

This Week in Chancery Court: Johnson & Johnson, TransCanada

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWY1MDgtZGU2NS1hOWNILWY3OWY0Y2JjMDAwNSlsmN0eHQiOiJTTE5XliwidXVpZCI6IkpkaUTRuRm1FdzVMM2Ind1UrS3M5dnc9PUNtbIBzT3RQVGF rMFRSWnJZWkFsVmc9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzAyIiwic2lnIjoIn0k3UGZiYzRlVUtJM1lUVVgyL3BaQnJXaURF PSIsInYiOiXln0=

Johnson & Johnson will face former Auris Health Inc. investors at trial before the Delaware Court of Chancery in a case alleging fraud related to the development and regulatory approval of a surgical robot system.

Here are more highlights from the court's calendar this week:

Tuesday: Fortis Advisors LLC v. Johnson & Johnson, Del. Ch., No. 2020-0881, trial 1/16/24

At issue: A long-running dispute stemming from the Food and Drug Administration's decision to change the regulatory pathway for "robotically assisted surgical devices" finally comes to trial. Johnson & Johnson faces allegations that its Ethicon Inc. unit duped Auris investors into a \$3.4 billion acquisition in 2019. Auris was developing the "iPlatform" surgical robot system at the time. Ex-Auris shareholders claim Ethicon misled them about the way it would allocate resources between iPlatform and another surgical robot in development. They also allege Ethicon made billions of dollars in post-deal payments to Auris contingent on unreachable regulatory and sales milestones related to iPlatform. Johnson & Johnson denies the allegations and argues it still poured time and resources into the iPlatform system even after receiving FDA feedback that made making its milestones "unachievable." Attorneys for the former Auris shareholders said in a pre-trial brief that "the milestones were not hit because that was never J&J's objective."

Court action: A ten-day trial opens Tuesday in Wilmington.

J&J Loses Bid to Nix Fraud Lawsuit Over \$3.4 Billion Auris Deal

Tuesday: Lien v. Eagle Equity Partners II LLC, Del. Ch., No. 2022-0972, oral argument 1/16/24.

At issue: An investor in online video game company Skillz Inc. is suing the Hollywood executives—including MGM Studios ex-chairman Harry Sloan and former CBS Entertainment president Jeff Sagansky—who backed the blank-check deal that took it public, claiming they engineered the merger to give them a windfall regardless of its merits and duped shareholders into approving it with virtually no due diligence. Attorneys for Sloan, Sagansky, and other defendants have filed motions seeking to dismiss the lawsuit. The Skillz acquisition resembles other SPAC litigation where the court has found that "the SPAC

structure may incentivize its fiduciaries to deviate from their duties of loyalty to pursue value-destructive deals that generate outsized returns for themselves at the expense of public stockholders,” the investor’s attorneys said in an answering brief.

Court action: Oral arguments on the motions to dismiss will be heard in Wilmington.

Skillz eSports Investor Sues Hollywood Veterans Behind SPAC Deal

Friday: In re Columbia Pipeline Grp., Merger Litig., Del. Ch., No. 2018-0484, hearing 1/19/24.

At issue: The court last year found TransCanada liable to investors for allowing certain fiduciary breaches to occur during a \$13 billion merger with Columbia Pipeline Group Inc., and the plaintiffs were awarded sale process damages of \$1 per share based on a reneged-upon \$26 per share deal and disclosure damages of \$0.50 per share. However, there remained some issues for the court to resolve, the parties told Vice Chancellor J. Travis Laster in a letter. Among those issues: TransCanada seeks a judgment reduction under the terms of a \$79 million class action settlement that allowed two former Columbia executives to exit the litigation in 2022. The plaintiffs also now seek pre- and post-judgment interest and an award for fees and costs.

Court action: Hearing in Wilmington to address remaining post-opinion issues.

TransCanada Breached Duties in \$13 Billion Columbia Merger (1)

Friday: Omni Newco LLC v. Forward Air Corp., Del. Ch., No. 2023-1104, trial 1/19/24.

At issues: Omni Logistics sued Forward Air Corp. in late October, seeking a court order that would compel closing a \$3.2 billion supply chain logistics merger after Forward moved to cancel the transaction. The litigation is a relatively rare breed of court cases that seek to force a transaction after one side balks, a remedy called specific performance. This lawsuit has proceeded on an expedited basis, with the parties recently arguing over motions to compel text messages, handwritten notes, or other documents before trial.

Court action: A four-day trial begins Friday in Wilmington and continues the following week.

Omni Sues Forward to Force Closing of \$3.2 Billion Merger (1)

To contact the reporter on this story: Jennifer Kay in Philadelphia at jkay@bloomberglaw.com

To contact the editors responsible for this story: Alex Clearfield at aclearfield@bloombergindustry.com; Andrew Childers at achilders@bloomberglaw.com

AT&T Board, Execs Sued for Allegedly Hiding Toxic Cable Risks

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWZiYUUtZDZiNjY1hNWNmLWZmZWZhZGY5MDAwMSIsImN0eHQiOiJTTE5XliwidXVpZCI6IiBsMkZ0WmRDdWpwcFNFQW41Q3JFS3c9PUE5UFJNa3psWmM5N3lOSmFOaUF6K0E9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzA2Iiwic2lnIjoizDRIRUM1bCs5elY0RzhHUWtEZzY0ZkeEI4PSIsInYiOiIxIn0=

- COURT: D. Del.
- TRACK DOCKET: 1:24-cv-00032

AT&T Inc.'s top executives and directors spent more than three years concealing the environmental and health risks associated with lead-covered cables in its network, a shareholder derivative lawsuit says.

Several stock drops followed the revelation in July 2023 that AT&T was among the telecommunications companies with toxic cables leftover from the Bell System, the complaint says. Before then, the company's leadership had failed to disclose its ownership of the lead-covered cables or any of the risks those cables posed, according to the complaint filed Thursday in US District Court for the District of Delaware.

The company represented to the public that it was compliant with environmental, health, and safety regulations, touting its dedication to protecting its employees and the communities it serves in regulatory filings and on its website since March 2020, the complaint says.

Shareholder George Miller's suit came the same day the US Environmental Protection Agency made public letters it sent to the telecommunications company and to Verizon Communications Inc. in December, requesting meetings with the companies concerning the situation.

Wall Street Journal articles published July 9 and 10, 2023 revealed the widespread existence of lead-covered cables across telecommunications companies' networks and noted that AT&T was aware of the associated heart disease, anemia, and infertility risks. AT&T's stock price fell more than 2% to close at \$15.27 on July 10, according to the complaint.

A follow-up article from the Wall Street Journal focused on the companies' knowledge of the health risks, reporting that AT&T had known for decades that the lead in its network posed a possible health risk to workers and had the potential to leach into the nearby environment. The day after another article including stories from current and former AT&T employees was published, the company's stock price fell more than 4% to close at \$14.50 per share on July 14, according to the complaint.

The company's stock fell again by nearly 7% to close at \$13.53 on July 17, the same day that the Journal published two more articles on the lead-covered cables and investing.com ran its own article highlighting how analysts had downgraded AT&T due to the revelations, according to the complaint.

Another WSJ article highlighting Justice Department and EPA probes into the telecommunication companies was published on July 26. The next day the company's stock price fell more than 2% to close at \$14.51 per share, according to the complaint.

Verizon is also subject to similar litigation.

Miller seeks to recover damages on behalf of the company for the executives' and directors' alleged violations of the Securities Exchange Act. He also seeks legal fees, the complaint says.

Another shareholder filed a class action against AT&T in July highlighting the telecommunications giant's alleged failure to disclose information to investors about the lead-covered cables in its network and associated risks. That suit is still pending in the US District Court for the District of New Jersey.

An AT&T spokeswoman declined to comment.

Farnan LLP and the Brown Law Firm PC represent the plaintiff.

The case is Miller v. Stephenson , D. Del., No. 1:24-cv-00032, complaint filed 1/11/24 .

To contact the reporter on this story: Ben Miller in New York City at bmiller2@bloombergindustry.com

To contact the editor responsible for this story: Andrew Harris at aharris@bloomberglaw.com

JPMorgan Leaders Fend Off Suit Over Epstein Ties' Costs to Bank

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWZmYmUtZDFiYS1hN2ZjLWZmZmY3NDdjMDAwMSIsImN0eHQiOiJTTE5XliwidXVpZCI6IjZhNjNINVBMc2VTQ1pWbW9SeEI4SWc9PUJwMHNENGg4cFJGckJwZkxhYWVvNIE9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzAzliwic2InIjoiaW5ZVmx5VzJKcmFCc3RHV3crKzZVdGFzaVdNPStsInYiOiIxN0=

Litigation

Signage is displayed at JPMorgan Chase & Co. headquarters in New York City.

Photographer: Michael Nagle/Bloomberg

JPMorgan Chase & Co. investors can't proceed with a suit against the company's directors and officers for retaining Jeffrey Epstein as a client, a federal judge said Friday.

The suit alleging the leaders knew or should have known "that Epstein was using the bank's financial services to facilitate Epstein's criminal sex trafficking and exploitation of women and underaged girls" was filed without a demand that the firm's board of directors approve the litigation, Judge Jed Rakoff said.

- Rakoff, of the US District Court for the Southern District of New York, explained the reasons for a ruling he originally made in a brief order in August
- The investors failed to show that making a demand on the board to approve the derivative suit would be futile, Rakoff said
- The suit, which pointed to \$365 million in settlements with Epstein victims and the US Virgin Islands, will be dismissed with finality

Grant & Eisenhofer PA and Bernstein Litowitz Berger & Grossmann LLP represented the investors. Wilmer Cutler Pickering Hale and Dorr LLP and Paul, Weiss, Rifkind, Wharton & Garrison LLP represented the defendants.

The case is City of Miami Gen. Emps. & Sanitation Emps. Ret. Trust v. Dimon , 2024 BL 11750, S.D.N.Y., No. 23-cv-03903, 1/12/24 .

To contact the reporter on this story: Martina Barash in Washington at mbarash@bloomberglaw.com

To contact the editor responsible for this story: Amy Lee Rosen at arosen@bloombergindustry.com

Browse More Stories in Litigation

- © 2024 Bloomberg Industry Group, Inc. All Rights Reserved

2nd Shareholder Lawsuit Filed Against Biotech Company

 [law.com/ctlawtribune/2024/01/12/2nd-shareholder-lawsuit-filed-against-biotech-company](https://www.law.com/ctlawtribune/2024/01/12/2nd-shareholder-lawsuit-filed-against-biotech-company)

By Emily Cousins

BioXcel Therapeutics Inc. was named in a second shareholder derivative lawsuit after clinical trials for a neurological medication allegedly did not follow proper guidelines and the company allegedly made contrary statements to the public.

The complaint was surfaced on Law.com Radar.

The original securities class action against BioXcel and top executives was filed in July 2023, leading now to two shareholder derivative lawsuits.

BioXcel, a biotech company, creates neurological medicine using artificial intelligence. It has one drug on the market called Igalmi, which is used to treat schizophrenia or bipolar disorder in adults, according to its website.

The complaint alleged that the company was seeking to create a medication derived from the same molecule used to create Igalmi to aid those with Alzheimer's disease.

However, the principal investigator allegedly did not follow U.S. Food and Drug Administration rules and regulations due to "mounting pressure to fast track [the drug] to market under exigent circumstances to meet artificial milestones set by BioXcel's biggest lenders Oaktree Capital Management L.P. and Qatar Investment Authority," the complaint said.

According to the complaint, the investigator "may have fabricated" emails to show a timely report of a "serious adverse event," and the correspondence was given to the FDA during an inspection.

BioXcel continued to release information to the public and the U.S. Securities and Exchange Commission that lacked information about its "exposure to the inept clinical trials" and FDA investigation, which breached the company's disclosure duties, the complaint said.

The plaintiff, Maria Vomvolakis, has been a BioXcel shareholder since November 2021, the complaint said, and she alleged that the defendants, BioXcel and executives, breached their fiduciary duties.

In addition, the individual defendants were accused of conspiracy, aiding and abetting, and concerted action due to efforts to "conceal" the truth about the clinical trials, the complaint said.

The plaintiff brought further claims of unjust enrichment, violations of the Securities Exchange Act of 1934 and waste of corporate assets.

Fletcher Moore of Moore Law and Lee Squitieri of Squitieri & Fearon, counsel for the plaintiff, did not respond to a request for comment. Counsel for the defendants has not appeared yet, and BioXcel did not respond to a request for comment.

This suit was surfaced by Law.com Radar, ALM's source for immediate alerting on just-filed cases in state and federal courts. Law.com Radar now offers state court coverage nationwide. Sign up today and be the first to know about new suits in your region, practice area or client sector.

Read the complaint:

NOT FOR REPRINT

© 2024 ALM Global, LLC, All Rights Reserved. Request academic re-use from www.copyright.com. All other uses, submit a request to asset-and-logo-licensing@alm.com. For more information visit Asset & Logo Licensing.

A New COVID-Related Securities Suit for the New Year

K [dandodiary.com/2024/01/articles/coronavirus/a-new-covid-related-securities-suit-for-the-new-year/](https://www.dandodiary.com/2024/01/articles/coronavirus/a-new-covid-related-securities-suit-for-the-new-year/)

January 14, 2024



By Kevin LaCroix on January 14, 2024

Posted in Coronavirus

BIONTECH

One of the most distinct securities class action lawsuit filing phenomena since the outbreak of COVID-19 in the U.S. in March 2020 has been the surge of pandemic-related securities suits, particularly during the period 2020 through 2022. This securities

suit filing trend even continued into 2023, although the incidence of COVID-related suits dwindled during the year. However, in an unexpected development, a plaintiff shareholder has now filed yet another COVID-related securities suit against BioNTech, the German biotechnology company that, along with its partner Pfizer, was lionized for helping to develop a COVID-19 vaccine. The company was hit with a securities suit after its share price declined following a sizeable inventory write-off. A copy of the January 12, 2024, complaint against the company can be found [here](#).

Background

As has become a part of the lore surrounding the recent pandemic, in 2020, German-based biotech company and U.S.-based Pfizer worked together to co-develop an mRNA-based vaccine for COVID-19 known as Comirnaty. After the vaccine was developed and approved, it was widely distributed and the company's fortunes soared.

As part of BioNTech's collaboration with Pfizer, the two companies agreed to share gross profits from COVID-19 vaccine sales. Over time, COVID evolved and new variants, including the Omicron XBB 1.5 subvariant, began to develop and eventually represented the majority of COVID cases. The new securities lawsuit alleges that despite not having a version of Comirnaty approved to treat the subvariant, BioNTech continued to represent to investors that Comirnaty remained relevant and in-demand.

On October 13, 2023, Pfizer announced that due to lower-than-expected utilization of its COVID-related vaccine products, it was taking a \$5.5 billion charge related to inventory write-offs. On October 16, 2023, BioNTech announced that as a result of Pfizer's inventory

write-offs, it would take a €0.9 write-off, representing half of the company's take under the gross profit sharing agreement and reducing the company's expected 2023 revenues. According to the subsequently filed securities lawsuit, the company's share price declined over 6% on the news.

The Lawsuit

On January 12, 2024, a plaintiff shareholder filed a securities class action lawsuit in the Central District of California against BioNTech and certain of its directors and officers. The complaint purports to be filed on behalf of investors who purchased BioNTech securities in the U.S. March 30, 2022, and October 13, 2023.

The complaint alleges that during the class period the defendants made false or misleading statements or failed to disclose that: "(i) BioNTech overstated demand for Comirnaty and/or its commercial prospects; (ii) the Company and/or Pfizer had accumulated excess inventory of raw materials for Comirnaty, as well as COVID-19 vaccine doses adapted to other non-XBB.1.5 variants that were produced at risk; (iii) accordingly, BioNTech was at an increased risk of recording significant inventory write-offs and other charges related to Comirnaty; and (iv) as a result, Defendants' public statements were materially false and/or misleading at all relevant times."

The complaint alleges that the defendants violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder. The complaint seeks to recover damages on behalf of the class.

Discussion

It is striking that BioNTech is now the subject of a securities class action lawsuit and that the lawsuit relates to the company's COVID vaccine. The company's development with Pfizer of the vaccine using the mRNA technology was and remains one of the great achievements of the global pandemic. Indeed, medical scholars have called the development of the vaccine "one of the greatest accomplishments of modern medicine."

But the development of the vaccine not only had technological and medical significance; it also had commercial significance. BioNTech rode the wave as demand for the vaccine it developed with Pfizer soared. But just as the coronavirus itself evolved and the medical circumstances underlying the pandemic changed, the commercial circumstances changed as well. The great wheel of fortune that the company rode as demand for the vaccine surged eventually turned and the company's fortunes ebbed.

While there are probably many lessons to be told from this story, there is nothing about these changes in fortune that necessarily turn this sequence of events into securities fraud. Specifically, when the time comes for the court to assess the adequacy of the complaint's

allegations, the court is going to have to look long and hard to find anything in this complaint that even arguably would satisfy the plaintiff's obligation to plead scienter.

All of that said, there is still the interesting fact that even at this late date, the plaintiff has filed a COVID-related securities lawsuit.

As I noted at the outset, the filing of COVID-related securities suits followed closely after the outbreak of the coronavirus in the U.S. in March 2020, and COVID-related securities suits were an important part of securities class action lawsuit filings in each of the years 2020, 2021, and 2022. Indeed, COVID-related securities suit filings continued into 2023 – according to my tally, there were nine COVID-related securities suits filed in 2023. However, the COVID-related securities suit filings dwindled as 2023 progressed; there were not COVID-related securities suits filed during 2023 after late August.

This new COVID-related securities suit is not only the first COVID-related securities suit of 2024, but also it is the first to be filed since August 2023.

By my count, there have now been a total of 72 COVID-related securities suits filed since the initial COVID outbreak in the U.S. in March 2020. Most of these lawsuits fell into one of several well-identified categories. The new lawsuit against BioNTech falls clearly falls into a relatively late-developing category involving companies who prospered at the outset of the pandemic but whose fortunes waned as the pandemic progressed and evolved. That story arc clearly describes what appears to have happened with BioNTech.

The New Year has only just begun, and it remains to be seen what patterns and trends will develop with respect to securities class action lawsuit filings during the year, but it is interesting to see that relatively long-standing patterns from recent years are still coming into play.

Gatos Silver's Board Sued for Misrepresenting Mining Estimates

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWZmNzktZDdkNi1hN2VmLWZmN2QyZDRhMDAwMSIsImN0eHQiOiJTTE5XliwidXVpZCI6Im9SVUdMYzJJR0lwNVlJWtNEOfg4U3c9PW5OQmRFT0VPdjFrZTVRSGN5WXhiRkE9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzA2Iiwic2lnIjoiriRGZqZldKUUVd0dVJyemkyZVBTZGpGY0N3NlFnPSIsInYiOiIxIn0=

Litigation

Photo: AmnajKhetsamtip/Getty Images

- **COURT:** D. Del.
- **TRACK DOCKET:** No. 1:24-cv-00040

Gatos Silver Inc.'s directors are responsible for statements supporting the reliability of a technical report on mineral reserves at a Mexican mine that proved too optimistic, an investor alleges.

Shareholder Noah Orozco's case, filed Thursday in the US District Court for the District of Delaware, is the second derivative suit in about a month alleging that board members caused the company to say activities at the mine wouldn't change the information in the report. The other case is also in the District of Delaware.

The suits follow the announcement in July of a proposed \$21 million settlement with investors in a class action with similar allegations. That deal is awaiting preliminary approval from a federal court in Colorado.

