Breyer raised several arguments against the majority's conclusion.<sup>93</sup> Most significantly, Justice Breyer did not believe that the person who "makes" a misstatement must have ultimate authority over the statement.<sup>94</sup> There can be a deviation, according to Justice Breyer, between the party who makes a misstatement and the party with ultimate authority over it, such as when "cabinet officials make statements about matters

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<sup>85</sup> See *id.* ("Even when a speechwriter drafts a speech, the content is entirely within the control of the person who delivers it. And it is the speaker who takes credit—or blame—for what is ultimately said.").

<sup>86</sup> See *id.*

<sup>87</sup> See *id.* at 2302–03.

<sup>88</sup> See *id.* at 2304. In addition, it is typical practice for the investment advisors to be elected to the board of directors of the fund. See Schiffman, *supra* note 17, at 183.

<sup>89</sup> See *Janus*, 131 S. Ct. at 2304.

<sup>90</sup> See *id.* A mutual fund, as the issuer of securities, is required to deliver a prospectus that complies with section 10 of the Securities Exchange Act prior to the sale of securities. See Securities Act of 1933 (1933 Act) § 5, 15 U.S.C. § 77e (2012).

<sup>91</sup> *Janus*, 131 S. Ct. at 2305.

<sup>92</sup> See *id.* at 2305–12 (Breyer, J., dissenting).

<sup>93</sup> With respect to Justice Breyer's argument against the majority, it is important to note that Justice Breyer believed that the majority confused primary and secondary liability under the 1934 Act when coming to its conclusion. See *id.* at 2306–09; see also Justin Marocco, Comment, *When Will It Finally End: The Effectiveness of the Rule 10b-5 Private Action as a Fraud-Deterrence Mechanism Post-Janus*, 73 LA. L. REV. 633, 647 (2013) ("Additionally, the dissent asserted that the majority incorrectly relied on *Central Bank* and *Stoneridge*.").

<sup>94</sup> See *Janus*, 131 S. Ct. at 2307.

that the Constitution places within the ultimate authority of the President.”<sup>95</sup>

Further, Justice Breyer did not think that the English language prevented several different individuals from collectively making a statement, either separately or together, so long as they were all complicit in producing such a statement.<sup>96</sup> Rather than relying on simply equating “ultimate authority” with “making a misstatement,” Justice Breyer concluded that “[p]ractical matters related to context, including control, participation, and relevant audience, help determine who ‘makes’ a statement and to whom that statement may properly be ‘attributed,’ at least as far as ordinary English is concerned.”<sup>97</sup>

Justice Breyer went on to examine the interplay between section 10(b)—primary liability under which Rule 10b-5 is promulgated—and 20(a)—secondary liability.<sup>98</sup> While Justice Thomas posited that the *Janus* rule was necessary to avoid a broader application of primary liability than secondary liability, Justice Breyer countered that any remedy under the securities law, section 20(a) included, would not prevent a claim under section 10(b).<sup>99</sup>

Rather than being alarmed by the overlap of the two claims, Justice Breyer was concerned with the potential loophole created by the majority’s interpretation of Rule 10b-5. In particular, Justice Breyer argued that “there is at least one significant category of cases that § 10(b) may address that derivative forms of liability, such as under § 20(a), cannot, namely, cases in which one actor exploits another as an innocent intermediary for its misstatements.”<sup>100</sup> If, for example, JIF’s board of trustees knew nothing about the misstatements in the prospectuses, then section 20(a) would not apply. Nor would the

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<sup>95</sup> *Id.* More relevant to the analysis, Justice Breyer states that “a management company, a board of trustees, individual company officers, or others, separately or together, might ‘make’ statements contained in a firm’s prospectus—even if a board of directors has ultimate content-related responsibility.” *Id.* at 2306.

<sup>96</sup> *See id.* at 2307.

<sup>97</sup> *Id.* (citations omitted).

<sup>98</sup> *See id.* at 2310.

<sup>99</sup> *See id.* at 2310. Section 20(a) reads: “Every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable . . . .” 15 U.S.C. § 78t(a) (2012). Justice Thomas was of the belief that any interpretation of the words “to make” that includes those persons who do not have ultimate authority of the statements would necessarily create double liability and, thus, a redundancy in the statutory code. *See Janus*, 131 S. Ct. at 2304 (majority opinion). Justice Breyer, however, believed that it was better to have some overlap of the two remedies rather than to leave some plaintiffs without a remedy under either sections 10(b) or 20(a). *Id.* at 2310 (Breyer, J., dissenting).

<sup>100</sup> *Janus*, 131 S. Ct. at 2310.

board of trustees be liable under Rule 10b-5, since it was unaware of the misstatements.<sup>101</sup> Justice Breyer wrote:

The possibility of guilty management and innocent board is the 13th stroke of the new rule's clock. What is to happen when guilty management writes a prospectus (for the board) containing materially false statements and fools both board and public into believing they are true? Apparently under the majority's rule, in such circumstances *no one* could be found to have "ma[d]e" a materially false statement . . . .<sup>102</sup>

If no one can be found to have made the misstatement, Justice Breyer continued, then no one could be held principally liable for it, and consequently, other parties would escape secondary liability.<sup>103</sup>

### B. In the Aftermath of *Janus*

The most telling part of the majority opinion is its analogy to the speechwriter and the speaker.<sup>104</sup> Although the analogy is simple enough to understand, one is left with more questions than answers when applying it to traditional Rule 10b-5 claims. Since the speaker is the only person who may be held liable for any material misstatements that the speech contains, how does a court decide who is liable for a corporate document that does not indicate the identity of the speaker? Furthermore, how is a plaintiff supposed to find out which corporate representative *made* the misstatement contained in the corporate document if the plaintiff is not entitled to discovery until after pleading with particularity the details of every element of the fraud?<sup>105</sup>

The Supreme Court never explicitly addressed the group pleading doctrine in *Janus*. By holding that liability could only be imposed upon the actual speaker of a misstatement, though, many district courts concluded that the group pleading doctrine was no longer viable because only one person, the speaker, could be liable for material misstatements.<sup>106</sup> Still, other courts have merely questioned the

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<sup>101</sup> As previously discussed, one of elements of a Rule 10b-5 claim is scienter, a defendant's knowledge of the fraud. *See Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 157 (2008); Chaffee, *supra* note 76, at 852.