The silver and zinc mining company touted the mineral reserves at its Cerro Los Gatos project in the state of Chihuahua ahead of its 2020 initial public offering, Orozco says. Later it disclosed errors in its technical report for the deposit, he says. That brought harm to the company, including its exposure to class securities claims, he says.

Orozco asserts claims for breach of fiduciary duties, securities fraud, contribution, indemnification, and unjust enrichment. He seeks compensatory damages, punitive damages, and disgorgement.

Gatos Silver didn't immediately respond to an emailed request for comment on behalf of itself or the individual defendants.

Farnan LLP and the Rosen Law Firm PA represent Orozco.

The case is Orozco v. Stairs , D. Del., No. 1:24-cv-00040, complaint 1/11/24 .

Liberty, Sirius Class, Derivative Settlement Gets Green Light

B

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWZlOTktZDZiNy1hNWNmLWZmZm1lZWE4MDAwMSIsImN0eHQiOiJTTE5XliwidXVpZCI6ImlaejZ5WEZwSXF3TnNiN3prVnpmZUE9PVBVbUICQUNSUhNoV25xVjFGM2IKaGc9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzA1Iiwic2lnIjoiTjVsWENuUmxWODBDN3hSTnNVMnlpTIVBc0xJPSIsInYiOiXln0=

- Class consists of Sirius XM stock holders as of Jan. 5
- Proposed settlement filed Jan. 8; hearing set for April 8

A proposed \$36 million settlement by Liberty Media Corp. and Sirius XM Holdings Inc. of derivative and class claims on behalf of Sirius stockholders won preliminary approval from the Delaware Chancery Court.

The complaint, filed Sept. 23, 2001, alleged that partial parent Liberty sought to back the entertainment company into a short-form merger by having Sirius buy back billions worth of stock.

Chancellor Kathaleen St. Jude McCormick preliminarily approved a settlement class, consisting of all holders of Sirius XM common stock, as of the close of trading on Jan. 5, 2024. The parties filed a proposed settlement agreement on Jan. 8.

The court Wednesday preliminarily appointed plaintiff Vladimir Fishel as class representative for the settlement class, and the law firm of Bernstein Litowitz Berger & Grossman LLP as class counsel for the settlement class.

For the purposes of settlement only, the court preliminarily found the settlement class met the requirements of numerosity, commonality, typicality, and that the plaintiff and his lead counsel are “fair and adequate representatives.”

The suit alleged a stock repurchase scheme by Liberty and the board to have the subsidiary spend more than \$16 billion buying back stock, indirectly increasing Liberty’s stake over time, without forcing it to put in place protections for minority shareholders.

As a result of the scheme, the suit alleged, “minority stockholders are coerced to sell now into the market and at no premium.”

The complaint alleged that there are 4,050,435,824 Sirius XM shares outstanding, about 20% of which are held by minority investors. “As a result, there are surely hundreds, if not thousands, of Sirius XM stockholders who are scattered throughout the United States, and likely the world,” the plaintiffs alleged.

The derivative claim targeted the Sirius board and 78% majority owner Liberty, which is controlled by billionaire John C. Malone.

A settlement hearing will be held on April 8.

Simpson Thacher & Bartlett LLP represents Sirius. Baker Botts LLP represents Liberty.

The case is Fishel v. Liberty Media Corp. , Del. Ch., No. 2021-0820, 1/10/24 .

To contact the reporter on this story: Peter Hayes in Washington at
PHayes@bloombergindustry.com

To contact the editor responsible for this story: Blair Chavis at
bchavis@bloombergindustry.com

Axis Insurance Must Deal With Executives' Fraud Dispute in Trial

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWZlZjYtZDFiYS1hN2ZjLWZlZjdmdZDQzMdAwMSIsImN0eHQiOiJTTE5XliwidXVpZCI6IlZuU0hvWGp1dGI3VVpGT1YzTGZlYVE9PS9reElhZ0FueGZhb1MwZGNqZml4MkE9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzA0Iiwic2lnIjoieVmlWbmZ3UnJoc25xajZoOWtHa1ROM2JvaXNVPSIsInYiOiIxIn0=

Insurance

- Federal court sticks with ruling in favor of policyholder
- Cantaloupe allegedly inflated revenue and stock prices

An AXIS Capital Holdings Ltd. insurance unit failed to convince a federal court to reconsider its decision ordering a jury to weigh a suit from payment technology company Cantaloupe Inc. seeking directors and officers insurance for federal securities probes and private lawsuits.

There is a factual dispute over what Cantaloupe executives knew about potential insurance claims arising from the alleged fraud before buying the policy, Judge Gene E.K. Pratter of the US District Court for the Eastern District of Pennsylvania said Thursday. The court kept in place a November decision calling for a jury to weigh the executives' "subjective knowledge" about an allegedly fraudulent stock offering that led to federal investigations and private suits.

Axis Insurance Co. has said that the court made a mistake by rejecting its bid for summary judgment to avoid coverage. Cantaloupe executives were aware of the underlying fraud—a \$70 million secondary stock offering they approved in May 2018 despite knowing the company had fake sales numbers—when they bought the policy, the insurer said.

The court refused, however, to rule that a "prior knowledge" exclusion applies.

Cantaloupe was hit with securities class actions and subpoenas from the Justice Department and the Securities and Exchange Commission in 2018 alleging the company inflated stock prices and violated securities laws. The probes and lawsuits came after Cantaloupe purchased the insurance policy and subsequently informed investors of an internal accounting investigation. Cantaloupe sued in January 2022 after Axis denied coverage.

"Whether Cantaloupe officials subjectively knew that the facts at the time could lead to a claim or instead constituted a minor financial irregularity couched in the-sky-is-falling language is in dispute," the court said Thursday.

Affeld Grivakes LLP and LeVan Stapleton Segal Cochran LLC represent Cantaloupe. Werner Ahari Mangel LLP represents Axis.

The case is *Cantaloupe v. Axis*, E.D. Pa., 2:22-cv-00030, 1/11/24 .

To contact the reporter on this story: Daphne Zhang in New York City at dzhang@bloombergindustry.com

To contact the editor responsible for this story: Michael Smallberg at msmallberg@bloombergindustry.com

[Browse More Stories in Insurance](#)

- © 2024 Bloomberg Industry Group, Inc. All Rights Reserved

Business Law Prof Blog

 lawprofessors.typepad.com/business_law/2024/01/supreme-court-to-hear-important-securities-fraud-case-tomorrow.html

Monday, January 15, 2024

Supreme Court to Hear Important Securities Fraud Case - Tomorrow!

By joanheminway

Tomorrow morning, the U.S. Supreme Court will be hearing oral arguments on a securities fraud case for which I am an amicus brief coauthor. The case is: *Macquarie Infrastructure Corporation, et al. v. Moab Partners, L.P., et al.* (No. 22–1165, Certiorari to the C. A. 2nd Circuit). The Court convenes at 10 am and has allotted one hour for oral argument: 30 minutes for the petitioners, 20 minutes for the respondent, Moab Partners, and 10 minutes for the U.S. Securities and Exchange Commission (“SEC”), as amicus supporting the respondents. An audio feed of the argument is live-streamed on the Court’s website, and the Court posts the audio later in the day.

The question presented to the Court is: “May a failure to make a disclosure required under Item 303 of SEC Regulation S-K support a private claim under Section 10(b) of the Securities Exchange Act of 1934, even in the absence of an otherwise misleading statement?” The issue in the case, in essence, is whether a mandatory disclosure rule properly adopted by the SEC gives rise to a duty to disclose that can be the basis of a securities fraud claim under Section 10(b) of and Rule 10b-5 under the Securities Exchange Act of 1934, as amended. There is a circuit split on this issue. As most of you know, in 1988, in *Basic v. Levinson*, the Supreme Court offered that “[s]ilence, absent a duty to disclose, is not misleading under Rule 10b-5.” A duty to disclose is therefore a foundational element in a Section 10(b)/Rule 10b-5 claim. Of course, the elements of proof extend beyond this essential disclosure duty element—including by incorporating the requirement that there be a misstatement or misleading omission of a material fact).

The *Macquarie* case involves a corporation’s alleged failure to comply with an SEC mandatory disclosure rule. The corporation and other original defendants are the petitioners. Our brief argues in favor of the respondents. In sum, we argue that the SEC disclosure requirement creates a judicially cognizable duty to disclose for purposes of a claim under Section 10(b)/Rule 10b-5. Accordingly, we contend that the omission of the required disclosure provides a basis for a Section 10(b)/Rule 10b-5 claim. An omission to state material fact required to be disclosed under an SEC mandatory disclosure rule may mislead investors who expect that any required disclosure is made or inapplicable.

Many of us teach in this space. If you have time to listen in, the argument may illuminate some new things. And it is bound to be interesting, regardless.

Supreme Court Signals Narrow Ruling on Securities Liability

B [bloomberglaw.com/product/blaw/bloomberglawnews/securities-law/XEQBILBC000000](https://www.bloomberglaw.com/product/blaw/bloomberglawnews/securities-law/XEQBILBC000000)

US Supreme Court justices once again found themselves debating a question on which the parties now seem to agree, this time in a much-anticipated securities case.

It's the latest example of when the justices don't discover until after they've granted a case that there's actually broad agreement on the issue. But the parties do differ widely on the effects the court's answer could have.

The precise question the justices agreed to decide is whether a "pure omission" in an SEC filing can give rise to a securities class action under Rule 10b-5, or whether there must be some statement that plaintiffs can point to that's misleading.

All parties appeared to agree during oral argument Tuesday there must be some statement in order for a class action to move forward. Now the argument is just how "narrow or capacious" the statement can be, Justice Elena Kagan said.

Several justices suggested answering just the question granted, and sending the case back to the lower courts to consider whether Macquarie Infrastructure Corp.'s failure to disclose that a new rule would decimate nearly half of its business made other statements about general risks to the business misleading.

Kellogg Hansen's David Frederick, arguing on behalf of one of MIC's shareholders Moab Partners, said that kind of ruling wouldn't provide a lot of clarity for the securities bar. He urged the justices to provide guidance on the question of how specific the alleged misleading statement must be before private shareholders can sue.

That's in part because both sides argue that the stakes are high. Frederick said requiring too much specificity would "create a roadmap for fraud." He noted that MIC's stock price fell 40% in one day after the new rule at the heart of the case was made known.

But MIC's attorney, Linda Coberly of Winston & Strawn, argued that a broad rule, allowing very general statements to give rise to liability, would force companies to keep silent on potential risks—or say so much that the information is essentially useless.

Coberly noted that the case comes to the court in the backdrop of Rule 10b-5, which the court has said "implies" a right for private plaintiffs to sue, even if that's not explicit in the statutory text. The court has been "loath to expand" that right, she said.

The case is Macquarie Infrastructure Corp. v. Moab Partners, U.S., No. 22-1165, argued 1/16/24 .

—With assistance from Martina Barash.

To contact the reporter on this story: Kimberly Strawbridge Robinson in Washington at krobinson@bloomberglaw.com

To contact the editors responsible for this story: Seth Stern at sstern@bloomberglaw.com; John Crawley at jcrawley@bloomberglaw.com

Bloomberg Law

Research Trail

My Work

000888

Help

Account

Litigation

Search Litigation

Select Sources

Go

Home

Practice Centers

Litigation

Transactional

Business

Practitioner Tools

News & Analysis

Laws & Regulations

Secondary Sources

 [Manage Subscription](#)

Litigation

Jan. 16, 2024, 8:00AM PST

Pro-Business Supreme Court to Be Tested in Regulatory Showdown

By Kimberly Strawbridge Robinson

- Justices consider overturning 40-year-old ruling on agency power
- Cases highlight complexity behind court’s pro-business reputation

Bloomberg Law News 2024-01-16T13:34:03096714904-05:00
Pro-Business Supreme Court to Be Tested in Regulatory Showdown

By Kimberly Strawbridge Robinson 2024-01-16T11:00:47000-05:00
Justices consider overturning 40-year-old ruling on agency power
Cases highlight complexity behind court’s pro-business reputation

A pair of cases that could reshape the future of government regulation cast the Roberts Court in a familiar light, as the most pro-business court in a century.

The justices Wednesday will consider whether to overturn a 1984 Chevron ruling that has the potential to reach far beyond the herring fishermen who brought the cases.

A victory for the fisherman seems all but certain, an outcome that reflects both what corporate America wants and the conservative justices’ fundamental notions about how government should be structured and what role agencies should play, court watchers say.

The cases challenging Chevron “may well be a place where business interests, speaking broadly, align with the justices’ concerns over the administrative state,” said Jonathan Adler of Case Western Reserve University School of Law, who wrote a 2016 book on the court’s reputation.

VIDEO: 'Fisherman's Blues' Could Lead Supreme Court to Overturn Chevron

https://www.bloomberglaw.com/product/blaw/bloomberglawnews/litigation/X4M7A4DC000000?bc=W1siU2VhcmNoICYgQnJvd3NlIiwiaHR0cHM6Ly93... 1/4

Aggressively Pro-Business

Loper Bright Enterprises v. Raimondo and *Relentless, Inc. v. Department of Commerce* challenge a National Marine Fisheries Service rule that requires herring fishing companies to foot the bill for federal monitors, “to the tune of 20% of their revenues,” according to a brief by the fishermen.

They are the latest in a long line of those seemingly attempting to rein in the so-called administrative state, which many conservatives on the court view as out of step with original design of the Constitution.

And businesses largely agree. According to a brief filed by the US Chamber of Commerce, agencies’ “distortion of the respective branches’ proper roles has helped to foster an unpredictable, unstable regulatory landscape” that’s “harmful to businesses.”

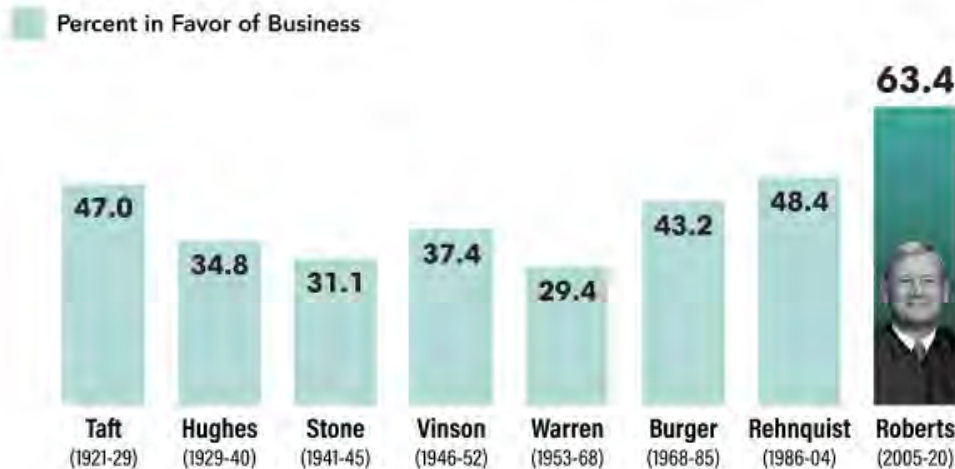
Court watchers, looking at the current court’s record in favor of business, anticipate at least a partial win for the fisheries here.

Backed up by the statistics and “any fair examination of the substance of what the court has done over the past decade,” Brian Frazelle, of the progressive Constitutional Accountability Center said, “there’s no doubt this is an aggressively pro-business court.”

A 2023 study shows that the Roberts Court has voted in favor of business interests in 63% of the cases its heard since 2005. That makes it the most likely to favor business in the last 100 years, said Lee Epstein, a professor of law and political science at the University of Southern California and one of the authors of the study.

And it’s more business friendly to business “by quite a distance,” said University of Virginia law professor G. Mitu Gulati, the study’s other author.

Business Success Rate at US Supreme Court by Chief Justice



Source: Lee Epstein and Mitu Gulati, *A Century of Business in the Supreme Court*

Bloomberg Law

Jonathan Hurtarte / Bloomberg Law

Some recent victories have included striking down environmental regulations, limiting when agencies can act on so-called major questions, and making it easier to challenge agency enforcement actions.

Carry the Day

But “the descriptor pro-business doesn’t tell us very much,” Adler said.

That’s in part because “pro-business means a lot of things to a lot of people,” said to Adam White a senior fellow at the American Enterprise Institute, a right-leaning, economically focused think tank.

The reality is that “there’s often business on both sides of the case,” White said, with big businesses often taking positions opposite of small ones and various industries interested in different outcomes.

All that can blur the perception of the court as friendly to business.

Moreover, Morgan Ratner, a partner at Sullivan & Cromwell, said it’s wrong to view the Roberts court as “reflexively” pro-business. The justices aren’t motivated by outcomes that service corporate America, she said.

Instead, it’s the conservative justices’ commitment to anti-regulation “that’s really animating this Supreme Court,” said University of Pennsylvania Carey Law School professor Jill Fisch, and the role that agencies play in our constitutional system of government.

That’s led the court to be skeptical of administrative agencies, and to pull back on the leeway they have to regulate business and other entities, Fisch said.

And the Roberts court has many opportunities to weigh in on the role of administrative agencies because many under Presidents Barack Obama, Donald Trump, and Joe Biden “have been doing novel, aggressive things,” White said.

“That’s where the real political energy is” and “so you’ll necessarily have hard cases” coming to the court,” White said.

Those concerns often translate into a pro-business outcome, but not always, Ratner said. She pointed to the court’s rulings—or lack thereof—on federal preemption of state law, state courts’ ability to haul businesses into their courthouses, and the dormant commerce clause as examples of where these background concerns with the structure of government have translated into outcomes that are bad for business.

There are areas where businesses are not getting what it wants, Adler said. In cases where what the business community wants diverges with the jurisprudential commitments of the justices, it’s the latter that will “carry the day over what matters to business.”

One Way Ratchet

Frazelle, who’s organization filed a brief urging the justices to uphold the Chevron doctrine, agreed that sometimes “when the interests of corporate American come up against those priorities, corporate America might lose.” But “those are pretty rare,” he said.

And a closer look at the entire scope of cases brought to the high court—not just those the justice agree to hear—gives an even more drastic picture of a court on the side of big business, Frazelle said.

The justices are largely accepting only cases for review that offer opportunities to reshape the law in favor of big business, Frazelle said. “But the court isn’t doing the opposite,” and taking up cases that offer opportunities to move the law in favor of consumer protection, environmental law, or employee rights.

So when you look at the cases that the court accepts for review and businesses win-loss record, “it’s a very skewed pool,” Frazelle said. And it “understates their true success.”

Loper Bright and *Relentless* are good examples, he said.

The cases could have been considered on narrow grounds, affecting just the herring industry and the federal marine fisheries regulator.

Instead, the Supreme Court only agreed to hear the broader issue of whether to overturn the Chevron doctrine, which applies to nearly all administrative agencies, from the Environmental Protection Agency to the Food and Drug Administration. Under that doctrine, courts must defer to an agency's reasonable interpretation of ambiguous laws.

"The very fact that the court is considering whether to reverse a well-established precedent going back 40 years" in *Loper Bright* and *Relentless* "is emblematic of the pro corporate tilt that this court has," Frazelle said.

The cases are *Loper Bright Enterprises v. Raimondo*, U.S., No. 22-451 and *Relentless, Inc. v. Department of Commerce*, U.S., No. 22-1219.

To contact the reporter on this story: Kimberly Strawbridge Robinson in Washington at krobinson@bloomberglaw.com

To contact the editors responsible for this story: Seth Stern at sstern@bloomberglaw.com; John Crawley at jcrawley@bloomberglaw.com

© 2024 Bloomberg Industry Group, Inc. All Rights Reserved

Bloomberg Law

Contact Us

View Full Desktop Site

BLAW[®] 24 / 7 Help Desk (888) 560-2529

Lawyers for Google app developers get \$26 mln in antitrust settlement

 [reuters.com/legal/transactional/lawyers-google-app-developers-get-26-mln-antitrust-settlement-2024-01-12](https://www.reuters.com/legal/transactional/lawyers-google-app-developers-get-26-mln-antitrust-settlement-2024-01-12)

Mike Scarcella

The Google logo is seen on the Google house at CES 2024, an annual consumer electronics trade show, in Las Vegas, Nevada, U.S. January 10, 2024. REUTERS/Steve Marcus Acquire Licensing Rights 

Jan 12 (Reuters) - A U.S. federal judge has approved a \$26 million payout to plaintiffs' lawyers who secured a \$90 million cash settlement for Android software developers that accused Alphabet's Google (GOOGL.O) of stifling competition in its Play app store.

U.S. District Judge James Donato in San Francisco on Thursday approved the settlement and the payment to plaintiffs firms including Hagens Berman Sobol Shapiro; Sperling & Slater; and Hausfeld.

Google agreed as part of the settlement to maintain a reduced 15% service fee until May 2025 for app developers on their first \$1 million in annual revenue. Google also said it would revise its developer distribution agreement.

The developers' case was part of a coordinated antitrust legal proceeding challenging Google's Play store practices.

Google in December lost a jury trial before Donato in a lawsuit from "Fortnite" maker Epic Games, which is seeking a court order to overhaul Play store policies. Google said on Thursday it expects to ask Donato to overturn the verdict or grant a new trial.

In another related case, states and consumers last month settled with Google for \$700 million and an agreement by Google to revamp its Play store. The state and consumer plaintiffs had alleged Google overcharged them through unnecessary fees and other restrictions on the distribution of apps.

Google did not immediately respond to a request for comment on Thursday's order in the app developers' case. Google has denied any wrongdoing.

Plaintiffs' attorney Steve Berman, who was on the team for the developers, said Donato's order means "we can now distribute to the class and that the settlement binds Google to a reduced commission which will benefit developers."

The plaintiffs' attorneys said in a filing they "advanced millions of dollars out-of-pocket" and "devoted substantial time to this litigation." They told Donato they invested 34,000 hours into the case.

Donato said the fees amounted to about 24% of the \$112 million settlement deal, which includes the \$90 million cash fund and \$22 million in savings to developers through various reforms.

The court said the attorney compensation fell within the “non-binding and informal guideline that a fee award of up to 25% may be reasonable.”

The plaintiffs’ attorneys said some class members will receive payments of more than \$200,000, and hundreds will receive more than \$20,000.

Another set of plaintiffs’ lawyers involved in the consumer and state case said they will ask for up to \$122.8 million in legal fees as part of Google’s \$700 million settlement.

Donato has not yet weighed approval of that deal.

The case is In re: Google Play Developer Antitrust Litigation, U.S. District Court, Northern District of California, No. 3:20-cv-05792-JD.

Read more:

Legal fees could top \$120 million from Google's app store settlement

Google to pay \$700 million to US consumers, states in Play store settlement

Epic Games wins antitrust case against Google over Play app store

Get the latest legal news of the day delivered straight to your inbox with The Afternoon Docket.

Corporations Should Prepare to Go Under Congressional Microscope

B

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWY5NTAtZDZiNy1hNWNmLWZiN2I5NThlMDAwMSIsImN0eHQiOiJTTE5XliwidXVpZCI6IiVpNXRLLeVpnL0YwSEdIWnRaZFFucnc9PXFxbkxIWjhmaVJUVVXxb0JxMi9zZWc9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzA4Iiwic2lnIjoV1NZUm5CUFJyNUJwd002MlpidEVmVHFoS3c0PSIsInYiOiIxIn0=

Jenner & Block's Jon Skladany and Eric Petry say that congressional committees will be under pressure this year to produce results for investigations and hearings on ESG, trade with China, tech safety, and more.

House and Senate leaders back for the second session of the 118th Congress are focused on avoiding a partial government shutdown and whether to provide additional funds for Ukraine, Israel, and the border.

Meanwhile, congressional investigators are navigating impeachment proceedings against President Joe Biden and other administration officials. Business leaders and corporate executives, however, won't avoid Congress' attention.

With dim prospects for major legislative breakthroughs that might appeal to voters, the best opportunities to deliver electoral messaging may come during high-profile oversight hearings with corporate targets.

As the presidential election approaches, investigative committees will issue findings and hold hearings to wrap up high-profile matters involving the private sector, even as the hearing calendar and House floor schedule begin to reflect impeachment and contempt proceedings.

In 2023, congressional investigators continued directing document requests and subpoenas to the private sector—where corporate targets have fewer options than their executive branch counterparts to resist and more reasons to cooperate.

Committee leaders pledged to hold certain industries accountable at the outset of the 118th Congress. The first session made clear that witnesses from outside government are fair game for oversight and policy questions that may have been previously directed to the executive branch. The second session is an opportunity for investigators to show voters the results of that oversight work.

For example, environmental, social, and governance policies—which have been a target for House Republicans since the outset of the 118th Congress—will continue to receive scrutiny from the House Financial Services and Judiciary Committees.

The Financial Services Committee has a dedicated ESG working group that put executives at proxy advisory firms on notice that invitations to testify at a hearing may be forthcoming in an interim report in June 2023. Meanwhile, the Judiciary Committee is examining ESG policies pursuant to its jurisdiction over antitrust laws.

Congress will likely also continue its focus on China, with bipartisan interest driving the agenda. The House Select Committee on the Chinese Communist Party is facing unique pressure to conclude its work given the possibility it will disband at the end of the 118th Congress.

The select committee signaled a transition from member education and policy development toward higher-profile engagements, including possible testimony from executives at multinational companies subject to the select committee's oversight during the past year.

The select committee focused on restricting US investment in Chinese companies, and other financial ties between US businesses and the CCP and the Chinese military. Company leaders may be called to testify publicly about those ties in 2024.

While the Democrat-controlled Senate's priorities and political agenda differ from the Republican-controlled House, businesses can similarly expect Senate committees to move to wrap up high-profile investigations leading into an election that could see the chamber's partisan control flip.

Tech companies in particular should watch the Senate Judiciary Committee, which has made children's online safety legislation a priority into this year. Top tech CEOs are slated to appear at a high-profile hearing on children's online safety Jan. 31, which likely will spur renewed focus on legislative proposals and could generate follow-up information requests and further examination of those companies' online privacy and safety policies.

The Senate Budget Committee is also set to continue its series of hearings focusing on climate change into 2024, which could see additional executives from the fossil fuel industry appear before the committee following an exchange of letters between committee leaders last month.

Other committees with long-running investigations, such as the Senate Finance Committee; the Senate Health, Education, Labor and Pensions Committee; the Senate Commerce Committee; and the Senate Permanent Subcommittee on Investigations, may look to finalize their work and issue reports with findings in the coming months on issues including banking regulations and labor rights.

Expect a flurry of investigative reports and hearings from House and Senate committees in July, before members leave for August recess, and again in September, before members return to their districts to campaign full-time in October.

Because subpoenas issued by House committees expire in January 2025 at the end of this Congress, any ongoing compliance disputes will come to a head during that period, which adds the possibility of contempt proceedings to the already-busy 2024 oversight agenda.

This article does not necessarily reflect the opinion of Bloomberg Industry Group, Inc., the publisher of Bloomberg Law and Bloomberg Tax, or its owners.

Author Information

Jon Skladany is special counsel at Jenner & Block and a senior adviser in Congress.

Eric Petry is an associate at Jenner & Block with broad policy, trial, and appellate experience.

Jenner & Block's John Menton also contributed to this article.

Write for Us: Author Guidelines

To contact the editors responsible for this story: Jessie Kokrda Kamens at jkamens@bloomberglaw.com; Jada Chin at jchin@bloombergindustry.com

Wells Fargo Calls ERISA Mortgage Suit 'Square Peg' in Round Hole

B [bloomberglaw.com/product/blaw/bloomberglawnews/class-action/X78DQUMC000000](https://www.bloomberglaw.com/product/blaw/bloomberglawnews/class-action/X78DQUMC000000)

Wells Fargo Bank NA and mortgage service provider Ocwen Financial Corp. are disputing a novel attempt to hold them liable as ERISA fiduciaries for mortgage-backed securities held by pension funds, telling the Second Circuit that the case doesn't "make sense."

The pension fund-filed lawsuit appears to be the first-ever attempt to argue that mortgage-servicing misconduct can violate the Employee Retirement Income Security Act if funds invest in mortgage-backed securities, the companies said in a Jan. 12 brief.

Ocwen and Wells Fargo are asking the US Court of Appeals for the Second Circuit to affirm a lower court's June ruling that the securities don't qualify as plan assets under ERISA because they're more like debt than equity.

The lawsuit's unsupported legal theory is a "square peg" in a round hole that would enable pension funds to unilaterally change the legal obligations of an "almost limitless array of companies and industries entirely unrelated to ERISA, wreaking havoc on reasonable market expectations," they said.

A pension plan's investment in an entity must be managed in accordance with ERISA, but this duty doesn't extend to the entity's underlying assets, which aren't plan assets under the statute, Wells Fargo and Ocwen said.

A retirement plan's purchase of Amazon stock "does not turn Jeff Bezos into an ERISA fiduciary," and pension plans can "speculate on wheat futures without imposing an array of obscure ERISA duties on farmers across the Midwest," they said.

The six-year-old lawsuit by the trustees of the United Food & Commercial Workers Unions & Employers Midwest Pension Fund is an unusual attempt to hold Ocwen, one of the country's largest mortgage servicers and providers, liable as an ERISA fiduciary for its conduct in servicing residential mortgages.

The pension trustees say Ocwen, with help from the bank, enriched itself at the fund's expense by forcing homes into foreclosure, thereby devaluing assets held by the fund. Under the fund trustees' legal theory, these securities are ERISA plan assets and the defendants can be held liable under the statute for exercising control over them.

Judge Vernon S. Broderick of the US District Court for the Southern District of New York rejected that theory, prompting the trustees to appeal.

His opinion, which turned on a close reading of the relevant DOL regulation, the judge said mortgage-backed securities won't qualify as plan assets if they're treated as debt under local law and have no substantial equity features.

Turning to the Second Circuit, the trustees contend Broderick's "narrow and formalistic" regulatory interpretation overlooked important context, underlying legal rationales, and the "economic realities" of investing in mortgage-backed securities.

The trustees are represented by Keller Rohrback LLP and R. Bradley Miller of Alexandria, Va. Ocwen is represented by Orrick, Herrington & Sutcliffe LLP and O'Melveny & Myers LLP. Wells Fargo is represented by Jones Day.

The case is *Powell v. Ocwen Fin. Corp.*, 2d Cir., No. 23-999, response brief 1/12/24 .

To contact the reporter on this story: Jacklyn Wille in Washington at jwille@bloomberglaw.com

To contact the editor responsible for this story: Andrew Harris at aharris@bloomberglaw.com

LensCrafters Consumers Seek Nod for \$39 Million False-Ad Deal

B [bloomberglaw.com/product/blaw/bloomberglawnews/class-action/X8N16K00000000](https://www.bloomberglaw.com/product/blaw/bloomberglawnews/class-action/X8N16K00000000)

LensCrafters customers urged a federal judge to approve a \$39 million class settlement resolving allegations that the eyewear chain duped them about the capabilities of its measuring system.

Final approval from Judge Pamela K. Chen of the US District Court for the Eastern District of New York would bring the almost six-year-old lawsuit nearer to a close.

Yesenia Ariza and others alleged Luxottica North America Retail Inc. misleadingly touted its AccuFit Digital Measuring System as “five times more precise” than traditional methods and promised clearer vision.

The consumers and Luxottica, which does business as LensCrafters, reached a settlement shortly before a scheduled trial last July.

The settlement covers all US residents who bought prescription eyeglasses from LensCrafters after Sept. 5, 2013, and were fitted with AccuFit.

Chen preliminarily approved the deal last September.

Since then, 205,485 settlement class members have submitted claims for 364,611 pairs of prescription eyeglasses, with only 39 class members opting out of the settlement, the plaintiffs said in a Jan. 12 filing seeking final approval.

Based on these numbers, class members should receive approximately \$50 per pair of eyeglasses, the filing said. That’s more than the \$23.28 per pair damages that their expert attributed to the alleged deceptive marketing, the plaintiffs said. None of the funds will revert to LensCrafters.

The plaintiffs’ attorneys are seeking \$11.5 million for their work negotiating the deal.

The requested fee—less than a third of the common fund—is standard for complex class action litigation with large common fund settlements, they said.

It’s also consistent with their lodestar amount of roughly \$10.3 million, the lawyers said. The lodestar is the amount of time spent on the case multiplied by the hourly rates of attorneys and paraprofessionals.

Chen was also asked to authorize \$8,000 service awards for the class representatives.

In 2021, the plaintiffs won class certification for certain claims under New York, Florida, and California law. The US Court of Appeals for the Second Circuit rejected LensCrafters's bid for a quick appeal of that ruling.

Cohen Milstein Sellers & Toll PLLC is class counsel. Blank Rome LLP represents Luxottica.

The case is *Ariza v. Luxottica Retail North Am., Inc.*, E.D.N.Y., No. 1:17-cv-05216, 1/12/24 .

To contact the reporter on this story: Julie Steinberg in Washington at jsteinberg@bloombergindustry.com

To contact the editor responsible for this story: Nicholas Datlowe at ndatlowe@bloombergindustry.com

Web User-Tracking Lawsuits Find New Tack in Pen-Register Theory

B [bloomberglaw.com/product/blaw/bloomberglawnews/class-action/XFNI7414000000](https://www.bloomberglaw.com/product/blaw/bloomberglawnews/class-action/XFNI7414000000)

Jan. 16, 2024, 2:05 AM PST

Tonya Riley

- Class actions say software collects signals to identify users
- California law doesn't require proof data was actually used

California class-action plaintiffs trying to target website user-tracking software they call a powerful surveillance tool are turning to a new theory of harm now that their claims filed under the state's wiretap laws have run into headwinds.

Since November, a small group of plaintiffs—represented by the same attorney—have brought more than 50 class actions in California state courts against a bevy of website operators, alleging they violated state law by installing software that acts as an illegal “pen register.” Website operators targeted in the complaints include retailers Anine Bing Corp., Stitch Fix Inc., and Primer Labs Inc.

Under the California Invasion of Privacy Act, pen registers—devices or processes that record or decode the dialing and routing information of communications, but not the contents—can only be installed pursuant to a court order. The complaints claim the code used by the accused websites operates in a similar manner, monitoring a user's activity and decoding device data to help identify sensitive information such as their location, race, age, and ethnicity.

It's the latest evolution in lawsuits challenging a rapidly growing suite of technologies that track online users, including tracking-pixel and session-replay technologies from companies such as Meta Platforms Inc. and Google Inc. So far, cases brought against retailers over practices such as violations of wiretap laws have struggled to find firm legal footing, often failing to get past dismissal motions based on jurisdiction or failure to prove information was collected without consent.

Attorneys say that the new wave of pen-register lawsuits may find better traction.

The pen-register law is “a much broader statute than the wiretapping they've been using so far,” said Crowell & Moring LLP partner Jason Stiehl. “It touches on another portion of the same kind of wiretap universe in California, that doesn't have some of these hurdles that have allowed defendants to get out of cases under the the other kind of wiretapping concepts.”

A New Theory

Previous user-tracking lawsuits largely based their arguments on two provisions: one that prohibits willful wiretapping seeking communications in transit, and another that bans recording customer calls without consent. Such complaints require plaintiffs to show not just that a monitoring device was deployed, but that it actually captured data and that its use violated an expectation of privacy.

The California law requires that plaintiffs prove a pen register was deployed without a court order or consumer consent—or without meeting one of the statute's other exceptions. Breaking the law can trigger statutory damages of \$5,000 per violation. Courts have yet to define the contours of what actions constitute separate violations, Stiehl said.

“What’s creative about it, is that a lot of the arguments that we’ve been making to defeat these things—like lack of standing or consent, or the in-transit argument that have been kind of successful out of California—go out the window, because none of those are elements of the pen register statute,” said Stiehl.

The new crop of lawsuits have all been filed by one plaintiffs’ counsel, Scott Ferrell. He has a prolific track record when it comes to CIPA-related cases, including those alleging violations of the law by chatbot and session-replay technologies. Ferrell’s known for filing dozens of identical complaints against retailers for statute violations.

His pen-register approach has caught the eye of other attorneys. Other user-tracking lawsuits, such as pixel-tracker cases in the health-care space, saw a similar progression, said Wynter Deagle, partner at Sheppard Mullin.

“You start with a almost a scattershot filing of the same complaint against a number of defendants,” she said. “And then once it catches on a little bit, you do start to see more interest from other plaintiffs lawyers.”

Sheppard Mullin has represented clients against Ferrell.

Ferrell declined to speak on the record for this story.

Kochava Provides Precedent

The wave of California class-actions aren’t the first cases to bring a CIPA claim using a pen-register theory.

In July the US District Court for the Southern District of California mostly denied a motion to dismiss a plaintiff’s claim in *Greenley v. Kochava* accusing a data broker of using its software development kit—sold to a variety of third-party apps—to collect user data. The court

rejected Kochava Inc.'s claim that the software wasn't a pen register, instead noting, "Today, pen registers take the form of software."

"As a result, private companies and persons have the ability to hack into a person's telephone and gather the same information as law enforcement," Judge Cynthia Bashant wrote in her opinion. "Perhaps for this reason, the California legislature does not limit its prohibition on installing pen registers to law enforcement."

The federal court also noted that California's law uses "expansive language" that doesn't limit what devices constitute a pen register.

"The pen-register theory is not even in its infancy yet," said Joshua Swigart, Swigart Law Group founder who served as plaintiffs' counsel in *Greenley v. Kochava*.

While *Greenley* was brought directly against a software company that developed a tracking tool, the recent wave of complaints target website operators, not the developers of the alleged pen registers.

An abstract provided by the Ferrell, the plaintiffs' counsel in the new wave, and reviewed by Bloomberg Law names ContentSquare as the software provider of these firms. However, Ferrell noted there are "dozens" of such providers.

Fight Ahead

Swigart said that while articulating the existence of a pen register may be technically simple under the statute, the real fight for defendants in these cases will be proving whether there was consent—an exception to the requirement for a court order. In *Greenley*, the court held that Kochava wasn't covered by the consent given to the third-party websites, making its interception of the data a plausible CIPA violation.

The consent questions could be more complicated for complaints directed against website operators.

"One of the arguments might be who actually is controlling the pen register, who's aware of it. Because that's not really clear," said Stiehl.

Both Deagle and Swigart noted that other California wiretapping complaints have not entirely died out. For instance, health care-related pixel tracking complaints have had increased success, due in part to pressure from federal regulators and the risks associated with the sensitive nature of health data.

To keep ahead of potential complaints, companies need to take stock of the tracking software they're using and make sure marketing and legal departments are on the same page about what it does and whether its potential return-on-investment is worth the risk,

Deagle said.

“This is the latest iteration,” she said, but that “doesn’t mean it’s the last.”