<sup>102</sup> *Janus*, 131 S. Ct. at 2310.

<sup>103</sup> *Id.* Prosecuting a party for aiding and abetting requires a primary violator. *See id.* (citing *SEC v. DiBella*, 587 F.3d 553, 566 (2d Cir. 2009)).

<sup>104</sup> *Id.* at 2302 (majority opinion).

<sup>105</sup> *See* 15 U.S.C. §§ 77z-1(b)(1), 78u-4(b)(3)(B) (2012) (discussing stays on discovery relating to motions to dismiss).

<sup>106</sup> *See, e.g., In re UBS AG Sec. Litig.*, No. 07 Civ. 11225(RJS), 2012 WL 4471265, at \*10 (S.D.N.Y. Sept. 28, 2012) (holding that the group pleading doctrine does not survive *Janus*); *see also In re Am. Apparel, Inc. S'holder Litig.*, No. CV 10-06352 MMM (JCGX), 2013 WL 174119, at \*26 (C.D. Cal. Jan. 16, 2013) (dismissing certain claims against a company's CEO and CFO but allowing plaintiff to amend "to state a viable claim against them outside the group pleading doctrine").



group pleading doctrine's validity,<sup>107</sup> while some courts continue to apply the group pleading doctrine.<sup>108</sup>

### III

#### THE GROUP PLEADING DOCTRINE AND CORPORATE INSIDERS

Without a doubt, *Janus* forecloses the application of the group pleading doctrine to executives of one corporation for the misstatements of a different corporation. This Note does not attempt to argue that *Janus* was wrongly decided; that argument has been made elsewhere.<sup>109</sup> This Part argues that there is still a place for the group pleading doctrine to ensure that corporate insiders are held liable for misstatements made by *their* corporation. This application of the group pleading doctrine is consistent with its original use, with the Court's holding in *Janus*, and with Congress's intent under the PSLRA.

In subpart A, I argue that it is not enough simply to cite to *Janus* for the proposition that the group pleading doctrine has been rejected. The group pleading doctrine is still viable in situations where

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<sup>107</sup> See, e.g., *Orlan v. Spongetech Delivery Sys., Inc.*, Sec. Litig., Nos. 10-CV-4093 (DLI) (JMA), 10-CV-4104 (DLI) (JMA), 2012 WL 1067975, at \*10 (E.D.N.Y. Mar. 29, 2012) (questioning without deciding the viability of the group pleading doctrine); *In re Optimal U.S. Litig.*, 837 F. Supp. 2d 244, 262–64 (S.D.N.Y. 2011) (noting that the case does not concern the group pleading doctrine for a federal securities law); *Rolin v. Spartan Mullen Et Cie, S.A.*, No. 10 Civ. 1586(CM)(FM), 2011 WL 5920931, at \*5 (S.D.N.Y. Nov. 23, 2011) (discussing whether *Janus* abrogates the group pleading doctrine is an open question); *Haw. Ironworkers Annuity Trust Fund v. Cole*, No. 3:10CV371, 2011 WL 3862206, at \*3 (N.D. Ohio Sept. 1, 2011) (holding that the requirements of particularity in *Janus* apply to corporate insiders);

<sup>108</sup> See, e.g., *In re Satyam Computer Servs. Ltd.* Sec. Litig., 915 F. Supp. 2d 450, 477 (S.D.N.Y. 2013) (acknowledging and agreeing with plaintiffs' choice to use the group pleading doctrine); *City of Pontiac Gen. Emps.' Ret. Sys. v. Lockheed Martin Corp.*, 875 F. Supp. 2d 359, 373–74 (S.D.N.Y. 2012) (agreeing that the group pleading doctrine is alive and well); *Warchol v. Green Mountain Coffee Roasters, Inc.*, No. 2:10-CV-227, 2012 WL 256099, at \*1, \*5 n.9 (D. Vt. Jan. 27, 2012) (noting that the group pleading doctrine is the majority rule in the Southern District of New York); *In re St. Jude Med., Inc.* Sec. Litig., 836 F. Supp. 2d 878, 906 n.11 (D. Minn. 2011) (noting that the group pleading doctrine might be sufficient to hold the defendants accountable); *Murdeswar v. Search Media Holdings Ltd.*, No. 11-CIV-20549, 2011 WL 7704347, at \*12 (S.D. Fla. Aug. 8, 2011) (noting that the Pre-Merger Statements are attributable to defendants because of the group pleading doctrine); see also *In re Coinstar Inc.* Sec. Litig., No. C11-133 MJP, 2011 WL 4712206, at \*10–11 (W.D. Wash. Oct. 6, 2011) (endorsing the survival of the group pleading doctrine implicitly by finding it inapplicable to the particular case at issue).