“The good housekeeping that we’re suggesting is becoming more and more important, because, as we’ve seen, this is a very heavily focused and evolving area of law that is very attractive for claims because of the statutory damages.”

“The risk level has changed,” Deagle added.

Some predicted the wave of pen-register complaints is poised to grow.

“You will see more cases piled on this pen-register theory this year for sure,” said Swigart. “It’s going to be more interesting what happens when these cases are filed in the federal court and they’re ruled on more quickly and made public.”

To contact the reporter on this story: Tonya Riley in Washington at triley@bloombergindustry.com

To contact the editors responsible for this story: Adam M. Taylor at ataylor@bloombergindustry.com; Tonia Moore at tmoore@bloombergindustry.com

Plaintiffs Firms Are Embracing Mergers to Solve Succession-Planning Uncertainty

 [law.com/nationallawjournal/2024/01/16/plaintiffs-firms-are-embracing-mergers-to-solve-succession-planning-uncertainty](https://www.law.com/nationallawjournal/2024/01/16/plaintiffs-firms-are-embracing-mergers-to-solve-succession-planning-uncertainty)

By Amanda O'Brien

What You Need to Know

- A sudden burst of plaintiffs firm mergers marked the beginning of 2024 for Pennsylvania's personal injury market.
- COVID-19 created some financial pressures on plaintiffs firms, with court delays complicating their economic model.
- Organic succession planning efforts at plaintiffs firms are complicated by recruiting concerns, such as finding time and identifying quality talent.

Mergers are becoming increasingly more common as a resolution for the succession-planning quandary at plaintiffs firms, which don't regularly restock their ranks in the same fashion as the corporate law firms they face off against in the courtroom. Case in point: three sets of personal injury firms in Pennsylvania announced mergers going into effect at the start of 2024.

In December 2023, McLaughlin & Lauricella announced it would close its doors to join Feldman Shepherd Wohlgelernter Tanner Weinstock Dodig, while in January Anapol Weiss announced it had acquired Golomb Legal and Gay & Chacker went public with a merger with Ginsburg & Associates.

"A lot of this is generational," suggested Max Kennerly, who co-founded his own plaintiffs firm based in Philadelphia. He added that the COVID-19 pandemic, which spurred an unprecedented court system shutdown, may have accelerated these generational shifts.

"The real enemy of the plaintiffs lawyer is not necessarily the wins and the losses, it's time," Kennerly explained. "If they have a lot of cases that go on for too long or [have] too long of a dry spell ... it starts to cause real friction."

Following that logic, the most recent enemy of the plaintiffs lawyer, and most litigators, was COVID and the associated court closures.

"The straight-up delay—so many things got pushed back, not weeks or even months. The calendar got punted by a year or two years or even more," Kennerly said, noting that the COVID delays created some financial pressure on plaintiffs firms.

“You can’t sustain this stuff forever if you get too long a backlog,” he said.

David Pizzica, the newly ascended managing partner of Pansini Law group, sees the sudden surge of plaintiffs firm mergers as a simpler and more supportive method of succession planning.

“Every attorney’s concern is to ensure the clients are being taken care of,” Pizzica explained. “Before anyone chooses to merge, they want to make sure clients are taken care of,” and a merger can provide not only efficiency in the transition, but a team of attorneys helping to manage a client’s case.

“When you’re merging firms, you’re merging clients,” Pizzica said.

While organic succession planning within the firm is an option, Pizzica noted that there’s an inherent risk in bringing someone new aboard with the goal of finding a successor, especially for smaller shops.

“At a one- or two-man shop, the challenge on finding a natural successor is you might need to bring someone completely fresh to the business,” Pizzica said. “Maybe they don’t ultimately work out because they don’t understand the business as well or they’re not as hard of a worker as the older attorneys view themselves.”

“That’s what might make a merger more attractive,” he continued. “There’s proven success, a proven track record and the funds in order to make that transaction a lot more doable.”

Finding the time to bring on new recruits also poses a challenge for plaintiffs firm leaders juggling business and administrative duties with legal practice.

McLaughlin Lauricella co-founder and former managing partner Paul Lauricella described being inundated with legal and administrative work as part of the reason he decided to move his practice over to Feldman Shepherd.

Following the tragic death of co-founder Slade McLaughlin, Lauricella found himself “working seven days a week and putting in all sorts of crazy hours” just to keep up with both casework and administrative work.

“When Slade died it added some new complexities to my professional life,” he said in a prior interview with The Legal. “I’ve been spending too much time as an office administrator and not enough time doing what I like to do, which is practice law.”

Pizzica suggested that plaintiffs firms’ leaders might consider bringing on a recruiter to aid in recruitment efforts, although Kennerly observed that the small-firm nature of personal injury law prevented these firms from having similarly large cohorts of associates as their corporate colleagues.

“You can’t do what corporate law firms do,” Kennerly said. “They’re large enough and they have these kind of incoming classes—there’s a regularity to it. Succession planning is very different because they tend to be quite small. ... Plaintiffs firms ... they either have employees briefly, or they have them for a really long time.”

“That person either defaults into being your succession plan or they leave and go somewhere else,” he added. “No plaintiffs firm has a regular next generation.”

As for Pizzica, he said that “if a managing partner is able to outsource [recruiting] work a little bit, it makes our lives easier, for sure.”

“Does it come at a price? Yes,” Pizzica continued. “But that price pales in comparison if they find someone who’s a hard worker and someone who can help grow and maintain the business down the line.”

NOT FOR REPRINT

© 2024 ALM Global, LLC, All Rights Reserved. Request academic re-use from www.copyright.com. All other uses, submit a request to asset-and-logo-licensing@alm.com. For more information visit Asset & Logo Licensing.

Parabellum's New \$754 Million Litigation Fund Is Among Largest

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWY5MzQtZDdkNi1hN2VmLWZiN2MyYjNmMDAwMCIsImN0eHQiOiJTTE5XliwidXVpZCI6ImZYk2ckNrWDIaUFNYbi9abklTeHc9PVVmR2d1b2pZL2E1Sm s2NXhCVUUvcVE9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzA4liwic2lnIjoiczFiR0loeWlYQm5oY29GVWgxRG1LU0Jiek5VPSI sInYiOiIxIn0=

- Fund has already committed to 50 investments
- Asset class is 'moving into a state of maturity'

Parabellum Capital, spun off 12 years ago from Credit Suisse, has closed on a \$754 million fund that is among the largest private pools raised for litigation finance.

Parabellum has committed two-thirds of the fund to 50 investments in which the firm seeks a return by paying for the cost of commercial lawsuits. Parabellum declines to identify investors who bought into the fund or name the lawsuits the pool of money is backing.

The new fund, which is Parabellum's third—and biggest—shows the rising popularity of the litigation finance industry as an option for returns that are uncorrelated to equity markets. Forty-four funders managed \$13.5 billion in US commercial litigation investments in 2022, up 9% from the previous year, according to Westfleet Advisors.

"The asset class is moving out of infancy and moving into a state of maturity," Howard Shams, chief executive officer and co-founder of Parabellum, said in an interview. "Serious people can recognize this as a way to make money over and over again with excellent results—private equity-like results."

Large players such as Parabellum are increasingly dominating the litigation finance space, while some smaller rivals fall off the radar, said Rebecca Berrebi, a litigation finance broker and consultant.

"The proof of their success is in their ability to fund-raise large amounts," Berrebi said of Parabellum. "In this market, \$700 million-plus in one fund is quite a bit. It takes a lot to raise that much capital."

Shams and Aaron Katz, Parabellum's chief investment officer, in 2006 started what was then called the legal risk strategies and finance business at Credit Suisse—the first institutional commercial litigation finance business of its kind, according to Parabellum. In the more than a decade since Credit Suisse spun it off, Parabellum has grown to \$1.45 billion in assets under management with 18 employees.

Parabellum's last litigation finance fund of \$465 million raised in 2020 resulted in 78 investments in around 400 to 500 cases. That fund is now in harvest mode—meaning it is managing cases rather than investing in new ones—and should complete its life in about a year, Shams said.

The First Fund

Parabellum's first fund closed for \$166 million and financed 55 investments, adding up to hundreds of cases. The firm sold the remaining partially-realized, and unrealized, assets from the first fund in a nine-figure secondary transaction, amounting to about half of the original investments.

Shams said the buyer is an established investment manager and the purchase returned all capital to the investors, plus profit. "Nobody's done a secondary trade of that size," he said.

The litigation finance secondary market has seen growth in recent years. In December, Omni Bridgeway announced the sale of a 25% interest in a portfolio of 15 intellectual property investments to an affiliate of GLS Capital Partners for \$21.5 million.

Parabellum's \$754 million fund included some insurance protection for around 20% of the investors, or \$158 million, which is able to be used for leverage.

While insurance markets have begun to compete with litigation finance deals and take some of the industry's top talent, there are also ways they work in tandem. Parabellum's structure is one example.

"The insurance attracts the leverage," Shams said. "Most leverage providers, they're not litigation financiers, they're coming in and they're saying, 'I'd love to lend, but I don't know how to evaluate this stuff.' But once an insurer's able to come in and say, 'We'll guarantee that you won't lose money,' at that point, it's off to the races."

To contact the reporter on this story: Emily R. Siegel at esiegel@bloombergindustry.com

To contact the editors responsible for this story: John Hughes at jhughes@bloombergindustry.com;

Audit Watchdog Urged to Oversee Corporate Climate Report Vetting

B

news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThjLWZmMjctZDdkNi1hN2VmLWZmN2Y0NTk4MDAwMSIsImN0eHQiOiJTTE5XliwidXVpZCI6InJyeWdEQU1HQVFhOWEra05iU25lUkE9PS9CUSszd3FhWkhNR2cxMkFyeGNObkE9PSIsInRpbWUiOiIxNzA1NDA3MjAzNzAxliwic2InIjoilZlxY0ZuT0lYKzNzMTthZGRpTWWhOdERCYU9RPSIsInYiOiIxIn0=

- Groups call for climate assurance standards from US audit board
- They say guidance would boost confidence in company disclosures

Consumer advocates and environmental organizations are urging the US audit regulator to issue standards for firms that review the reliability of public companies' climate-related disclosures.

The Public Company Accounting Oversight Board should address climate disclosures as part of an update to its attestation standards, the groups said in a Jan. 12 letter to board chair Erica Williams. Groups that signed the letter include nonprofit consumer advocate Public Citizen and environmental organization Sierra Club.

Typically, companies hire an audit firm or other third-party to vet their reporting and draw conclusions about the accuracy of information, in other words to attest that numbers are reliable. The PCAOB should give guidance to assurance providers to instill confidence in climate-related disclosures as companies face new reporting mandates in California and elsewhere, the groups said.

Last year, California enacted a law requiring that by 2027 large companies with a presence in the state report greenhouse gas emissions from their operations and throughout their supply chain. The Securities and Exchange Commission is expected to finalize a rule later this year that would apply similar reporting requirements to publicly traded companies across the US, though it is not clear if the rules would go as far as California on indirect emissions.

The PCAOB declined to comment on the advocacy groups' letter.

The board, which oversees audits of US-listed companies' financial statements, has said previously that it had no plans to address climate data in its standard-setting or research projects. Its main advisory group has questioned whether the board would have the legal authority to write standards that go beyond its remit.

Other signatories to the letter include groups focused on financial regulation such as Americans for Financial Reform Education Fund and Better Markets.

There's a lack of standardization around assurance for disclosures on issues like greenhouse gas emissions, resulting in market confusion about the quality of such reporting, the letter said.

"Rigorous attestation standards are needed to prevent assurance providers from rubber-stamping inaccurate climate-related disclosures, ensuring the investors receive credible information to inform their decisions," Mekedas Belayneh, policy advocate with Public Citizen's climate program, said in a statement.

To contact the reporter on this story: Andrea Vittorio in Washington at avittorio@bloombergindustry.com

To contact the editors responsible for this story: Amelia Gruber Cohn at agrubercohn@bloombergindustry.com; Jeff Harrington at jharrington@bloombergindustry.com

Ex-Regulator's Assets Remain Frozen in FirstEnergy Bribe Row (1)

B [bloomberglaw.com/product/blaw/bloombergterminalnews/bloomberg-terminal-news/S7D2RPT0AFB4](https://www.bloomberglaw.com/product/blaw/bloombergterminalnews/bloomberg-terminal-news/S7D2RPT0AFB4)

Jan. 16, 2024, 7:52 AM PST

Eric Heisig

Bloomberg Industry Group

- Justices said appeals court improperly analyzed freezing order
- Case stems from massive FirstEnergy corruption investigation

By Eric Heisig

(Bloomberg Law) --

The Ohio Supreme Court on Tuesday reinstated a trial court judge's order that froze millions of dollars worth of a now-indicted former state utility regulator's assets after he was implicated in a massive bribery probe involving FirstEnergy Corp.

The state's high court said the Tenth District Court of Appeals erred when it reversed a "prejudgment attachment" order issued against former Public Utilities Commission of Ohio Chairman Samuel C. Randazzo's assets without his knowledge.

The opinion doesn't mark a change in the status of Randazzo's assets, though, as the justices re-froze them pending their own ruling. The case is also about litigation that was filed before he was indicted on federal charges last month.

The Columbus-based appeals court focused on the issuance of the ex parte order said the state hadn't properly shown that it would "suffer irreparable injury if the order is delayed until the defendant against whom the motion has been filed has been given the opportunity for a hearing."

The problem is that an appeal must flow from denial of a motion to vacate, Justice R. Patrick DeWine wrote. He added that an asset's owner may file such a motion and request a hearing, which Randazzo did.

"Once the other side has had an opportunity to be heard," DeWine wrote, "there is no longer any effective relief that can cure a trial court's erroneous decision to grant an attachment ex parte."

The justices also shot down the Tenth District's assertion that the state used the wrong forms to freeze Randazzo's assets and said that the former regulator wasn't harmed by their use.

The justices were mostly unanimous in their decision, though Justice Patrick F. Fischer wrote separately to address the use of the incorrect forms. While the state said the Franklin County Clerk of Courts' office didn't have the right forms available, Fischer said that isn't an excuse.

"While I concur in the majority opinion, I respectfully wish to also caution future litigants that their failure to follow statutory procedures could result in this court finding reversible error under different circumstances," Fischer wrote.

The opinion stems from a massive federal corruption probe, which included an investigation into the passage of a legislative package in 2019 that bailed out two nuclear power plants owned at the time by the Akron-based utility FirstEnergy. The probe ultimately led to a \$60 million racketeering case against former Ohio House Speaker Larry Householder (R), who is serving a 20-year prison sentence, and four others.

FirstEnergy struck a deal with federal prosecutors in 2021 in which it agreed to pay \$230 million and cooperate. In a deferred prosecution agreement, it admitted to bribing Randazzo with \$4.3 million in exchange for favorable treatment when he later became chair of the Public Utilities Commission of Ohio. Randazzo's lawyer Roger P. Sugarman, during oral arguments in the frozen assets case last June, described FirstEnergy's admission as no more than an "allegation."

The FBI raided Randazzo's house in November 2020, and federal prosecutors charged him in December with a bevy of bribery, fraud, and other charges.

Ohio Attorney General Dave Yost (R) sued Randazzo and his company Sustainability Funding Alliance of Ohio Inc. in 2021. He sought to freeze his assets after the ex-regulator allegedly gave his son a house worth \$500,000 and sold four other real estate properties for more than \$4.8 million. All these transactions happened after the FBI raid, the attorney general said.

Franklin County Common Pleas Judge Christopher Brown ordered the prejudgment attachment for up to \$8 million of Randazzo's assets. However, the Tenth District said the judge didn't sufficiently justify freezing Randazzo's accounts.

Charles M. Miller, special counsel for the Ohio Attorney General's Office, said during his oral argument that about \$900,000 of Randazzo's money held in banks and with a brokerage firm is frozen. An additional \$3 million is in attorney-trust accounts, and Randazzo's lawyers agreed to hold it pending the outcome of the Ohio Supreme Court case, Miller said.

Randazzo is also represented by Allen Stovall Neuman & Ashton LLP.

The case is *Ohio ex rel. Yost v. FirstEnergy Corp.*, Ohio, No. 2022-1286, 1/16/24.

To contact the reporter on this story: Eric Heisig in Ohio at ehesig@bloombergindustry.com

To contact the editor responsible for this story: Alex Clearfield at
aclearfield@bloombergindustry.com

(Updates with additional information from the opinion.)

State can seize Randazzo assets, high court rules

B [toledoblade.com/local/courts/2024/01/16/state-can-seize-randazzo-assets-high-court-rules/stories/20240116107](https://www.toledoblade.com/local/courts/2024/01/16/state-can-seize-randazzo-assets-high-court-rules/stories/20240116107)



Jim Provance

The Blade

jprovance@theblade.com

Jan 16, 2024

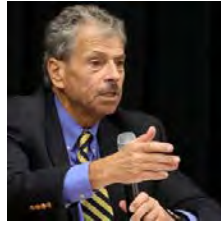
10:18 AM

COLUMBUS — The state can freeze the assets of indicted former chief utilities regulator Samuel Randazzo pending trial, the Ohio Supreme Court unanimously ruled on Tuesday.

The appeal had been initiated by Ohio Attorney General Dave Yost prior to the indictment of the former chairman of the Public Utilities Commission of Ohio on federal bribery and embezzlement charges. The decision reinstates a Franklin County Common Pleas Court order to allow the state to garnish \$8 million in Mr. Randazzo's assets, an order that had been overturned by the 10th District Court of Appeals.

The Supreme Court opinion was written by Justice Pat DeWine, son of Gov. Mike DeWine, who had appointed Mr. Randazzo to the powerful post despite warnings to his administration of his close ties to Akron utility giant FirstEnergy Corp.

The utility later said in a deferred prosecution agreement in which it paid a \$230 million fine that it had paid a \$4.3 million bribe to Mr. Randazzo, via his Sustainability Funding Alliance of Ohio, Inc., as he moved from a contracted consultant for the corporation to the state post.



Tom Henry

Former PUCO Chief Sam Randazzo gets indicted on 11-counts, drawing swift response

FirstEnergy said it expected preferential treatment from the new PUCO chairman as a result. Mr. Randazzo has pleaded not guilty to federal charges brought later.

Mr. Randazzo resigned as PUCO chairman in 2020. The state offered evidence that Mr. Randazzo had moved immediately to sell off properties that he owned following an FBI raid of his Columbus home, but the former PUCO chairman said the state failed to follow proper procedure in going after his assets.

The Supreme Court ruled that the district appeals court was wrong to have overturned the order to freeze Mr. Randazzo's assets. The state maintained that Mr. Randazzo could ultimately be liable under law for \$12.9 million in damages — triple the amount of the alleged bribe.

All of this is related to the federal racketeering convictions of former Ohio House Speaker Larry Householder and former Ohio Republican Party Chairman Matt Borges and the guilty pleas of two of their allies.

Householder is serving a 20-year sentence for his leadership role in a scheme in which FirstEnergy paid most of the cash in a \$61 million scheme to return Householder as House speaker so that he could usher through a bill providing a \$1.3 billion, customer-financed bailout of two struggling nuclear power plants then owned by a subsidiary.

Borges is serving five years, primarily for his role in successfully killing a subsequent petition effort that could have subjected the new House Bill 6 to voter repeal. He paid a \$15,000 bribe to a manager of the petition effort in hopes of getting inside information on its progress and tactics.

Mr. Yost moved to freeze the assets of these defendants and FirstEnergy players in the wake of the first July 2020 indictments and then added Mr. Randazzo to the list after the accusations leveled by FirstEnergy.