<sup>109</sup> See, e.g., Zachary K. Ostro, *Janus Capital Group, Inc. v. First Derivative Traders: Further Limiting Limited Liability, and Missing an Opportunity to Curb Corporate Misconduct*, 8 J. BUS. & TECH. L. 275, 312 (2013) ("The Court's holding in *Janus Capital Group, Inc. v. First Derivative Traders* was a three-part failure."); James D. Redwood, *To Make or to Mar: The Supreme Court Turns Away Another Securities Law Plaintiff*, 14 U. PA. J. BUS. L. 463, 513 (2012) ("The Court's willful slighting of the actual meaning of the word 'make,' and its activist substitution of an artificial test of 'ultimate authority' or 'control' for a reasonable definition of the word, without any precedent to back up its approach, were unfounded measures which the facts did not justify.").

corporate insiders are being held liable for misstatements by their corporate employers. *Janus* is a different case factually, and the concerns expressed by Justice Thomas in *Janus* do not apply when the group pleading doctrine is applied to corporate insiders.<sup>110</sup> Indeed, all that is required is a finding that the corporate insider has “ultimate authority” over the misstatement. Therefore, in subpart B, I argue that multiple corporate insiders could and generally do have ultimate authority over the misstatements of their corporation. Since *Janus* has

no bearing on how corporate officers who work together in the *same* entity can be held jointly responsible on a theory of primary liability[,] [i]t is not inconsistent with *Janus Capital* to presume that multiple people in a single corporation have the joint authority to “make” an SEC filing, such that a misstatement has more than one “maker.”<sup>111</sup>

Finally, in subpart C, I argue that this interpretation is not inconsistent with Congress’s intent in passing the PSLRA. Even though Congress intended to prevent frivolous lawsuits under the federal securities laws, ensuring corporate insiders do not escape liability altogether is not at odds with that goal.

#### A. Application of *Janus* to Corporate Insiders

Since *Janus*, several courts have simply cited to *Janus* for the proposition that the group pleading doctrine is not viable in light of that decision. This oversimplifies the rule derived from *Janus*. Not only does the factual predicate for the Court’s decision differ from the traditional group pleading doctrine application, but the policy concerns expressed by the majority opinion are not relevant in those traditional applications.

##### 1. *Factual Circumstances of Janus*

Prior to *Janus*, lower courts predominantly applied the group pleading doctrine in cases where plaintiffs were attempting to attribute a corporation’s actions to its own insiders.<sup>112</sup> *Janus* provides very little guidance on these traditional cases because *Janus* involved entirely different factual circumstances: a plaintiff attempting to attri-

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<sup>110</sup> *But see Janus Capital Grp., Inc. v. First Derivative Traders*, 131 S. Ct. 2296, 2310 (2011) (Breyer, J., dissenting) (noting that Justice Thomas’s holding applies to corporate insiders).

<sup>111</sup> *City of Pontiac*, 875 F. Supp. 2d at 374 (emphasis added).

<sup>112</sup> *See, e.g., In re Raytheon Sec. Litig.*, 157 F. Supp. 2d 131, 137 (D. Mass. 2001) (attempting to attribute corporation’s actions to its CEO and CFO, among others); *In re SmarTalk Teleservices, Inc. Sec. Litig.*, 124 F. Supp. 2d 527, 545 (S.D. Ohio 2000) (attempting to attribute corporation’s actions to its executive vice president, among others); *In re Livent, Inc. Sec. Litig.*, 78 F. Supp. 2d 194, 219 (S.D.N.Y. 1999) (attempting to attribute corporation’s actions to its CEO and other executives).

bute misstatements by one corporation to the corporate insiders of another corporation.<sup>113</sup>

The plaintiffs in *Janus* would not have been able to rely on the group pleading doctrine to assert JCF's liability for misstatements in JIF's prospectuses. After all, the majority explicitly found that the two corporations were independent of one another.<sup>114</sup> Because the group pleading doctrine only creates a presumption of involvement, that presumption would not be appropriate in a case where the corporate agent is not an agent involved in the day-to-day activities of the company that released the misstatement.<sup>115</sup> Rather, it is more sensible to presume that a corporate insider is only involved in his own corporation's activities.

## 2. *Respecting Business Formalities*

In addition to the factual differences mentioned above, investors like the ones in *Janus* have the benefit of other legal protections available to them. Unlike investors who traditionally rely on group pleading, investors like the ones in *Janus* have the protection of the "piercing the corporate veil" doctrine.<sup>116</sup> However, Justice Thomas held that JIF and JCM observed the corporate formalities and were wholly independent, thereby foreclosing any veil-piercing argument.<sup>117</sup> Justice Thomas stated,

Although First Derivative and its *amici* persuasively argue that investment advisers exercise significant influence over their client funds, it is undisputed that the corporate formalities were observed here. . . . Any reapportionment of liability in the securities industry

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<sup>113</sup> See *Janus*, 131 S. Ct. at 2299–301 (2011) (majority opinion); *supra* notes 69–76 and accompanying text.

<sup>114</sup> *Janus*, 131 S. Ct. at 2304.

<sup>115</sup> See *In re GlenFed, Inc. Sec. Litig.*, 60 F.3d 591, 593 (9th Cir. 1995); *Blake v. Dierdorff*, 856 F.2d 1365, 1369 (9th Cir. 1988) (noting that "presumption of collective action when there is misleading 'group published information' is equally applicable to members of a board of directors"); *supra* text accompanying notes 23–25.