Despite what was essentially a corporate plea deal, no current of former executive associated with FirstEnergy or subsidiary FirstEnergy Solutions has been charged to date.

The state told the Supreme Court that, soon after the FBI raid, Mr. Randazzo transferred a house worth more than \$500,000 to his son for nothing, sold two Florida properties for \$4 million, sold two Ohio properties for about \$800,000 total, and wired millions from a brokerage account to an out-of-state law firm.

“We are pleased that the court recognized that Mr. Randazzo cannot spend down his bribe proceeds and render himself judgment-proof,” Mr. Yost said.

The 10th District had overturned the original order allowing the freezing of the assets, determining that Mr. Randazzo had not been given an opportunity and that the state had failed to show it would “suffer irreparable injury” if the order were delayed until after such a hearing.

“Randazzo had a right to appeal the trial court’s denial of the motion to vacate the attachment,” Justice DeWine wrote. “But he did not have a right to challenge the trial court’s conclusion that irreparable injury was likely to occur unless it issued the order” without a hearing.

While he agreed with the majority’s ruling, Justice Patrick Fischer raised concern about the state’s admission that it failed to follow the correct procedures in the case, improperly filing forms indicating that it had already frozen \$8 million when it was still going after \$4.3 million, the amount of the alleged bribe.

First Published January 16, 2024, 6:54am



Jim Provance

Follow to receive notifications any time Jim Provance publishes a new story

45 Followers

Join the Conversation

We value your comments and civil discourse. Click here to review our Commenting Guidelines.

Loading...

Morgan Stanley Agrees to Pay \$249 Million to Resolve Block Trading Investigations

 [law.com/nationallawjournal/2024/01/12/morgan-stanley-agrees-to-pay-249-million-to-resolve-block-trading-investigations](https://www.law.com/nationallawjournal/2024/01/12/morgan-stanley-agrees-to-pay-249-million-to-resolve-block-trading-investigations)

Morgan Stanley has agreed to pay \$249 million to resolve federal investigations into its block trades business, officials at the U.S. Attorney's Office for the Southern District of New York and the U.S. Securities and Exchange Commission announced Friday.

U.S. Attorney Damian Williams of the SDNY also announced that Morgan Stanley has entered into a non-prosecution agreement and that Pawan Passi, the former head of the bank's U.S. equity syndicate desk, has entered into a deferred prosecution agreement.

Passi admitted that, between 2018 and 2021, he promised equity block sellers that the bank would keep information about their potential sales confidential, but he shared that information to buy-side investors knowing the investors would use it to trade ahead of block sales, prosecutors said.

Passi is represented by Milbank partner James Cavoli, and Morgan Stanley is represented by Sullivan & Cromwell.

The SEC's order found that Passi and Morgan Stanley each violated Section 10(b) of the Securities Exchange Act and that the bank also violated Section 15(g). Morgan Stanley was ordered to pay \$138 million in disgorgement, \$28 million in prejudgment interest and an \$83 million civil penalty.

The SEC announced that the disgorgement and prejudgment interest will be considered "partially satisfied" by the \$136 million in forfeiture and resolution paid by the bank as part of the criminal resolution.

Morgan Stanley's non-prosecution agreement requires the bank to cooperate with and provide information to the government for at least three years. The NPA filing notes that the bank did not receive credit for voluntary disclosure but did receive full credit for "its extensive cooperation with the United States' independent investigation."

"As the Statement of Facts makes clear, the Government's investigation uncovered the misconduct at Morgan Stanley," Williams said in a statement. "This fact serves as a reminder that we are watching. And we will continue to use all the tools at our disposal to root out fraud in our financial markets."

Williams emphasized that the resolution also demonstrates that his office is willing to “evaluate each case and each prosecution on its facts and circumstances” and consider alternatives to prosecution, including declining to prosecute or entering into NPAs and DPAs.

“Here, with respect to Morgan Stanley, while many factors weighed in Morgan Stanley’s favor, including extraordinary cooperation and remediation, the misconduct was not uncovered and voluntarily disclosed,” he said. “Morgan Stanley now must comply with the terms of the NPA for the next three years and have a criminal resolution with the U.S. Attorney’s Office on its permanent record.”

A Morgan Stanley spokesperson said the bank is pleased to resolve the matter.

“We are pleased to resolve these investigations and are confident in the enhancements we have made to our controls around block trading, including strengthening our policies, procedures, training and surveillance,” the spokesperson said. “The core of this matter is the misconduct of two employees who violated the Firm’s policies, procedures and our core values, as outlined in the settlement documents.”

NOT FOR REPRINT

© 2024 ALM Global, LLC, All Rights Reserved. Request academic re-use from www.copyright.com. All other uses, submit a request to asset-and-logo-licensing@alm.com. For more information visit Asset & Logo Licensing.

Morgan Stanley Banker Was 'Daddy' to Hedge Fund He Tipped (1)

B [bloomberglaw.com/product/blaw/bloomberglawnews/securities-law/X8508H7C000000](https://www.bloomberglaw.com/product/blaw/bloomberglawnews/securities-law/X8508H7C000000)

For years, hedge funds knew that one man at Morgan Stanley could make them millions.

A big block of shares would come up for sale, and block-trading head **Pawan Passi** would tip off the funds. One even told Passi he had put that investor “in the game” (adding a colorful modifier) and that the investor “would be at the kiddie table” if not for him.

“I know who my daddy is,” the investor said in a call, according to federal prosecutors.

On Friday Passi entered into a deferred-prosecution agreement with the US Justice Department, in which he pleaded not guilty to securities fraud, to settle a long-running probe into his and Morgan Stanley’s trading practices. He mishandled confidential information, he acknowledged, agreeing to a one-year ban from the brokerage business.

Pawan Passi arrives at court in New York on Friday.

Photographer: Alex Kent/Bloomberg

That agreement and the bank’s own nonprosecution deal with the US, which Bloomberg reported on Thursday, come after a years-long descent for Passi, once a beloved member of Morgan Stanley whose desk brought in \$1.4 billion in revenue from 2018 to 2021.

Read More: [Morgan Stanley to Pay \\$249 Million to End Block Trade Probes](#)

Passi’s fall also scarred Morgan Stanley, which agreed on Friday to pay a total of \$249 million to the Justice Department and the Securities and Exchange Commission to settle their probes into its block-trading business. Its pact allows the bank to avoid criminal charges.

Gray Areas

Talks with investors about block trades — purchases or sales of amounts of stock big enough to move the share price — often occur in legal gray areas. Bankers routinely canvass prospective buyers about their hypothetical interest in specific stocks. They take care not to leak deals that are actually in the works.

QuickTake: [How Block Trades Work and Why They Arouse Suspicions](#)

Except when they don’t. Prosecutors outlined a case against Passi and the bank that included years of alleged leaks, lies and compromised confidential information.

Here's what the government claimed:

- For years Passi and another employee at the bank's market-leading equities syndicate desk, who wasn't charged, told select investors about upcoming sales of large blocks of shares of public companies — information they had promised to keep to themselves. In multiple instances, the investors shorted the stock ahead of the sale.
- The equities-syndicate desk was contacted in 2018 about a block of 10 million Canada Goose shares. That same day, an investor asked a desk employee whether there was anything he should be focusing on. "How is your store of cold weather jackets," the employee replied. The investor made a \$760,000 profit from shorting the stock, according to prosecutors.
- In another instance, involving a 2021 sale of millions of shares of Star Bulk Carriers Corp., Passi told the seller that he would keep the prospective sale confidential. He proceeded to share the details of the negotiations of the sale with a hedge fund "on an almost daily basis." The fund then shorted Star Bulk Carriers on its very first trade in the company's shares. It would later buy a chunk of the block to cover its short.
- Passi even suggested to hedge funds how they should trade ahead of upcoming block trades he was running, and many took short positions. He then promised "favored buy-side investors" they would get enough of the allocation of the block trade to cover their shorts.
- Suspicion of such leaks spread not only on the Street — some perhaps driven by envy of Morgan Stanley's block-trading success — but also within the bank itself. Investors were too perfectly positioned to make money on the trades, one employee said. "How are they set up for every one of these f—ing things?!" the employee asked Passi in August 2021.
- The question came after a suspect move in iHeartMedia Inc. shares the day the bank was executing a block trade on behalf of a client. Passi blamed a different bank for leaking information about the deal. The day before, he had sent information about the trade to a hedge fund that was shorting the media company.

Morgan Stanley said in a statement that "the core of this matter is the misconduct of two employees who violated the firm's policies" and that it is "confident" in its enhanced controls. Passi's lawyer George Canellos said earlier that he was pleased the government didn't pursue a criminal conviction of his client.

The SEC has been concerned for years about potential abuses in the highly secretive world of block trading. Executives overseeing the practice had privately expressed doubts that authorities would find anything.

In the end, Passi — the center of the government's case — can move to have the charge against him dismissed after six months if he abides by the terms of his agreement. And Morgan Stanley, accused of lax controls over how it handled confidential information, had to concede that it engaged in misconduct and pay a fat penalty but escaped criminal prosecution.

A 'Win for Everybody'

Richard Hong, a former SEC enforcement official now at the law firm Morrison Cohen, called it “a meaningful case for the SEC and DOJ,” though not one he expects to change the industry overnight.

“This is not going to shake the Earth,” Hong cautioned.

Still, he said, “it’s a win for everybody. The government gets a major fine and tells Wall Street that it has to block-trade by the book. And Morgan Stanley gets to move on from this without any lasting damage, and clean the closet for their new CEO.”

At Passi’s court appearance Friday, the judge had some advice.

“You have been given a real opportunity here today to avoid a criminal conviction,” US Magistrate Judge **Robyn Tarnofsky** told Passi in approving his deal with the government. “I hope this is the only time I see this case again.”

(Updates with Canada Goose bullet item)

To contact the reporters on this story:

Austin Weinstein in Washington at aweinstein18@bloomberg.net;

Sridhar Natarajan in New York at snatarajan15@bloomberg.net;

Ava Benny-Morrison in New York at abennymorris@bloomberg.net

To contact the editors responsible for this story:

Peter Jeffrey at pjeffrey@bloomberg.net

Peter Blumberg

© 2024 Bloomberg L.P. All rights reserved. Used with permission.

Morgan Stanley Leaked Some Block Trades

B [bloomberglaw.com/bloombergtterminalnews/bloomberg-terminal-news/S7D7J6DWRGG0](https://www.bloomberglaw.com/bloombergtterminalnews/bloomberg-terminal-news/S7D7J6DWRGG0)

By Matt Levine

(Bloomberg Opinion) --

Block trades

Here's a simple model of a block trade. There's a public company, its stock trades on the exchange, its current price is \$100. A big shareholder wants to sell a block of a million shares. This will drive down the price: supply and demand, more sellers than buyers, etc. Let's say that fully selling all of the shares will drive the price down by \$3.

You're a bank, and the seller comes to you and says: "I want to do a block trade. I want you to buy all this stock at a firm price and resell it at your own risk. You have to buy it after the market closes in two hours; I'll call you for your bid then." How much should you bid? Well, on my numbers in the previous paragraph, the stock is at \$100, selling all the shares will take \$3 off the price, and you'll be able to resell it at \$97. So you should bid, like, \$96, to add a little cushion (in case that \$3 estimate of the price impact is wrong) and some profit for you.

But in fact the stock will move around over the next two hours. Maybe in two hours it'll be \$99, or \$101. And reselling the stock will drive it down by \$3. So really your bid should be (1) whatever the closing price is in two hours minus (2) say, \$4 (the \$3 effect of the sale, plus \$1 for your profits). And in fact the seller will probably ask you for a bid that is not a dollar price but a discount (percentage or dollars) to the last sale price. If the stock closes at \$99.73 and your bid is "down \$4" then your bid is \$95.73.

You have two hours to come up with your bid. You have two goals:

1. *Accuracy*: You want your bid to accurately reflect the price at which you can resell the stock (plus a little profit for you); you don't want to pay \$98 if you'll have to resell the stock at \$95.
2. *Competitiveness*: The seller is probably calling a bunch of banks, and will take the highest price (the lowest discount to the last sale). So you want to offer the highest price.

Here is a good trick: You spend those two hours *selling all the stock*. You pre-sell the million shares that the seller is offering; you sell them short. As you do this, naturally, the price declines, from \$100 to \$97, to reflect all of that selling. (Also maybe other stuff happens — maybe there's economic news or other big buyers or sellers or whatever — so the stock

ends up at \$96 or \$98 or whatever, but the \$3 effect of all the selling is fully incorporated into the price.) And then at the end of that process you go to the seller and bid “down \$1”: That is, you’ll pay \$1 less than the last price; if the last price was \$97 you’ll pay \$96.

Now, two things are true:

1. Your bid is more accurate. You already know the price you can get for all that stock, because you’ve already sold it. If you sold it at \$97 and bid \$96, you have \$1 of profit that is totally safe.¹
2. Your bid is *tighter*, more competitive. Instead of bidding “down \$4,” as you would have in the naive case, you bid “down \$1,” because the \$3 impact of selling the stock is already reflected into the price.

Notice that your bid is not *actually better*: In the naive case, the stock is at \$100 and you bid down \$4 (\$96) to reflect the likely impact on the price of reselling all the stock. In the pre-selling case, the stock is at \$97 and you bid down \$1 (\$96) because you’ve already resold all the stock. Either way the seller gets \$96.

But if you are in competition, your competitors don’t know that you’ve pre-sold the stock. They see the closing price of \$97 and think that that reflects the market’s valuation of the stock; they think that reselling the million-share block will require *another* \$3 price drop. So they bid “down \$4” — the naive bid — which works out to \$93. And you bid \$96, you win, you get the stock, and you make an easy \$1 profit.

There are some problems with this trick. One is, if you do it and *don’t* win, you’ve pre-sold all this stock and don’t get to buy it at a discount; you have to go and cover your short in the market and might lose money. What if another bank does the same trick? Then, between you, you’ve sold *two* million shares, the price has gone down *too* far, and whoever loses the auction will have to buy back the million shares at higher prices. What if five banks do this trick?

There are ways to mitigate this risk. A simple one is, instead of actually pre-selling the stock yourself, you just call up the likely buyers — the big hedge funds that tend to buy block trades — and say “hey, got one coming for Amalgamated Widgets, you in?” And then the hedge funds give you an order, and *they* short the stock, and it goes down to \$97, and you proceed as above, bidding \$96 and winning the auction, and you sell them the stock at \$96.50 and they make money and you make money. This moves the risk from you to the hedge funds.²

Another problem with this trick is that it is pretty bad customer service. It *looks* like good customer service: You can give the seller a tight bid on the block, and then resell it quickly and efficiently. But it is *actually* bad customer service, because you drive down the price ahead of the block trade and make the auction for the seller’s shares less competitive.³

Ordinarily sellers will swear you to secrecy; they will call you up and say “I want you to bid on this block, but don’t tell anyone that it’s coming.” If the seller finds out that you did pre-sell the shares, or that you leaked the news to hedge funds to pre-sell the shares, they will be mad at you.⁴

A third problem with this trick is that it is ... I was about to say “very illegal,” but apparently it is only, like, the regular amount of illegal. Possibly less. It is mildly illegal? (Not legal advice!) It is a form of *insider trading*, or rather front-running: Your client (the big shareholder) called you and said “I want to sell stock after the close today,” and probably swore you to secrecy, and then you went and traded on it, or told hedge funds to trade on it, so you could make more money for yourself with less risk. You had nonpublic information about a big shareholder’s plans to sell, that information was material, you had a duty to keep it confidential, and instead you used it to tip off some hedge funds (or trade yourself) to make money for yourself.

A certain amount of illegal. On Friday, the US Securities and Exchange Commission and US federal prosecutors in Manhattan settled a case against Morgan Stanley and Pawan Passi, its former head of US equity syndicate. “Equity syndicate” is the desk that does this stuff; specifically:

1. When big shareholders ask for a price on a block trade, equity syndicate is the desk that gives them the price.
2. When Morgan Stanley wins a block trade, equity syndicate is the desk that coordinates selling the shares out to investors.
3. When big shareholders ask for a price on a block trade, equity syndicate is *the desk that calls potential investors and say “hey what price would you pay for this block?” to formulate its bid.*

Oh, I mean, not really; No. 3 is illegal. But kind of. Certainly Pawan Passi did that, though now he is the *former* head of equity syndicate. The SEC says:

Selling shareholders or their agents then typically send a bid-wanted-in-competition (“BWIC”) email to the investment banking firms that had expressed an interest on the initial outreach calls. BWICs are typically sent to firms two to three hours before the market close. They reiterate the information provided on the outreach call (the seller’s identity, the stock, and size of the block), request bids by 4:05 pm ET that day, and set forth the confidential auction process. BWICs typically pre-condition a firm’s participation in the auction process on the firm agreeing to keep information about the potential block trade confidential. Selling shareholders or their agents require the select group of auction participants to keep such information confidential because if the market becomes aware of an imminent block trade, as stated above, the price of the stock might decline, and the seller might receive a worse price from the auction. ...

During the Relevant Period, Passi disclosed non-public, potentially market-moving information received from selling shareholders or their agents about block trades to certain potential purchasers of the block, including a portfolio manager (“Portfolio Manager A”) in the London, England office of a Hong-Kong-based hedge fund (“Hedge Fund A”) while the auction process was ongoing. ...

Passi provided this information to Portfolio Manager A with the understanding that he would take large short positions in the stock in anticipation, and prior to the execution, of the block trade, and that, if Morgan Stanley won the auction, Portfolio Manager A would request and receive allocations from the block trade to cover those short positions.

Passi knew that providing information about block trades to buy-side investors, such as Portfolio Manager A, could cause the stock price to decline if those investors sold significant amounts of stock in advance of the block trade.

Portfolio Manager A’s pre-positioning activities benefitted Morgan Stanley as they ensured that there would be a large buyer for at least a portion of the block trade, thereby lowering Morgan Stanley’s risk on the transaction, and giving the firm comfort to offer a tighter and more competitive bid.

It seems that Passi called several investors to place a bunch of the stock (and thus largely de-risk Morgan Stanley’s bid), but it’s not clear how methodical he was; it’s possible that he just called a few of his favorites. For instance this guy, from the criminal statement of facts:

Hedge fund investors who received confidential information from the Head of the Desk [Passi] and Employee-1 about upcoming blocks recognized that this information allowed them to profit in ways they otherwise would not have. For example, an investor working at a Nevada-based hedge fund (“Investor-3”) told the Head of the Desk in an August 2021 call, “I know who my daddy is,” referring to the assistance that the Head of the Desk had provided Investor-3 in profiting from block trades. Investor-3 stated in the same call, again referring to block trades, that the Head of the Desk had “put [Investor-3] in the ... game,” and that Investor-3 “would be at the kiddie table if it wasn’t for” the Head of the Desk.

Because, yes, if you do this right, it is nearly risk-free profit for the hedge fund (who shorts the stock during the day and then gets it back at the close at a discount to the trading price) and for Morgan Stanley (who locks in buyers a higher price than it agrees to pay the seller). You don’t need to be a big or good hedge fund to get the call for this trade; you just need to be a loyal friend of Passi’s.