<sup>116</sup> The concept of piercing the corporate veil "is among the most confusing in corporate law." Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89, 89 (1985). Although states frame their veil-piercing doctrines in terms of equitable relief, the simplest enunciation of veil piercing is that courts will forgo a corporation's limited liability where there is evidence that the corporation is merely an instrumentality for transacting another's affairs. See, e.g., *In re Payroll Express Corp.*, 216 B.R. 344, 361 (S.D.N.Y. 1997), *aff'd*, 186 F.3d 196 (2d Cir. 1999) (applying New Jersey "alter ego" doctrine); *Vill. at Camelback Prop. Owners Ass'n v. Carr*, 538 A.2d 528, 532–34 (Pa. Super. Ct. 1988) ("We have said that whenever one in control of a corporation uses that control . . . to further his or her own personal interests, the fiction of the separate corporate identity may properly be disregarded." (quoting *Ashley v. Ashley*, 393 A.2d 637, 641 (Pa. 1978))), *aff'd*, 572 A.2d 1 (Pa. 1990).

<sup>117</sup> *Janus*, 131 S. Ct. at 2304 ("JCM and Janus Investment Fund remain legally separate entities, and Janus Investment Fund's board of trustees was more independent than the statute requires.").

in light of the close relationship between investment advisers and mutual funds is properly the responsibility of Congress and not the courts.<sup>118</sup>

Application of the group pleading doctrine in *Janus* would require a court to disregard JCM's independence from JIF, resulting in an unacceptable inconsistency between veil-piercing and group pleading. That is, it would be counterintuitive to say that JCM did not exhibit sufficient control over JIF for the court to pierce the corporate veil<sup>119</sup> but did exhibit sufficient control to presume that JCM made the misstatements for purposes of group pleading.<sup>120</sup>

The same concerns of contradiction do not arise when the group pleading doctrine is used to hold corporate agents liable for statements by their own corporation. Courts use veil piercing to reach the owners of the corporation, not its directors or executives.<sup>121</sup> Therefore, investors cannot rely on veil piercing to reach corporate agents that are not controlling owners of the corporation for which they work. Instead, investors generally must rely on derivative suits, which require particularity pleading under Rule 9(b) of the Federal Rules of Civil Procedure.<sup>122</sup> These stringent pleading requirements were the reason that group pleading was created in the first place.<sup>123</sup>

### 3. Reporting Obligations

Last, Justice Thomas relied on JIF's statutory obligation to file a prospectus to distinguish JIF's liability from that of JCM.<sup>124</sup> There is no such distinction in the traditional application of the group pleading doctrine because the corporate insiders work for the same company that files prospectuses with the SEC. Further, it is those corporate insiders who are ultimately responsible for the corpora-

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<sup>118</sup> *Id.* (citation omitted).

<sup>119</sup> See generally Douglas G. Smith, *Piercing the Corporate Veil in Regulated Industries*, 2008 BYU L. REV. 1165, 1169–82 (2008) (detailing a number of factors that “courts generally apply . . . none of which by itself is sufficient to establish liability”).

<sup>120</sup> It would be odd to say that JCM was both in control and not in control of JIF at the same time for two different purposes. See *Janus*, 131 S. Ct. at 2301–05.

<sup>121</sup> See generally Robert Charles Clark, *The Duties of the Corporate Debtor to Its Creditors*, 90 HARV. L. REV. 505, 541 (1977) (“subjecting to corporate liabilities the personal assets directly held by shareholders” when piercing the corporate veil); Mark J. Loewenstein, *Veil Piercing to Non-Owners: A Practical and Theoretical Inquiry*, 41 SETON HALL L. REV. 839, 839–40, 852–53 (2011) (noting that the entity owner is the party at risk for liability while the officers are not).

<sup>122</sup> See FED. R. CIV. P. 9(b). Securities laws claims must meet particularity requirements under the PSLRA as well. See *supra* notes 42–44 and accompanying text.

<sup>123</sup> This statement is not intended to prove that group pleading is legally sound. Rather, it is intended to show that group pleading serves an important purpose in its traditional application that is *different* and *unique* from its perceived purpose in a situation like *Janus*. The soundness of group pleading under the PSLRA is discussed *infra* Part III.C.

<sup>124</sup> See *Janus*, 131 S. Ct. at 2304.

tion's filings.<sup>125</sup> In *Janus*, for example, there is no reason why plaintiff investors would not be able to allege violations of Rule 10b-5 by JIF even if the Court refused to find JCM's management liable.<sup>126</sup>

## B. Corporate Insiders and Ultimate Authority

Even if the traditional application of group pleading is inherently different from the facts presented in *Janus*, the Court still provided a concrete standard for Rule 10b-5 liability. To be liable under Rule 10b-5, a corporate insider must have made the misstatement,<sup>127</sup> and the majority in *Janus* defined the maker of the misstatement as "the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it."<sup>128</sup> This, too, can complicate the application of the group pleading doctrine if *Janus* were read to restrict liability to only one person. After all, if only one person may have ultimate authority over a misstatement, then a presumption that several corporate insiders made the misstatement would be inapposite. This subpart aims to show that nothing in the *Janus* opinion suggests that only one person could have ultimate authority over a misstatement. Justice Thomas did not intend such a narrow view, and the statutory language of Rule 10b-5 does not support this narrow view. Further, the fundamental structure of business organizations makes such a reading illogical. Corporate decision making is a complex process, and most statements are not attributable to one person.

### 1. Justice Thomas's Narrow Construction

The *Janus* dissent assumed, without justification, that the majority intended only a single individual or entity to have ultimate authority over a corporate statement.<sup>129</sup> Although Justice Thomas used the sin-

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<sup>125</sup> See, e.g., Form 10-Q, General Instructions G ("At least one complete copy of the report . . . must be manually signed on the registrant's behalf by a duly authorized officer of the registrant and by the principal financial or chief accounting officer of the registrant." (emphasis added)); Form 10-K, General Instructions D (requiring signatures of several executives as well as "at least the majority of the board of directors"). Specifically for prospectuses, section 5 of the 1933 Act prohibits the sale of securities unless a statutory prospectus is filed with the SEC. See 1933 Act, § 5(b), 15 U.S.C. § 77e(b) (2012).

<sup>126</sup> In *Janus*, though, it would have made little sense to bring suit against JIF because JIF was, in all likelihood, bankrupt. See *Janus*, 131 S. Ct. at 2299 ("[JIF] has no assets apart from those owned by the investors.").

<sup>127</sup> Recall that the first element of a Rule 10b-5 claim is a material misrepresentation or omission by the defendant. See *supra* note 76.

<sup>128</sup> *Janus*, 131 S. Ct. at 2302.

<sup>129</sup> See *id.* at 2307 (Breyer, J., dissenting) ("Nothing in the English language prevents one from saying that several different individuals, separately or together, 'make' a statement that each has a hand in producing.").

gular when articulating the Court's rule,<sup>130</sup> nowhere in the opinion did he state that only one person or entity must be ultimately responsible for a statement.

Justice Thomas said that the "statements in the Janus Investment Fund prospectuses were made by Janus Investment Fund, not by JCM."<sup>131</sup> A principal tenet of corporate law, however, is that a corporation can only act through a human representative or agent.<sup>132</sup> To hold a corporation liable for a claim under Rule 10b-5 would be in direct conflict with the statutory language, which contemplates only natural persons being liable for untrue statements.<sup>133</sup> Therefore, if anyone would be liable for a violation of Rule 10b-5, it would be one or more of the corporation's agents.

The language of Rule 10b-5 sheds further light on the issue. Rule 10b-5 states that "[i]t shall be unlawful for *any* person . . . [t]o make any untrue statement."<sup>134</sup> The use of the word "any," rather than "a" indicates that more than one person can be liable for an untrue statement. "Any" is defined as "one or some indiscriminately of whatever kind."<sup>135</sup> Although sometimes only one person might be responsible for untrue statements, the dictionary definition of "any" indicates that more than one person may be responsible if they all make the untrue statement.<sup>136</sup> Many courts, including those that have upheld and rejected the application of the group pleading doctrine, have followed this reading of Rule 10b-5 post-*Janus*.<sup>137</sup>

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<sup>130</sup> See *id.* at 2302 (majority opinion) ("For purposes of Rule 10b-5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it.").

<sup>131</sup> *Id.* at 2305.

<sup>132</sup> See *Suez Equity Investors, L.P. v. Toronto-Dominion Bank*, 250 F.3d 87, 101 (2d Cir. 2001).

<sup>133</sup> 17 C.F.R. § 240.10b-5 (2013) ("It shall be unlawful for any *person* . . ." (emphasis added)). Whether a corporation may be liable under Rule 10b-5 is an open question; however, at least one court has held that a corporation may not be liable. See *In re Merck & Co., Inc. Sec., Derivative & "ERISA" Litig.*, Nos. 05-1151 (SRC), 05-2367(SRC), 2011 WL 3444199, at \*25 (D.N.J. Aug. 8, 2011) ("*Janus* does not alter the well-established rule that 'a corporation can act only through its employees and agents.'" (quoting *Suez Equity Investors, L.P. v. Toronto-Dominion Bank*, 250 F.3d 87, 101 (2d. Cir. 2001))).

<sup>134</sup> 17 C.F.R. § 240.10b-5 (emphasis added).

<sup>135</sup> *Any Definition*, MERRIAM-WEBSTER, <http://www.merriam-webster.com/dictionary/any> (last visited Oct. 21, 2013).

<sup>136</sup> See, e.g., *Hammaker v. Brown & Brown, Inc.*, 214 F. Supp. 2d 575, 580 (E.D. Va. 2002) ("The term 'any' is defined as 'one or more.'" (citing WEBSTER'S THIRD NEW INT'L DICTIONARY (1993))); *Alcatel Space, S.A. v. Loral Space & Commc'ns Ltd.*, 154 F. Supp. 2d 570, 578 n.12 (S.D.N.Y. 2001), *aff'd*, 25 F. App'x 83 (2d Cir. 2002) ("'[A]ny' is defined as '[o]ne or some, regardless of sort, quantity or number.'" (citing WEBSTER'S II NEW RIVERSIDE UNIVERSITY DICTIONARY 76, 115 (1994))).

<sup>137</sup> See, e.g., *In re UBS AG Sec. Litig.*, No. 07 Civ. 11225(RJS), 2012 WL 4471265 (S.D.N.Y. Sept. 28, 2012) (holding that "*Janus* might not necessarily imply that there can be only one 'maker' of a statement in the case of express or implicit attribution" (quoting *City of Roseville Emps.' Ret. Sys. v. EnergySolutions, Inc.*, 814 F. Supp. 2d 395, 417 n.9 (S.D.N.Y.

## 2. *Business Organizations and Corporate Decision Making*

Because the majority opinion in *Janus* does not necessarily foreclose the possibility of more than one responsible party, a look at the structure of corporate decision making can help demonstrate that holding multiple corporate insiders liable is more sensible than attempting to attribute corporate statements to one particular individual.

Each state, through its corporate law, allocates decision-making responsibilities within an organization.<sup>138</sup> Generally speaking, management of a business organization is vested in the board of directors,<sup>139</sup> which then delegates and authorizes action to the organization's officers.<sup>140</sup> Since the typical board of directors of a large or medium-sized corporation consists of fifteen board members,<sup>141</sup> almost all high-level decisions will involve board members sharing ultimate authority.