Anyway, two related points. One is that this is *illegal*, but it’s on a continuum. As a general matter, when you want to sell a large block of stock, you have to balance your desires to (1) tell everyone, to drum up buyers and (2) tell no one, to avoid anyone front-running you. In different circumstances, you might strike that balance in different ways. *Sometimes*, it is *good* customer service for Morgan Stanley to “socialize” a block trade before bidding, to pre-market it before actually doing the trade. Ordinarily to do that you’d wall-cross the investors first: You’d call them up to ask “hey would you buy this block,” but only if they first promise not to short the stock ahead of the trade. In fact Morgan Stanley marketed that service; from the statement of facts:

When Morgan Stanley’s marketing materials referenced investor outreach, the materials suggested that such outreach would be done only to investors that had been wall-crossed. Sellers were told that while block trades were one option for selling their shares, another option was an “overnight with wall-cross and backstop,” which was described as a registered sale that would “launch[] publicly after wall-crossing several investors capable of acting as anchor investors.” The stated advantage of this “overnight with a wall-cross” was that “anchor investor feedback helps provide early pricing insight ahead of public launch.” In other slides shown to potential sellers, the possibility of wall-crossing a select number of investors “ahead of launch to maximize demand visibility/pricing” was offered as a possible way to execute a registered block trade.

It’s just that, when sellers instead chose to do block trades without pre-marketing, Passi pre-marketed the shares anyway — not to benefit the client but to benefit Morgan Stanley. (Also Passi “did not wall cross any investors before sharing confidential information about the Relevant Blocks with them.”)

Even without wall-crossing, though, there are some gray areas about what sort of information-gathering a syndicate desk can do before putting in a bid. Like:

- Calling up some hedge funds at 2 p.m. and saying “hey we got a block of Amalgamated Widgets coming after the close today, are you in? If so you should short the stock now”: pretty illegal.
- Calling up some hedge funds at 2 p.m. and saying “just hypothetically, how are you feeling about the widget sector these days,” to get a sense of investor demand: maybe okay?

You can get some deniability on these calls. Though some sellers know to look out for this; the SEC notes that one selling shareholder’s agent sent Morgan Stanley a bid-wanted-in-competition request that said:

Prior to the purchaser being selected, please do not engage in any discussion with potential investors or purchasers, even hypothetical ones, including discussions in which several names are mentioned in order to solicit general interest.

The other point is that this is illegal, but apparently not *that* illegal. Morgan Stanley paid a total of \$249 million of penalties to the SEC and \$153 million to the Justice Department, though there is overlap in those numbers. (And some of the payment is for restitution to the block sellers who got ripped off.) Meanwhile Passi will pay \$250,000 to the SEC and agreed to a deferred prosecution agreement in the criminal case: He has to “demonstrate good behavior and fulfill the terms of the DPA, in which case PASSI will not be further prosecuted criminally.” So it’s not quite *real* insider trading: If you do this stuff they don’t send you to jail; you get a warning first.

Oh Elon

The most normal way to be a tech entrepreneur goes something like this:

1. You take your best idea and found a company to do it.
2. If you need more money to do the idea, you raise capital from outside investors, lowering your ownership of the company from 100% to 50% or 20% or 10% or whatever, depending on how much money you need and what valuation the investors are willing to give your idea.
3. If you have some additional ideas, well, you’ve already got this company, it’s already got capital, it’s probably making money, so you might as well have the company do the other ideas too.

So Mark Zuckerberg had an idea for putting Harvard’s facebook on the internet, and this turned out to be a gajillion-dollar idea, though it did require enough outside capital and cofounders and so forth that he now only owns about 14% of the company that did it.⁵ But

now that company generates oceans of cash, which Zuckerberg has used to get into things like artificial intelligence and “the metaverse.” To the point that the company he founded to put Harvard’s facebook on the internet, Facebook, is now called Meta Platforms Inc., because it’s not just a facebook anymore. Zuckerberg keeps having ideas, and Meta keeps reflecting these ideas.

This is not the only way to do things, and it is in some corporate finance sense not the *optimal* way to do things. Consider an entrepreneur who has *two* ideas. One is a simple consumer-facing app that she could code herself in an afternoon and that she thinks will be wildly popular, lucrative, and cheap to scale. The other is, like, “build rocket ships,” and will be incredibly capital-intensive.

Clearly she should start *two* companies. For one thing, there are no special synergies between her two projects: Maybe the consumer-app project and the rocket-ship project could share, like, an accountant, but there’s no reason to think that the equipment and tools and engineers and salespeople for one project would do much good on the other project.

Also, though, as a matter of her personal economic interests, the rocket-ship company is going to require a ton of outside capital, so she won’t own all that much of it — she’ll own 20% or whatever of the company, with the rest going to the outside investors who give her money to build the rockets. Whereas the consumer-app company she can just build herself for free and own 100% of the profits. There is no reason for her to build those two projects in one company and give 80% of the profits of the consumer app to the rocket-ship investors. She can raise outside capital for the capital-intensive projects, giving up some ownership of those projects, but keep the capital-light projects for herself.

Similarly, an entrepreneur with, like, 20 ideas should arguably start 20 different companies to do them: Why share any of the profits of any of the ideas with the outside investors in any of the others? Give up only as much ownership of each idea as you need to fund that idea.

Though at that level things get trickier. You might be able to raise money at a higher valuation for “here’s a slew of good ideas” than you would for each individual idea, though maybe not. In any case, you will probably be able to raise money at a higher valuation if you tell your investors “this company has my full attention and I will devote myself night and day to its success, since it represents substantially all of my net worth,” than if you tell them “meh I got a lot of irons in the fire but I promise to work on this company from 9 a.m. to 11 a.m. most Tuesdays.” Tech investors like to think that they are backing an entrepreneur, not just an idea: If they look you in the eye and shake your hand and believe in your talent and drive, they will happily give you money for whatever your current idea is, and be happy to let you pivot to another idea if the first one doesn’t work. If you only sell them one idea and keep the other 19 for yourself, then they are not really getting the deal they want.

Elon Musk does not have literally 20 companies, but he does have a lot. And his investors do seem unusually content to back *him*, as a person, as a visionary tech entrepreneur, while only getting a small portion of his attention. And now he's using that for leverage? Bloomberg's Edwin Chan and Linda Lew report:

Elon Musk leaned on Tesla Inc.'s board to arrange another massive performance award for him after he sold a significant chunk of his stake in the company to acquire Twitter.

In one of several posts on the topic, Musk wrote that unless he has roughly 25% voting control at Tesla, he'd prefer to build artificial intelligence and robotics products elsewhere. While he remains the carmaker's biggest shareholder with an almost 13% stake, he cashed in almost \$40 billion worth of shares in 2022 to help fund the Twitter deal.

Musk, 52, praised Tesla's board in other posts and said directors were waiting for a Delaware Chancery Court ruling before preparing another compensation plan. Judge Kathaleen St. J. McCormick — who also presided over Musk's ill-fated attempt to get out of the Twitter deal — will decide a case brought by a Tesla shareholder who alleges Tesla's board failed to exercise independence from Musk as it drew up his \$55 billion performance award in 2018. ...

Musk's claim that he's "uncomfortable growing Tesla to be a leader in AI & robotics" follows repeated boasts over the years that the company was a leader in the fields. Tesla markets products it calls Autopilot and Full Self-Driving — both of which are driver-support features — and has been developing a humanoid robot called Optimus. ...

In July of last year, Musk announced the formation of xAI, a startup that aims to rival Microsoft Corp.-backed OpenAI and Google's Deepmind. A week later, an analyst asked him during a Tesla earnings call whether the new AI company would overlap with, compete with or enhance the value of the carmaker's AI efforts. He said the latter.

I laid out the theoretical corporate finance considerations above and, sure, Tesla's car factories are capital-intensive while some of Musk's software projects are maybe less so. But that's not really what's going on here. What's going on here is:

1. Musk started Tesla, ⁶ raised outside money, and still owned about 20% of it.
2. He then *sold* a big chunk of that stake to raise cash, for himself, to buy another company (Twitter) in his personal account (*not* for Tesla).

3. Now he's going back to Tesla to be like "well, I own a lot of companies, and I can't really give Tesla my full attention while only owning 13% of it, so you'd better double my stake, for free, if you want me to keep doing good ideas at Tesla instead of at all my other companies."

Honestly it's a good threat! If you're Tesla's board, and you know that Elon Musk's top priority now is building AI, wouldn't you rather have him do it at Tesla than elsewhere? Presumably you want him paying attention to Tesla — that's why you've paid him billions of dollars to be Tesla's CEO! — so you'd be sad if he turned all of his attention elsewhere.

And yet there is something pretty obnoxious about it. He can keep doing this! What if you give him 25% of Tesla, he sells *that* stake for billions of dollars, he uses the billions of dollars to fund some new distracting hobby, and he comes back to you in a year saying "yeah, I don't know, my heart isn't really in Tesla anymore, maybe if you gave me another 25% it would motivate me." The \$55 billion pay package in 2018 — the one that the board is currently getting sued for — was supposed to motivate him to focus on Tesla, and it very clearly had the opposite effect! It gave him too much money, which he spent on distractions. And now he needs more money to turn back to Tesla from those distractions.

In general, with normal workers, the tension is that you want to pay them enough to motivate them, but not so much that they "call in rich" and stop working. With Elon Musk, who is on some days the richest man in the world, you might think this would not be a huge problem. You might think "well, whatever motivated him to work night and day to increase his wealth from tens of billions to hundreds of billions of dollars, it probably wasn't his *paycheck*, so we can rely on his intrinsic motivation to solve big problems and get glory for himself."

But that is wrong: Musk has plenty of intrinsic motivation, sure, but no particular reason to solve big problems *for Tesla*, as opposed to the many other companies that he has started or could start. It turns out that the problem of motivation is *much worse* for him. He's got too much going on, and too much money; his companies need to compete for his attention, and that competition is expensive.

GIP

When I was an investment banker, I sometimes had to fly to the middle of the country to pitch potential deals. On the one hand, this was good, this was the point, my whole goal as an investment banker was after all to get mandated on large lucrative deals, and the way to do that was to fly around meeting with important clients and impressing them. On the other hand, it was bad, because I did not like flying off to places, or meeting with important clients, or trying to impress them. I did not like, and was not good at, the travel and social elements of the job. So eventually I quit to become a blogger.

In this, I am very much like Adebayo Ogunlesi, except (1) he was a much better investment banker, (2) he did it for longer and (3) he quit to become a billionaire instead? The Financial Times reports:

In 2005, Ogunlesi, then a top banker at Credit Suisse, was summoned to Omaha, Nebraska, by the energy arm of Warren Buffett's Berkshire Hathaway to study a large takeover. It was the kind of call most financiers dream of, but Ogunlesi complained to his wife: "I really don't want to go."

In an interview with the Financial Times, he said his wife offered an ultimatum: "Either you decide you like your job and you want to keep doing it. Or, if you decide you don't, go find something else. But please don't think you can spend the next five years moaning."

I mean, completely fair, and basically why I left. But "after that 'kick in the behind,' Ogunlesi quit banking and at the age of 52, decided to try his hand as an investor," got into infrastructure, built Global Infrastructure Partners, and sold it last week to BlackRock Inc. for \$12.5 billion. I cannot believe that this involved *less* travel, or more glamorous travel. (He bought *airports*, which presumably involved flying around just to look at airports?) Also this is fun:

Though Ogunlesi will have his first boss in 18 years, he said [BlackRock CEO Larry] Fink, a friend since both worked at First Boston, has downplayed the potential for conflict: "Larry said to me: 'You will be on the board of directors, you will be my boss'. I think we have mutually assured destruction."

All the best friendships are premised on mutually assured destruction.

Grayscale

We talked last week about the long-awaited approval of spot Bitcoin exchange-traded funds in the US. It has been widely assumed that these ETFs would be good for the price of Bitcoin: Spot Bitcoin ETFs are a convenient and easy way for normal people (and traditional institutions) to own Bitcoin, and now that they are here, perhaps more people (and institutions) will buy Bitcoin through the ETFs. Demand for the ETFs will drive demand for Bitcoin, because each dollar that flows into the ETFs will ultimately, through arbitrage, go to buying Bitcoins.

But there is another, minimalist view you could take of the ETF approvals:

1. The biggest pot of publicly traded Bitcoins is the Grayscale Bitcoin Trust (GBTC), which we have also talked about a number of times.

2. GBTC's distinguishing feature, for most of its recent history, has been that you could put Bitcoins *in*, but you couldn't take them *out*. When we talked about it last week, there was about \$29 billion worth of Bitcoin in GBTC, and GBTC shareholders could not exchange their shares for Bitcoin.
3. GBTC led the charge for spot Bitcoin ETF approval, sued the SEC to get it done, won, applied to convert into an ETF, succeeded, and last week did in fact convert into an ETF.
4. Now you *can* take your Bitcoins out of GBTC. That is in a sense the *point* of the ETF structure. Now GBTC shareholders can sell their shares on the stock exchange, and if there are more sellers than buyers then arbitrageurs and "authorized participants" can deliver GBTC shares to Grayscale and get back Bitcoins.⁷
5. It is *possible* that the *main* effect of the launch of spot Bitcoin ETFs would be people taking money *out* of GBTC — which they have never been able to do before — rather than putting money *into* GBTC or the other ETFs.

That is, the launch of spot Bitcoin ETFs might be not a way to attract normal people into Bitcoin, but a way to let trapped GBTC investors out.

I'm not sure I'd bet on that as the main story or anything, but Bitcoin prices *did* fall since the ETFs launched, and GBTC *has* seen some redemptions,⁸ and it would be a very *funny* story. What if GBTC has just trapped some demand for Bitcoin since 2017, and ETF approval finally released it? Here's Bloomberg News with, I'm sorry, Anthony Scaramucci:

Bitcoin's decline since the start of trading of exchange-traded funds that hold the cryptocurrency was driven in part by sales of Grayscale Bitcoin Trust shares, according to SkyBridge Capital founder Anthony Scaramucci.

"There seems to be of lot of selling of Grayscale," Scaramucci said during a Bloomberg Television interview on Friday.

The hedge fund manager said that his trading desk noted that holders of the shares, which were converted from a trust this week when the US Securities and Exchange Commission signed off on the ETFs, were selling to book losses and shifting to lower fee alternatives.

"Shifting to lower-fee alternatives" should be neutral for Bitcoin — "Selling one Bitcoin product to buy another should not impact Bitcoin's price, said Zach Pandl, Grayscale's managing director or research" — but just getting out entirely would lower the price, and GBTC holders haven't been able to do that for years.

Things happen

Goldman Tops Estimates as Stock Trading Surges Past Expectations. Morgan Stanley Wealth Unit Beats Forecasts as Traders Fall Short. Morgan Stanley CEO Ted Pick Inherits a Bank That's Never Been More Boring. The Last Man Standing in Crypto. China Weighs More Stimulus With \$139 Billion of Special Bonds. Argentina, Turkey Lure Investors Seeking High-Yield Bond Returns. South Korea Alleges Naked Short Selling by Two More Global Banks. The Green Investor Calling Out Biden's Climate Law for Enriching Bankers and Consultants. Got \$60 Million? Goldman Sachs Wants to Lend You More. Evercore Grows Real Estate Arm as Clients Look to Private Credit. Large Backers of Private Equity Are Asking For Their Money Back. Bill Ackman Is Bringing Activist Playbook to America's Culture Wars. Bill Ackman escalates Business Insider plagiarism feud with legal threat. The M.B.A.s Who Can't Find Jobs. The \$65 Million Perk for CEOs: Personal Use of the Corporate Jet Has Soared. Trump-Tied SPAC Jumps After Former President's Decisive Iowa Win. Crash Parties, Escape Dull Chitchat and Make Powerful Friends: What Davos Elites Know. Bitcoin is a special-interest group. "They flew business class for the extra luggage allowances, and moved £1 million or more by checking-in three or four suitcases."

If you'd like to get Money Stuff in handy email form, right in your inbox, please subscribe at this link. Or you can subscribe to Money Stuff and other great Bloomberg newsletters here. Thanks!

To contact the author of this story:

Matt Levine at mlevine51@bloomberg.net

To contact the editor responsible for this story:

Wendy Pollack at wpollack@bloomberg.net

1. In this simple model you're selling all the stock at \$97, but realistically you are probably averaging down — selling some at \$100, some at \$99, some at \$98, etc., so that you actually sell for an average price of \$98.50 or whatever. Whereas once the block trade is announced, the price might jump down, and you'd have to resell all of it at a lower price. I am keeping things simple in the text but this is a potentially important advantage: Your bid is a discount to the last sale, but if you sell into the bid your average selling price could be quite a bit higher than the last sale.
2. It also lowers the absolute amount of risk: If all the banks would sell to the same hedge funds, then even if multiple banks do this trick, all that will happen is that the same hedge funds will get multiple calls about the same block, and they will just short the stock once.

3. In my simple model, your bid is the same with or without the trick. But the point of the trick is that you end up with better information in the auction than the other banks, so the other banks' bids are less competitive, so you win the auction with a fat safe profit margin. Without this trick, every bank would be bidding its best guess at the clearing price, and the most overconfident bank would win. If some bank thought "we can sell this down \$2 and only need \$0.25 of profit," they'd bid \$97.75 and win the auction; but if you pre-sell the stock down to \$97 they'll bid \$94.75 and lose to your bid of \$96.
4. "Blackstone, Oaktree Burned by Morgan Stanley's Block-Trade Leaks," reports Bloomberg News about the Morgan Stanley block-trade leaks, and presumably they're annoyed.
5. That is, 13.7% of the economic interests, though 61.1% of the voting rights.
6. This is not technically true but it is true in important senses. Like, he's the guy who ran the company when it raised a lot of the outside capital.
7. Technically they get back cash, and GBTC sells the Bitcoins to raise the cash, because the SEC did not approve spot Bitcoin ETFs with in-kind creation and redemption, as we discussed Thursday. But same effect.
8. Bloomberg data shows 692.4 million shares of GBTC outstanding on Wednesday, before the ETF approval, 690.1 million on Thursday and 677.7 million on Friday.

This copy is for your personal, non-commercial use only. Distribution and use of this material are governed by our Subscriber Agreement and by copyright law. For non-personal use or to order multiple copies, please contact Dow Jones Reprints at 1-800-843-0008 or visit www.djreprints.com.

<https://www.wsj.com/business/autos/elon-musk-seeks-greater-control-over-tesla-ahead-of-ai-advancements-f9139b12>

BUSINESS | AUTOS

Elon Musk Seeks Greater Control Over Tesla Ahead of AI Advancements

Billionaire says he would prefer to build AI products outside of the car company unless he gets greater control

By [Mauro Orru](#) [Follow](#) and [Rebecca Elliott](#) [Follow](#)

Updated Jan. 16, 2024 10:46 am ET



Elon Musk currently controls about 13% of Tesla. PHOTO: GONZALO FUENTES/REUTERS

Elon Musk said he feels uncomfortable making Tesla a leader in artificial intelligence and robotics without having about 25% voting control of the electric-car maker.

Musk said late Monday in a post on X that he wants enough control at Tesla TSLA **0.75%** ▲ to be influential, but not so much that he couldn't be overruled.

“Unless that is the case, I would prefer to build products outside of Tesla,” Musk wrote on the social-media platform.

The billionaire currently controls about 13% of Tesla, according to FactSet, having previously sold some of his holding in the company to fund his purchase of what was then called Twitter.

Tesla shares were up about 1% in morning trading Tuesday. The company didn't immediately respond to a request for comment.

Some investors have long been excited about Tesla's work and plans for deploying AI with driverless cars and humanoid robots.

Such initiatives have helped underpin Tesla's lofty market valuation and are a part of the company's longer-term growth strategy. Musk, in the posting, noted that Tesla isn't only one startup but a dozen. "Simply look at the delta between what Tesla does and GM," he wrote.