In addition, the Sarbanes-Oxley Act requires “[e]ach principal executive and principal financial officer of [an] issuer, or persons performing similar functions . . . [to] sign a certification” when the corporation releases disclosure reports.<sup>142</sup> Any and all signatories to the certification can be liable under Rule 10b-5 if there is a false statement in the certified form.<sup>143</sup> By its very terms, the Sarbanes-Oxley

2011)) (internal quotation marks omitted)); *City of Roseville*, 814 F. Supp. 2d at 417 (“There is no dispute that [EnergySolutions, Inc.] and each of the Individual Defendants who signed the Registration Statements ‘made’ the statements . . .”).

<sup>138</sup> See, e.g., CAL. CORP. CODE § 300 (West 2012) (“The board may delegate the management of the day-to-day operation of the business of the corporation to a management company or other person provided that the business and affairs of the corporation shall be managed and all corporate powers shall be exercised under the ultimate direction of the board.”); DEL. CODE ANN. tit. 8 § 141(a) (West 2012) (requiring a board of directors to manage a corporation); N.Y. BUS. CORP. LAW § 701 (McKinney 2012) (“[T]he business of a corporation shall be managed under the direction of its board of directors . . .”); see also Wayne O. Hanewicz, *Director Primacy, Omnicare, and the Function of Corporate Law*, 71 TENN. L. REV. 511, 511 (2004) (“[C]orporate law does and should allocate decision-making authority to various institutions, such as the board, the shareholders, and the judiciary, and . . . this decision-making authority ought to be allocated so as to most efficiently advance the ultimate goal of corporate law.”).

<sup>139</sup> See, e.g., MODEL BUS. CORP. ACT § 8.01(b) (4th ed. 2007) (“All corporate powers shall be exercised by or under the authority of the board of directors of the corporation, and the business and affairs of the corporation shall be managed by or under the direction . . . of its board of directors . . .”).

<sup>140</sup> *Id.* § 8.41. Beyond delegating power to management, at least one scholar has suggested that a board of directors may continue to “serve as a source of advice and counsel to the [CEO].” MYLES L. MACE, *DIRECTORS: MYTH AND REALITY* 13–17 (1971) (examining director interviews in which directors claim they serve in an advisory role).

<sup>141</sup> MACE, *supra* note 140, at 10.

<sup>142</sup> 17 C.F.R. § 240.13a-14 (2013). The reports include Form 10-Q, Form 10-K, Form 20-F, and Form 40-F, with a few narrow exceptions. See *id.*

<sup>143</sup> See Marc H. Folladori, *A Practical Overview of the SEC’s Internal Controls and Executive Disclosure Certification Rules*, FULBRIGHT & JAWORSKI L.L.P. LEGAL UPDATE 2–6 (July 26,

Act implicates the possibility of multiple persons with ultimate authority. When both the CEO and CFO certify a statement, as required under Sarbanes-Oxley, and a court determines that it was materially untrue, both can be liable under Rule 10b-5.

The same can be said about joint press releases. Of course, a press statement by just the CEO warrants Rule 10b-5 liability solely for that particular executive. Rationally, the CEO in this scenario, as the sole signatory of the press statement, was the party with ultimate authority over its content.<sup>144</sup> It logically follows that any press statement made by several executive officers should be attributable to any and all of them. The same assumption inheres in this scenario: by becoming signatories to the press release, each and every party had ultimate authority over its contents.

Similarly, boards of directors have consistently been characterized as the “ultimate decisionmaking authority within the firm.”<sup>145</sup> For example, the Delaware General Corporation Law’s default rule places the responsibility of “business and affairs” in the hands of the boards of directors.<sup>146</sup> Corporate codes do not place decision-making power in the hands of one person but in the entire board.<sup>147</sup>

An example of group decision making by a board of directors can be found in committee decisions. One of a board of directors’ responsibilities is to oversee compensation and governance of the corporation.<sup>148</sup> To do this more efficiently, boards delegate certain responsibilities to smaller groups of board members called commit-

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2005), available at [http://www.martindale.com/banking-financial-services/article\\_Fulbright-Jaworski-LLP\\_173006.htm](http://www.martindale.com/banking-financial-services/article_Fulbright-Jaworski-LLP_173006.htm). Any persons who certify a periodic report also open themselves up to criminal liability. See 18 U.S.C. § 1350 (2012).

<sup>144</sup> See SEC v. Carter, No. 10 C 6145, 2011 WL 5980966, at \*2 (N.D. Ill. Nov. 28, 2011).

<sup>145</sup> Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 291 (1999); see JONATHAN R. MACEY, CORPORATE GOVERNANCE: PROMISES KEPT, PROMISES BROKEN 51 (2008) (“Perhaps the most basic principle of corporate law in the United States is that corporations are controlled by boards of directors, rather than shareholders.”); see also *Quickturn Design Sys., Inc. v. Shapiro*, 721 A.2d 1281, 1291 (Del. 1998) (“One of the most basic tenets of Delaware corporate law is that the board of directors has the ultimate responsibility for managing the business and affairs of a corporation.”); John C. Coates IV, *Measuring the Domain of Mediating Hierarchy: How Contestable Are U.S. Public Corporations?*, 24 J. CORP. L. 837, 840 (1999) (“Absent tailored charter provisions, boards of directors of both [public and private] corporations have ultimate legal authority to determine, say, whether to pursue mass layoffs to increase profits.”).

<sup>146</sup> DEL. CODE ANN. tit. 8, § 141 (West 2012).

<sup>147</sup> See *supra* note 138.