Elon Musk demonstrating a humanoid robot at a Tesla event. PHOTO: TESLA/AGENCE FRANCE-PRESSE/GETTY IMAGES

Tesla is the world's most valuable automaker, with a market valuation of nearly \$700 billion. GM is valued around \$48 billion.

In 2022, Musk showed off a new humanoid robot at a Tesla event, part of his efforts to shape public perception of the company as more than just an electric-vehicle maker.

The Tesla chief also revealed last summer the car company plans to spend more than \$1 billion through the end of 2024 on a supercomputer, dubbed Dojo, that is to help develop driverless-car technology.

Musk described Dojo as giving Tesla an advantage over rivals looking to train autonomous-car systems by employing enhanced computing power to get it done faster. Dojo was developed especially to handle the large amount of video generated by a driverless car.

Musk has also separately launched an AI company while calling the technology one of the biggest threats to humanity.

Musk, who serves as chief executive of Tesla, said in another post on X that he would be fine with a dual-class voting structure to gain greater control of the automaker but that he was told it was impossible after its initial public offering.

Companies with a dual-class structure carry two classes of shares with different voting rights, with one class typically offered to company founders and others for general shareholders.

Musk added that from his standpoint, his compensation—which has been subject to a court case—was about ensuring the right amount of voting influence at Tesla.

In the X posting, Musk said that “the Tesla board is great” and the reason he has no new compensation plan is because of the court case, which is being tried in a Delaware court and still awaiting a decision. His most recent compensation plan was approved by shareholders in 2018 and is worth around \$59 billion at recent share prices.

A Tesla shareholder is seeking to nullify that pay package, alleging Musk was too involved in determining his own pay and claiming the board failed to disclose crucial information to shareholders.

Tesla representatives have argued that Musk didn’t dictate the terms of the grant, which vested based on Tesla’s valuations and achievement of various milestones. Tesla cleared the last of those hurdles in 2022.

Write to Mauro Orru at mauro.orrु@wsj.com and Rebecca Elliott at rebecca.elliott@wsj.com

Musk wants 25% voting control at Tesla before fulfilling AI goal

 [reuters.com/technology/musk-seeks-25-voting-share-tesla-2024-01-16](https://www.reuters.com/technology/musk-seeks-25-voting-share-tesla-2024-01-16)

Chandni Shah, Hyunjoo Jin

Elon Musk, Chief Executive Officer of SpaceX and Tesla and owner of X, formerly known as Twitter, attends the Viva Technology conference dedicated to innovation and startups at the Porte de Versailles exhibition centre in Paris, France, June 16, 2023. REUTERS/Gonzalo Fuentes/File Photo Acquire Licensing Rights , opens new tab

Jan 16 (Reuters) - Tesla (TSLA.O) , opens new tab CEO Elon Musk said he would be uncomfortable growing the automaker to be a leader in artificial intelligence and robotics without having at least 25% voting control of the company, nearly double his current stake. loading

Musk said on Monday in a post on social media platform X, formerly known as Twitter, that unless he got stock in the world's most valuable automaker that was "enough to be influential, but not so much that I can't be overturned", at Tesla, he would prefer to build products outside of the electric-vehicle manufacturer.

He has long touted Tesla's partially automated "Full Self-Driving" software and its prototype humanoid robots but the electric-vehicle maker generates most of its revenue from its automotive business.

Some analysts have also pegged the technologies, including Tesla's Dojo supercomputer to train AI models, as drivers of the EV maker's valuation, with Morgan Stanley analyst Adam Jonas saying in September that Dojo could boost its market value by almost \$600 billion.

Tesla's shares fell about 2% in premarket trading on Tuesday, following Musk's comments.

Musk, the world's richest person, currently owns around 13% of Tesla stock after selling billions of dollars of shares in 2022 partly to help finance his \$44 billion purchase of Twitter.

In a separate post on X, he said he would be fine with a dual-class share structure to achieve his goal of getting 25% voting control, but was told it was impossible after Tesla's initial public offering.

"It's weird that a crazy multi-class share structure like Meta has, which gives the next 20+ generations of Zuckerbergs control, is fine pre-IPO, but even a reasonable dual-class is not allowed post-IPO," he said, referring to the Facebook parent's founder Mark Zuckerberg.

Companies with dual-class structures have two or more types of shares with different voting rights — usually one with greater voting rights for founders or early investors and another for other shareholders with less voting power.

Tesla did not immediately respond to a request for comment.

Musk currently faces a lawsuit over his compensation package. Tesla shareholder Richard Tornetta sued Musk and the board in 2018 and hopes to prove the co-founder used his dominance over Tesla's board to obtain an outsized compensation package that did not require him to work at the EV maker full-time.

Musk said on X there was no "feud" with the board over his new compensation package and said the pending verdict was holding back the discussions.

loading

loading

Reporting by Chandni Shah and Akash Sriram in Bengaluru and Hyunjoo Jin in San Francisco; Editing by Subhranshu Sahu, Jamie Freed and Shounak Dasgupta

Our Standards: The Thomson Reuters Trust Principles. [↗](#), opens new tab

- 
- 
- 
- 
- 

Acquire Licensing Rights



@annmlipton@esq.social

@AnnMLipton

...

I should add really interesting Q whether, if board grants comp for the purpose of handing Musk more control, a SH challenge would be direct or derivative, and what SHs should expect in exchange for giving up control.

See my paper, Three Faces of Control:

[papers.ssrn.com/sol3/papers.cfm...](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=458888)



Elon Musk

@elonmusk

Subscribe

...

I should note that the Tesla board is great. The reason for no new "compensation plan" is that we are still waiting for a decision in my Delaware compensation case. The trial for that was held in 2022, but a verdict has yet to be made.

I put "compensation plan" in quotes, because, from my standpoint, this is primarily about ensuring the right amount of voting influence at Tesla.

If I have 25%, it means I am influential, but can be overridden if twice as many shareholders vote against me vs for me.

At 15% or lower, the for/against ratio to override me makes a takeover by dubious interests too easy.

I would be fine with a dual class voting structure to achieve this, but am told it is impossible to achieve post-IPO in Delaware.

5:16 PM · Jan 15, 2024 · 1.3M Views



@annmlipton@esq.social @AnnMLipton · 20h

okay so I know it would be very easy for the board to do but has Tesla formally renounced any interest in business opportunities presented to its officers under DGCL 122? I.e., is Musk diverting opportunities from Tesla to his other entities?

renounced any interest in business opportunities presented to its officers under DGCL 122? I.e., is Musk diverting opportunities from Tesla to his other entities?



Elon Musk  
@elonmusk

Subscribe



I am uncomfortable growing Tesla to be a leader in AI & robotics without having ~25% voting control. Enough to be influential, but not so much that I can't be overturned.

Unless that is the case, I would prefer to build products outside of Tesla. You don't seem to understand that Tesla is not one startup, but a dozen. Simply look at the delta between what Tesla does and GM.

As for stock ownership itself being enough motivation, Fidelity and other own similar stakes to me. Why don't they show up for work?

2:55 PM · Jan 15, 2024 · 824.3K Views

7:13 AM · Jan 16, 2024 · 3,204 Views



2



3



24



1



Post your reply

Reply



KSAlberta @k_salberta@masto.ai @ksalberta.bsky.so @k_salberta · 3h ...

This also appears to be a violation of the SEC settlement, because Musk has been touting AI as a Tesla strength, and now he's tweeting about it, presumably w/o board approval. So it's turtles all the way down.



2



14



1.9K



KSAlberta @k_salberta@masto.ai @ksalberta.bsky.so @k_salberta · 3h ...

This is going to wind up in court some way under some form of shareholder lawsuit no matter what happens. I bet the Officers' & Directors' ins co lawyers are getting a bellyache right now.



3



38





@annmlipton@esq.social
@AnnMLipton

...

okay so I know it would be very easy for the board to do but has Tesla formally renounced any interest in business opportunities presented to its officers under DGCL 122? I.e., is Musk diverting opportunities from Tesla to his other entities?



Elon Musk
@elonmusk

Subscribe

...

I am uncomfortable growing Tesla to be a leader in AI & robotics without having ~25% voting control. Enough to be influential, but not so much that I can't be overturned.

Unless that is the case, I would prefer to build products outside of Tesla. You don't seem to understand that Tesla is not one startup, but a dozen. Simply look at the delta between what Tesla does and GM.

As for stock ownership itself being enough motivation, Fidelity and other own similar stakes to me. Why don't they show up for work?

2:55 PM · Jan 15, 2024 · 824.3K Views

3:13 PM · Jan 15, 2024 · 14K Views



6



17



58



6



Post your reply

Reply



@annmlipton@esq.social @AnnMLipton · 19h
also i assume the twitter sitter didn't review this?

...



2



10



2.8K



Anat Alon - Beck @anatalonbeck · 19h

...

I couldn't believe that his lawyers or @Tesla lawyers let him tweet this! Corporate opportunity doctrine exam hypo in the books!



1



1



13



501



@annmlipton@esq.social @AnnMLipton · 19h
Oh yeah - did the Twitter sitter review this?

...



1



1



5



689



Peter A. Roselle @PhenomenalPoto · 3h

...

I love that we're still cosplaying like the SEC isn't totally incompetent or (more likely) sitting in a room with bribe money up to their ears.



Peter A. Roselle @PhenomenalPoto · 3h

...

I love that we're still cosplaying like the SEC isn't totally incompetent or (more likely) sitting in a room with bribe money up to their ears.



1



44



Peter A. Roselle @PhenomenalPoto · 3h

...

Like honestly. You can tweet a fake buyout of your company now. You can threaten your shareholders with clear conflicts of interest to up your pay package. You can embezzle funds to start a company you own 100% of.

They should replace corp law classes with corp bribery classes.



33



DJ @DJNYCNY · 19h

...

Great job by the board giving him \$10bn in stock options without securing either a non-compete or even an understanding that this equity level would sufficiently motivate him to invest him time and talent at Tesla.



1



5

319



Jochen Kruse 🇺🇸 @Odenwaldjok · 20h

...

Tesla needs to raise capital, but Musk doesn't want to contribute, but keep his share percentage. Is that what he's talking about?



1



3

292



Don Linn @DonLinn · 18h

...

Oh. You mean the fiercely independent Tesla Board?



5

146



Jen Taub @jentaub · 19h

...

Thank you for flagging, as I'm teaching business organizations this semester, beginning Wednesday!



3

301



Musk's Many Billions and Tesla's Are Made of AI Dreams

B [bloomberglaw.com/bloombergterminalnews/bloomberg-terminal-news/S7D8QYDWLU68](https://www.bloomberglaw.com/bloombergterminalnews/bloomberg-terminal-news/S7D8QYDWLU68)

By Liam Denning

(Bloomberg Opinion) --



What's the next big thing? Elon Musk at the launch of Tesla's Cybertruck.

Photographer: Frederic J. Brown/AFP via Getty Images

There are any number of ways to read Elon Musk's tweet about why he should have 25% control of Tesla Inc.:



Photographer: Denning, Liam

To me, it renders as: “Nice wannabe AI company you’ve got there. Be a shame if it turned out to just be a carmaker.”

Why is Musk suddenly tweeting gossamer-veiled threats to take his genius elsewhere? Possible explanations run the gamut. At a basic level, he dumped a lot of Tesla stock during 2022 when he was buying Twitter Inc. and it is generally agreed that this is not an investment that has performed well. Any investor who self-ignites tens of billions of dollars, and does so very publicly, would probably like a do-over of some sort. It is notable that he calls out Fidelity — absurdly, but still — which recently made headlines for marking its X stake down (again) to a fraction of what Musk paid.

Meanwhile, Musk is also, along with Tesla, awaiting judgment in a lawsuit claiming shareholders were misled about a compensation package that he was awarded in 2018 worth more than \$50 billion. A recent, lengthy article in the Wall Street Journal reporting concerns among Tesla’s board about Musk’s alleged drug-taking may also have prompted a fit of pique.

In any case, Musk’s tweet usefully, and amusingly, reminds the world about one important thing. Tesla is, in tangible terms, a successful maker of EVs facing a slowing, and more competitive market. In valuation terms, however, it is a dream conceived in Musk’s head that has been internalized by the capital markets.

Tesla is, overwhelmingly, a maker of electric vehicles, combining high growth with high margins — until recently anyway. Deliveries increased by 38% in 2023 — below the company's long-term target of 50% per year — and the consensus for 2024 implies just 21%. Trailing 12-month net profit as of the third-quarter was actually down, year over year.

Yet in the most starry-eyed Wall Street financial models, the making and selling of vehicles — generating 92% of Tesla's current gross profit ¹ — accounts for only a fraction of Tesla's purported valuation. The rest relates to whatever Tesla's next big thing might turn out to be, usually something related to artificial intelligence, be it robotaxis, licensed self-driving systems, the Optimus humanoid robot or just something else that might spring from the company's Dojo supercomputing project.

Amorphous as the narrative may be, remove it and the tenuous tether between Tesla's valuation and something approximating a potential future reality evaporates entirely.

So Musk's apparent discomfort with forging ahead on AI at Tesla without owning a stake virtually two times as big as his current one seems like a real threat. Except, of course, that Tesla stock and options currently account for more than 70% of Musk's own net worth, according to the Bloomberg Billionaires Index (where he tops the list). Should he get so "uncomfortable" as to actually start dallying elsewhere, the financial foundation that allows him to, say, buy a social media site for tens of billions and then take a flame-thrower to it would also suffer enormously.

The very idea that he needs a formal 25% blocking stake is highly dubious for the same reason. Tesla is worth what it is because of belief in Musk. Even if someone else could afford to buy a sizeable enough stake with a view to launch an activist campaign or taking over the company, without Musk's full agreement, they may as well incinerate their own cash.

Musk's power doesn't derive from this or that percentage of shares outstanding. Exhibit A for this: The fact that he can toss off an apparent threat to his own company, trashing the very idea of a fiduciary duty of loyalty, and not immediately draw a public rebuke from Tesla's chronically supine board and a sell-off in the stock. The best counterargument against his absurd demand is that he feels empowered enough to make it.

More From Bloomberg Opinion:

- Matt Levine's Money Stuff: Elon Musk Isn't Getting Enough Sleep
- Two Odes to Musk's Genius Need a Grain of Salt: Liam Denning
- Let's Resolve to Ditch the \$100,000 EV in 2024: Liam Denning

Want more Bloomberg Opinion? OPIN . Or you can subscribe to our daily newsletter.

To contact the author of this story:

Liam Denning at ldemming1@bloomberg.net

Boeing Co

'It ain't working': Boeing's quality pledges in question after Max 9 incident

US group's efforts to strengthen engineering processes are coming under scrutiny after mid-air door plug blowout

Sylvia Pfeifer in London and Claire Bushey in Chicago JANUARY 14 2024



In October last year, Boeing chief executive Dave Calhoun said the US plane maker was focusing on improving the quality of its aircraft. The company, he told analysts, had in recent years “added rigour” to its “quality processes”.

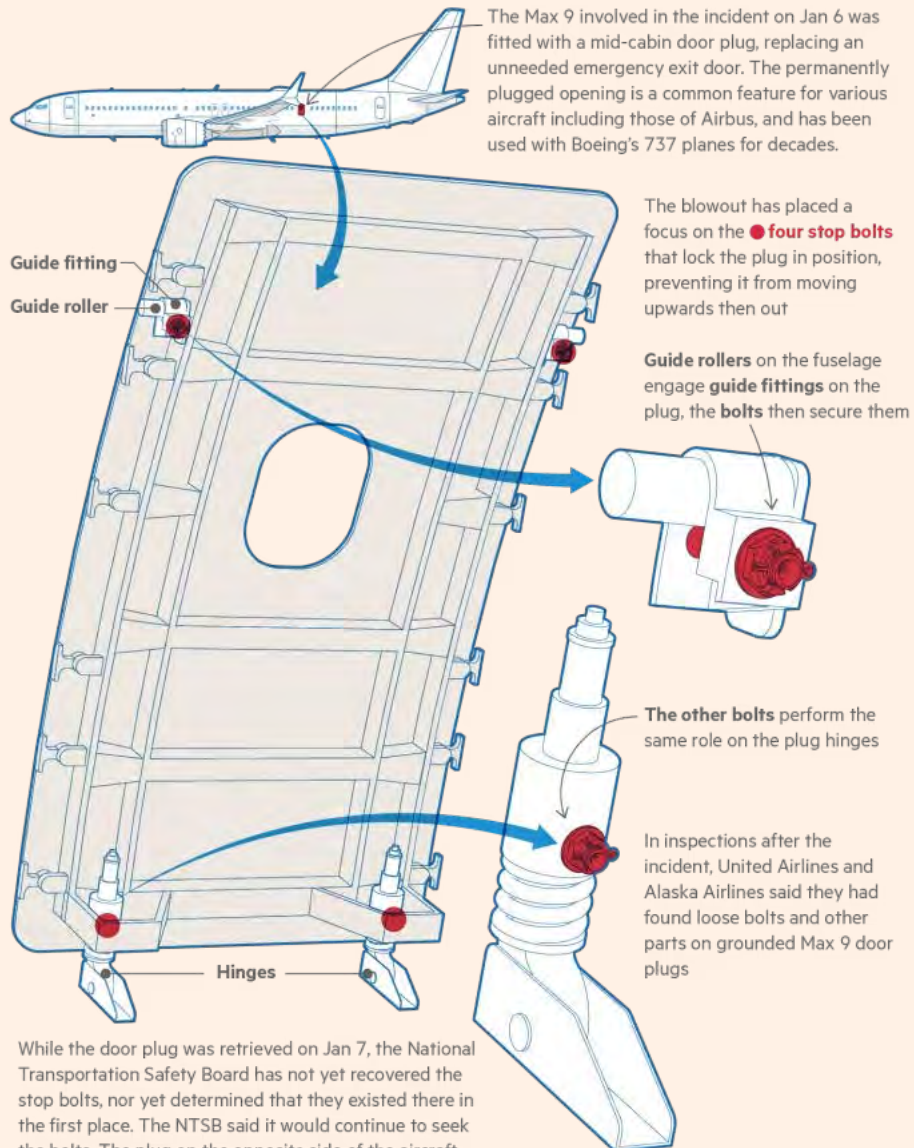
“We’ve worked hard to instil a culture of speaking up and transparently bringing forward any issue, no matter the size, so that we can get things right for a bright future. As a result, we’re finding items that we need to resolve,” he added.

Those comments will now haunt Calhoun as he confronts the latest blow to Boeing’s reputation: the likelihood that a manufacturing error or lack of quality control led to a dangerous blowout of a section of the fuselage of an Alaska Airlines flight just over a week ago.

Calhoun, who has promised the company will be completely transparent in helping investigators, will know too well that his own credibility and that of his executive team are also on the line.

The US Federal Aviation Administration, which had grounded some of the planemaker’s 737 Max 9 aircraft pending inspection, has opened a [formal probe](#) into the incident. The regulator on Friday said it would reassess the current system where some aircraft inspections were delegated to Boeing employees, as well as conducting an audit of the Max 9 production line. Later, the FAA said that the 737 Max 9 would stay grounded until Boeing provided additional data.

What is a mid-cabin door plug?



While the door plug was retrieved on Jan 7, the National Transportation Safety Board has not yet recovered the stop bolts, nor yet determined that they existed there in the first place. The NTSB said it would continue to seek the bolts. The plug on the opposite side of the aircraft remained intact with no discrepancies found by the NTSB

Sources: NTSB; FT research
© FT

"They may have changed the way they're doing things, but it ain't working," said Captain Dennis Tajer, spokesperson for the pilots union for American Airlines. "It doesn't matter what system you put in place. We're measuring it on the outcome."