<sup>148</sup> See, e.g., Regina F. Burch, *Director Oversight and Monitoring: The Standard of Care and the Standard of Liability Post-Enron*, 6 WYO. L. REV. 481, 517 (2006) (discussing two decisions centering on the board of directors’ duty to oversee CEO compensation); Martin D. Mobley, *Compensation Committee Reports Post-Sarbanes-Oxley: Unimproved Disclosure of Executive Compensation Policies and Practices*, 2005 COLUM. BUS. L. REV. 111, 117 (noting that the board of directors is one of the primary participants in corporate governance).



tees.<sup>149</sup> At a minimum, public corporations have at least three different committees: audit,<sup>150</sup> compensation,<sup>151</sup> and nominating.<sup>152</sup> Each of these committees is responsible for a function related to corporate governance and to ensure that the public receives proper disclosure. When a committee fails to serve its purpose, the members of that committee can be liable for damages that other directors would not be liable for.<sup>153</sup> In *In re Lernout & Hauspie Securities Litigation*,<sup>154</sup> the court found sufficient evidence to hold the members of the audit committee liable for misstatements on a Form 10-K based on the fact that they all signed the Form S-3, which incorporated the fraudulent statements.<sup>155</sup> Just as a CEO and CFO can both be liable for their corporation's untrue statements, multiple committee members can also be liable for statements made by their respective committees.

### C. PSLRA and Corporate Insiders

Even if *Janus's* "ultimate authority" requirement does not preclude the application of the group pleading doctrine to multiple corporate insiders, the PSLRA still stands as a gatekeeper to the federal courts.<sup>156</sup> But as is evident from the legislative history, Congress passed the PSLRA to prevent frivolous lawsuits, not to shield all corporate insiders. Using group pleading to ensure that corporate insiders are liable for unattributed group statements is consistent with the goals of the PSLRA.

The fundamental purpose of group pleading is to presume that corporate insiders are responsible for their corporation's misstatements only when those corporate insiders are sufficiently involved in

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<sup>149</sup> See Scott V. Simpson, *The Emerging Role of the Special Committee—Ensuring Business Judgment Rule Protection in the Context of Management Leveraged Buyouts and Other Corporate Transactions Involving Conflicts of Interest*, 43 BUS. LAW. 665, 665 (1988).

<sup>150</sup> See Sarbanes-Oxley Act of 2002 § 301 (codified at 15 U.S.C. § 78j-1(m) (2012)).

<sup>151</sup> See 15 U.S.C. § 78j-3 (2012); see also Regulation S-K (codified at 17 C.F.R. § 229.402 (2013)) (outlining the duties of the compensation committee). Although compensation reports do not create liability under section 11 of the 1933 Act because they do not need to be filed, an action under Rule 10b-5 is broader than section 11 liability and does not have a filing requirement to create liability.

<sup>152</sup> Although corporations are not required to have nominating committees, ninety-nine percent of Standards and Poor companies have them. See Michael K. Molitor, *The Crucial Role of the Nominating Committee: Re-Inventing Nominating Committees in the Aftermath of Shareholder Access to the Proxy*, 11 U.C. DAVIS BUS. L.J. 97, 108 (2010). For a discussion on the rise of nominating committees, see generally *id.*

<sup>153</sup> See, e.g., *In re JWP Inc. Sec. Litig.*, 928 F. Supp. 1239, 1257 (S.D.N.Y. 1996) (discussing the liability of members of an auditing committee); *Greenfield v. Prof'l Care, Inc.*, 677 F. Supp. 110, 114–15 (E.D.N.Y. 1987).

<sup>154</sup> 286 B.R. 33 (D. Mass. 2002).

<sup>155</sup> *Id.* at 37.

<sup>156</sup> See *Strum v. Marriot Marquis Corp.*, 85 F. Supp. 2d 1356, 1366 (2000) ("The Reform Act contemplates that the district courts will serve a gatekeeping role . . .").

their corporation's decision-making process.<sup>157</sup> Plaintiffs that rely on group pleading may not entirely forgo their obligation to plead facts that plausibly allege an untrue statement; rather, the traditional application of group pleading still requires that plaintiffs plead the *misrepresentations* with particularity.<sup>158</sup> Critics of group pleading contend that the PSLRA requires particularized factual allegations with respect to each specific defendant.<sup>159</sup> And as discussed above, several circuits have interpreted the PSLRA to require this particularized pleading with respect to each defendant's act.<sup>160</sup>

Pleading any allegation made on information and belief is not a barrier to the application of the group pleading doctrine because nothing in the statute requires particularized pleading as to each individual defendant. The PSLRA only requires particularized pleading for "an allegation regarding the *statement or omission*," not the defendants' identities.<sup>161</sup> Indeed, it is sufficient for a plaintiff to allege with particularity that specific statements by unknown defendants within a corporation are untrue. This makes sense considering what we know about business organizations and their decision making: multiple corporate insiders tend to be responsible for any given corporate decision.<sup>162</sup> Thus, once a plaintiff pleads particularized facts regarding an untrue statement, a court may permissibly presume that several corporate insider defendants were responsible for that untrue statement.<sup>163</sup>

This interpretation is also consistent with the purpose of the PSLRA: to end frivolous lawsuits.<sup>164</sup> Supporters like Richard Breeden,

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<sup>157</sup> See *supra* notes 22–25 and accompanying text.

<sup>158</sup> See *Wool v. Tandem Computers Inc.*, 818 F.2d 1433, 1440 (9th Cir. 1987).

<sup>159</sup> 15 U.S.C. § 78u-4(b)(1)(A) to (B) (2012) (stating that plaintiffs must allege "the defendant made an untrue statement of material fact . . . and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state *with particularity* all facts on which that belief is formed." (emphasis added)). The PSLRA also requires a plaintiff to plead each defendant's scienter with particularity. This requirement does not present problems with group pleading because group pleading presumes action by corporate insiders, not state of mind. There is another doctrine termed "collective scienter" that has a similar application to group pleading; however, this falls outside the scope of this Note. For background on collective scienter in SEC enforcement actions, see generally Bradley J. Bondi, *Dangerous Liasons: Collective Scienter in SEC Enforcement Actions*, 6 N.Y.U. J.L. & Bus. 1 (2009) (recounting the history of collective scienter and the various views by the circuits).

<sup>160</sup> See *supra* text accompanying notes 46–55.

<sup>161</sup> 15 U.S.C. § 78u-4(b)(1)(B) (emphasis added).

<sup>162</sup> See *supra* notes 138–55 and accompanying text.

<sup>163</sup> See, e.g., *Haw. Ironworkers Annuity Trust Fund v. Cole*, No. 3:10CV371, 2011 WL 3862206, at \*1 (N.D. Ohio Sept. 1, 2011) (upholding plaintiffs' complaint that four company officers worked together to falsify financial statements).

<sup>164</sup> William J. Clinton, Veto Message for Securities Litigation Reform Act (Dec. 20, 1995), 1995 WL 752715, at \*1 ("This legislation is designed to reform portions of the Federal securities laws to end frivolous lawsuits and to ensure that investors receive the best possible information by reducing the litigation risk to companies that make forward-looking statements."). In addition, Congress intended the PSLRA to curb the number of

former chairman of the SEC, praised the PSLRA prior to its passage. Still, he cautioned, “[t]he challenge, then, is to devise ways to reduce unwarranted securities litigation without closing the courthouse door for victims of intentional securities fraud.”<sup>165</sup> Once a plaintiff alleges that an untrue statement was made with the requisite particularity, courts should no longer be concerned with preventing frivolous lawsuits, primarily because the plaintiff’s allegations are sufficiently particular to assuage fears of frivolity. Instead, courts should be concerned with ensuring that their courthouse doors are not closed to plaintiffs. The inability of a plaintiff to allege precisely who made the untrue statement should not act as a bar.

### CONCLUSION

The group pleading doctrine does not attempt to create additional liability for innocent defendants. The doctrine is simply a presumption that certain corporate insiders involved with the day-to-day business of the corporation are responsible for statements made on behalf of the corporation.<sup>166</sup> The presumption only extends to “individuals with ‘direct involvement in the everyday business of the company.’”<sup>167</sup>

Although the group pleading doctrine should be narrowly applied after *Janus*, the complete rejection of group pleading is inappropriate. *Janus* makes it clear that a third party cannot have ultimate authority over the statements of an independent corporation.<sup>168</sup> This

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so-called strike suits that were being brought. 141 CONG. REC. E555-03 (daily ed. Mar. 8, 1995), 1995 WL 94323, at \*1 (statement of Rep. Lofgren) (“Over the past year of study, I have reached the conclusion that, especially for high technology companies, there is a problem of strike lawsuits that requires remedy.”). Strike suits are lawsuits that are brought with the sole intention of getting to discovery and seeking settlement with the corporation. See S. REP. NO. 104-98, at 6 (1995), reprinted in 1995 U.S.C.C.A.N. 679, 685, 1995 WL 372783 (“Indeed, a 1994 Securities Subcommittee Staff Report found ‘evidence . . . that plaintiffs’ counsel in many instances litigate with a view toward ensuring payment for their services without sufficient regard to whether their clients are receiving adequate compensation in light of evidence of wrongdoing.’”).

<sup>165</sup> *Securities Litigation Revisions: Hearing on S. 240 Before the Subcomm. on Sec. of the S. Comm. on Banking, Hous. & Urban Affairs*, 104th Cong. (1995) (testimony of Richard C. Breeden) (internal quotation marks omitted).

<sup>166</sup> See *In re Stratosphere Corp. Sec. Litig.*, 1 F. Supp. 2d 1096, 1108 (D. Nev. 1998) (“Under this doctrine, plaintiffs may rely on a presumption that statements in ‘prospectuses, registration statements, annual reports, press releases, or other “group-published information,” are the collective work of those individuals with direct involvement in the everyday business of the company.’” (quoting *In re Silicon Graphics, Inc. Sec. Litig.*, 970 F. Supp. 746, 759 (N.D. Cal. 1997), *aff’d*, 183 F.3d 970 (9th Cir. 1999))).

<sup>167</sup> *SEC v. Landberg*, 836 F. Supp. 2d 148, 156 (S.D.N.Y. 2011) (quoting *In re Refco, Inc. Sec. Litig.*, 503 F. Supp. 2d 611, 641 (S.D.N.Y. 2007)).

<sup>168</sup> See *Janus Capital Grp., Inc. v. First Derivative Traders*, 131 S. Ct. 2296, 2306 (2011) (holding that while Janus Management and Janus Fund are “closely related[,] . . . only the Janus Fund, not Janus Management, could have ‘ma[d]e’ those statements,” since only

is reasonable in light of previous case law and the PSLRA. *Janus*, however, does not foreclose the application of the group pleading doctrine to corporate insiders. Not only are the facts of *Janus* different from the traditional application of the group pleading doctrine, but the basic corporate model indicates that several individuals within an organization regularly have ultimate authority over the same statements.

Lastly, nothing in the PSLRA prevents plaintiffs from bringing an action against several corporate insiders, so long as they are able to allege the untrue statements on information and belief with particularity. The particularity requirement does not extend to individual defendants, and such a reading would be contrary to a plain reading of the statute and its purpose.

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“the Janus Fund’s board of trustees has ‘ultimate authority’ over the content of the statements in a Fund prospectus”).