When Calhoun took the helm in January 2020 after two crashes of the 737 Max 8 aircraft that killed 346 passengers and crew, Boeing was still reeling from the greatest crisis in its history. The former GE executive had been a Boeing board member since 2009. He promised to rebuild trust with regulators, airlines and the flying public, and to bring in greater transparency. Boeing's engineering and safety processes would be strengthened.

There has been progress. The company created a board-level aerospace safety committee and centralised its safety reporting functions.

Top engineers among business units who previously reported to executives leading those divisions began reporting to the company's chief engineer, who reported directly to the chief executive. Boeing created a product and services safety group, also reporting to the chief engineer.

Last year Boeing [appointed](#) Howard McKenzie as chief engineer to succeed Greg Hyslop, who retired, taking the role of adviser to the chief executive.

In January 2021 it named Mike Delaney, a vice-president overseeing the digital transformation of Boeing's production lines, to the newly created role of chief safety officer.

"Mike and his team are the only people in our company that can give the go-ahead to move aeroplanes back into the air," Calhoun said at an employee meeting at its 737 factory in Renton, Washington, last Tuesday.

Yet production mis-steps have continued, and while not all manufacturing errors affect safety, they suggest a disconnect between top-level initiatives and the reality on the shop floor. Boeing discovered in April last year that Spirit AeroSystems, one of its biggest suppliers, had improperly installed two fittings on the vertical stabiliser on the 737, forcing the jet maker to delay deliveries. Four months later a new problem arose: incorrectly drilled holes in the rear pressure bulkhead of some fuselages.

The two cases last year and the Alaska incident all have [Spirit](#) in common — the Wichita, Kansas-based company builds the Max fuselages, including the door plug that fell off the plane.



Boeing CEO Dave Calhoun addresses staff at a company-wide safety meeting at a factory in Renton, Washington. © Boeing

But there haven't been other manufacturing problems in recent years. Deliveries of the 787 Dreamliner were stopped for 20 months because of multiple glitches, including the installation of poorly fitted shims — thin pieces of material used to improve fit between joints in the fuselage — and aircraft that did not meet engineering specifications for skin flatness. The company has even struggled with its prestige project, the jet that carries the US president, Air Force One.

Boeing has made "improvements since the original Max problems in 2018", said John Cox, a retired pilot and chief executive of consultancy Safety Operating Systems. "Have they made sufficient improvements? The Alaska incident would suggest not," he added.

The blowout and subsequent discovery by Alaska and United Airlines of loose bolts on roughly 15 grounded Max 9 aircraft raise a number of questions about the assembly process at Boeing's Renton facility, said Cox.

"Is it unclear, is it overly complex, is it done between two shifts where one thinks it's been done by the other one? Or is the safety inspection not adequate to correct what has now been identified to be a recurring problem?"

David Soucie, a former safety inspector at the FAA, criticised Boeing for a design error, a more serious lapse. He noted that in a photo published in trade publication *The Air Current*, the door plug bolts were not secured with safety wire, which he said was necessary for any use where a loose bolt could lead to unsafe conditions. Safety wire threaded through a hole on the bolt counteracts the everyday vibrations that cause bolts to loosen.

Boeing has improved its safety protocols since the Max crashes, Soucie said. He noted that when he visited one of the factories in Washington in December 2019, assembly workers never rotated away from their stations. This gave workers a siloed view of the product, making it harder for them to identify mistakes made by others. Since then, Boeing has started using rotations.

The company has added an ombudsman for employees authorised to work on behalf of the FAA — a move required by a lawsuit settlement — and added real-time data and analytics software into its safety management system.

Boeing stock falls after mid-air blowout

Intraday share price (\$)

FINANCIAL TIMES

Source: Refinitiv

“Boeing has a very strong risk management programme now,” Soucie said. “It was fairly strong many years ago, and then it got weak, and now it’s getting strong again.”

Company insiders said the discovery last year of instances of the wrongly drilled holes and loose rudder bolts was evidence that the system was working. “The expectation is that you will find stuff and by finding stuff the system is working because you are working to address them,” said one.

Several industry experts said well-documented labour shortages in the aerospace industry may have contributed to the quality lapses. Boeing in particular, they said, suffered from a shortage of skilled workers stemming from the halt of Max production after the 2019 grounding, followed by the onset of Covid-19.

Robert Spingarn, an analyst at Melius Research, said that manufacturing errors had risen throughout the industry because Covid changed the composition of the workforce, with older workers departing through retirements or lay-offs.

“We have a much less experienced workforce at all these companies and throughout the supply chain, and that has been on the factory floor more than elsewhere,” he said.

Boeing [laid off](#) thousands of workers during Covid, including final assembly workers, said Scott Hamilton of aviation consultancy Leeham News. When the company was looking to rehire people, many failed to return, increasing the share of inexperienced workers.

"It takes a period of time for people to understand the learning curve to become efficient and proficient in building aeroplanes," said Hamilton. "You can probably point to a lot of this quality control issue to the new hires and learning curves. Spirit had the same problems."

Several long-term Boeing watchers believe the company is still suffering from the consequences of the much-criticised "Partnering for Success" initiative. Former chief executive Jim McNerney, who led the company from 2005 to 2015, launched it to squeeze costs out of suppliers.

Boeing pointed to recent moves to improve oversight and safety processes. It said it had grown its workforce since the pandemic, adding about 15,000 staff to reach 156,000 by the end of 2022, driven by significant hiring in engineering and manufacturing.

The Alaska incident has refocused attention on the FAA's role in overseeing Boeing, which was scrutinised during the Max 8 crisis.

Washington Senator Maria Cantwell sent a letter to the head of the FAA on Thursday saying "recent accidents and incidents — including the expelled door plug on Alaska Airlines flight 1282 — call into question Boeing's quality control. In short, it appears that FAA's oversight processes have not been effective in ensuring that Boeing produces aeroplanes that are in condition for safe operation."

Some long-term Boeing watchers worry that the company's engineering-driven culture has still not fully recovered from a merger completed in 1997 with aerospace company McDonnell Douglas and the relocation of the company's headquarters four years later from Seattle to Chicago. For some, the move away from the company's longtime home marked a shift in priorities from engineering to financial performance.

Before the merger, Boeing was "very much a product-focused company based in Seattle with a lot of control over everything they did", said Nick Cunningham, analyst at Agency Partners in London. Boeing launched its first big share buyback in 1998. It bought back \$41bn worth of shares between 2013 and 2019, including more than \$9bn a year in 2017 and 2018, contributing to its high debt levels.

Yet others dismiss suggestions that Boeing's culture is at fault. "Clearly something has gone wrong with this incident. I do not think the culture around individual people feeling responsible for what they are doing has changed," said one former industry executive.

Given the long lead times in the aerospace industry, the results of real corporate change will take time to manifest themselves.

"You can only judge by results," Cunningham said. "It takes a long time for things that go wrong to play out, and if you fix those things it takes a long time."

Taking stock of Boeing's past



© Mario Tama/Getty Images

Boeing has encountered engineering and manufacturing problems in recent years ranging from small production errors to the catastrophic crashes of the 737 Max 8. Some company observers say the root of its difficulties can be traced back three decades

1997

Boeing merges with McDonnell Douglas. Critics say McDonnell Douglas's culture — focused on financial performance — came to dominate over the ensuing years at the expense of Boeing's engineering-driven culture

2001

Boeing shifts its headquarters to Chicago from its longtime home in Seattle, site of its oldest commercial aircraft factories

2005

Boeing divests Spirit, shifting fixed costs of its manufacturing facilities and labour

OCT 2018

Lion Air flight JT610, operated on a Max 8, crashes off the coast of Indonesia



© Reuters

MAR 2019

Ethiopian Airlines flight 302, operated on a Max 8, crashes shortly after take-off. US regulators ground the Max three days later

DEC 2019

Chief executive Dennis Muilenburg is fired. Dave Calhoun, former GE executive and board member at Boeing since 2009, takes over the following month

2020

Boeing says it will cut 10 per cent of its workforce as Covid hits the US.



© Ellen M. Banner/The Seattle Times/AP

2021

Boeing pays \$2.5bn to resolve criminal charges connected to the Max crashes

2022

Boeing announces another move of its headquarters, this time to Arlington, Virginia. The relocation places the company's leadership close to government officials and lawmakers in the US capital. Arlington is also the home of the Pentagon, a leading customer

JAN 2024

A door plug blows out of Alaska Airlines 1282, a Max 9 aircraft. US Federal Aviation Authority orders audit of Max 9 production line. It will assess safety risks around delegation of inspections to Boeing employees. The FAA says the aircraft will stay grounded until Boeing provides further data



© NTSB/Getty Images

[Copyright](#) The Financial Times Limited 2024. All rights reserved.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Law360 Pulse Spotlight On Mid-Law Work

By **Emma Cueto**

Law360 (January 12, 2024, 4:08 PM EST) -- Kessler Topaz beating out two firms to become lead counsel in a proposed class action against Wells Fargo and Fredrikson & Byron's lobbying arm's new relationship with a cooperative business interest group lead this edition of Law360 Pulse's Spotlight On Mid-Law Work, recapping the top matters for Mid-Law firms from Jan. 1 to 12.

Taking the Lead Counsel Spot to the Bank

Kessler Topaz Meltzer & Check LLP was appointed as lead counsel for a proposed class of Wells Fargo inventors alleging that executives harmed the company by failing to comply with regulatory consent orders. U.S. District Judge Jon S. Tigar named the firm's client, the City of Hollywood Firefighters' Pension System, as lead plaintiff in the consolidated action, rejecting proposals from Robbins Geller Rudman & Dowd LLP and Lieff Cabraser Heimann & Bernstein LLP, who were also vying for the top spot.

The suit seeks unspecified damages on behalf of the company against nine board members, including CEO Charles Scharf, over what one shareholder claims is a pattern of illegal and fraudulent conduct dating back to at least 2002, including conduct that led to a \$3.7 billion fine by the Consumer Financial Protection Bureau.

A Cooperative Collaboration

The government relations arm of Midwest firm Fredrikson & Byron PA announced Jan. 11 that it would be assisting the Cooperative Network, an association dedicated to advancing the interests of cooperative businesses, during the 2024 Minnesota legislative session. The relationship will include preparing leaders for bill hearings, securing bill authors, legislative tracking, and other assistance on the group's policy priorities.

Cooperative Network said in an announcement that it was pleased with the firm's multi-sector experience and its ability to work on both sides of the political aisle.

Taking McMahon to the Mat

Robbins Geller Rudman & Dowd LLP and Prickett Jones & Elliott PA became the latest firms to enter the arena against World Wrestling Entertainment founder Vincent McMahon and top company officials and directors over WWE's allegedly rushed dive into a merger that created TKO Group Holdings Inc. Two other similar suits were filed last year, with shareholders seeking damages from McMahon for rushing into the TKO merger for less than full or fair value for the WWE and its stockholders.

Paltry Pandemic Payments

New Mexico healthcare system Presbyterian Healthcare Services, tapped Arnall Golden Gregory LLP and Madison Mroz Steinman Kenny & Olexy PA for a suit accusing the U.S. Department of Health and Human Services of violating federal law by shortchanging the system almost \$10.6 million in pandemic relief funds. In a Jan. 10 complaint, it alleged that federal officials initially encouraged the nonprofit system to seek reconsideration after the agency provided a lower-than-expected disbursement but later rejected the application without a good explanation.

Kickoff on a New Sports Venture

Financial services advisory company Consuello Group relied on Pryor Cashman LLP in launching its new sports-focused platform Consuello Strive, which seeks to support those investing in sports and entertainment businesses, according to a Jan. 10 announcement. Founding partners of the new venture include Super Bowl champion Tom Brady, tennis legend Serena Williams, and NBA Hall of Famer Paul Gasol.

Working at the Car Wash (Sale)

Michigan firm Varnum LLP began the new year by announcing on Jan. 11 that it had acted as counsel to Michigan Wash Co. LLC, which was created by private equity firm Ammori Equity Partners, in the acquisition of 19 Zax Auto Wash stores around southeast Michigan.

---Additional reporting by Dan McKay, Jeff Montgomery, Katryna Perera, Bonnie Eslinger, Jon Hill, Hailey Konnath, Lauren Berg and Jessica Corso.

All Content © 2003-2024, Portfolio Media, Inc.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

AT&T Brass Hit With Shareholder Suit Over Lead Cables

By **Sydney Price**

Law360 (January 12, 2024, 5:40 PM EST) -- An AT&T shareholder has alleged in a derivative suit that the company's executives and directors knew the network's lead cables were associated with serious health and environmental risks, adding another suit to the growing list of securities actions and federal investigations telecom providers face over their alleged use of highly toxic equipment.

George Miller filed the complaint Thursday in Delaware federal court on behalf of nominal defendant AT&T. The suit's individual defendants include several current and former executives and directors, including CEO John T. Stankey, Chief Financial Officer Pascal Desroches, former CEO Randall L. Stephenson and former CFO John Stephens.

The defendants breached their fiduciary duties by making false and misleading statements about the company during the relevant period, and by allowing the company to overpay for its own shares by more than \$1.7 billion, the suit states.

During the suit's relevant period, which runs from March 1, 2020, until July 27, 2023, AT&T assured investors through its website and U.S. Securities and Exchange Commission filings that it was in compliance with environmental, health and safety regulations and dedicated to protecting its employees and served communities, according to the complaint.

However, beginning in the summer of 2023, articles published by The Wall Street Journal revealed that these statements were false and misleading and that AT&T still owned "sprawling" networks of lead cables, the suit alleges. The articles contained historical background about the company's lead cable usage and testimonies from former AT&T employees, according to the suit.

A July 9 article from The Wall Street Journal revealed groundwater may be contaminated by 2,000 lead-covered cables, including some used by AT&T, the suit said. The article also alleged AT&T knew of the health risks associated with the cables, including heart disease, anemia and infertility. A subsequent Wall Street Journal article said that cables acquired by AT&T were leaching into the soil and groundwater of Louisiana's Bayou Teche, making the water unsafe for drinking under U.S. Environmental Protection Agency guidelines.

Following the articles, the price of AT&T shares fell 34 cents, or about 2%, from a closing price of \$15.61 on July 7, to close at \$15.27 on July 10, the suit says.

A couple of days later, The Wall Street Journal published an article that said AT&T and other telecommunications companies have known about the risks associated with their lead cables "for decades." On July 14, The Wall Street Journal published another article with quotes from AT&T employees alleging the company did not properly equip them to work with the toxic cables, according to the complaint.

AT&T's shares subsequently fell 62 cents each, or about 4%, from a closing price of \$15.12 per share on July 13, to close at \$14.50 on July 14, the suit says.

On July 17, both The Wall Street Journal and investing.com published articles alleging that analysts were concerned about the information recently uncovered regarding the lead cables, according to the complaint. On this news, AT&T shares fell 97 cents each, or nearly 7%, from a closing price of \$14.50 on July 14, to close at \$13.53 on July 17, according to the complaint.

The full truth was revealed, the suit claims, when The Wall Street Journal reported on July 26 that the EPA and the U.S. Department of Justice had launched investigations into AT&T and other telecommunications companies to find out how much they knew about the potential risks of the cables. On this news, AT&T shares fell 38 cents each, or about 3%, from a closing price of \$14.89 on July 26, to close at \$14.51 on July 27.

The EPA has performed its own tests at some of the sites identified by The Wall Street Journal's reporting, including in Louisiana, New Jersey and Pennsylvania. The EPA says its tests have shown that there are no immediate threats to people nearby that would warrant action by the agency.

In December, the EPA sent letters to AT&T and Verizon requesting meetings with executives to discuss "technical issues" related to the issue of lead-covered telecommunications cables.

"From the beginning, our member companies have worked collaboratively with the EPA," Marie Johnson, spokesperson for telecom industry group USTelecom, said in a statement Friday. "The companies requested to meet with the agency to discuss the technical results when they submitted them last year. There is still a desire to do so. The bottom line is that the test results continue to show telecom lead-sheathed cables pose no significant public health risk."

"Our member companies have already met with the EPA in-person and remotely on several occasions on this issue going back to the fall," Johnson added.

In a **separate shareholder action** filed in New Jersey in July, investors allege AT&T and some of its executives failed to disclose the dangers they knew the lead equipment posed.

Verizon, Lumen Technologies Inc. and others were also recently hit with proposed class actions by investors who allege the companies failed to disclose potential liabilities related to lead-wrapped cables.

A spokesperson for AT&T on Friday declined to comment on the derivative suit. Counsel for Miller did not immediately respond to requests for comment on Friday.

Miller is represented by Timothy Brown of The Brown Law Firm PC and Brian E. Farnan and Michael J. Farnan of Farnan LLP.

Counsel information for the AT&T defendants was not immediately available on Friday.

The case is Miller v. Stephenson et al., case number 1:24-cv-00032, in the U.S. District Court for the District of Delaware.

--Additional reporting by Juan-Carlos Rodriguez and Katherine Smith. Editing by Jay Jackson Jr.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Securities Class Actions Show No Signs of Slowing In 2024

By **Susan Saltzstein, Tansy Woan and William O'Brien** (January 12, 2024, 5:22 PM EST)

Plaintiffs asserted securities class actions at elevated levels in 2023 — a sign that filings will remain high in the year ahead. Based on data from Cornerstone Research through Sept. 30, 2023, plaintiffs were on pace to file approximately 216 federal and state securities class actions last year — a slight increase over the 208 suits brought in 2022 and roughly on par with the 218 suits brought in 2021.

While filing levels remained consistent from 2021 to 2023, their composition changed. Through Sept. 30, 2023, for instance, special-purpose acquisition company-related suits had fallen 37% as compared to the same period in 2022. This decline may be attributable to a significant decrease in SPAC initial public offerings and de-SPAC transactions since their peak in 2021.

Plaintiffs instead are targeting companies that allegedly have failed to anticipate supply chain disruptions, persistent inflation, rising interest rates and other macroeconomic headwinds.

For instance, in 2023, plaintiffs filed at least seven class actions against financial institutions, accusing them of downplaying liquidity and other concerns stemming from rising interest rates. Amid this ongoing period of economic uncertainty, we expect such filings to persist.

The Supreme Court will continue to shape securities law jurisprudence.

Next year, the U.S. Supreme Court is poised to decide at least two securities lawsuits that could change the landscape in both the private and regulatory arenas.

On Jan. 16, the Supreme Court will hear argument in *Macquarie Infrastructure Corp. v. Moab Partners LP*,[1] a closely followed case that ought to address whether a purported failure to make a disclosure required under Item 303 of U.S. Securities and Exchange Regulation S-K[2] can support a securities fraud claim under Section 10(b) of the Securities Exchange Act, even absent an otherwise misleading statement.[3]

The plaintiffs alleged that Macquarie had issued material misstatements and omissions concerning the potential impact of new international fuel regulations on the company's fuel storage business, in violation of both the Securities Act and the Exchange Act.

In support of their claims under Rule 10b-5, the plaintiffs alleged that, under Item 303, Macquarie had a duty to disclose that the company's most profitable subsidiary stood to lose a significant amount of its fuel storage business as a result of impending regulations, known as IMO 2020.

The U.S. District Court for the Southern District of New York granted Macquarie's motion to dismiss, holding that the plaintiffs had failed to plead an actionable misstatement or omission, a violation of Item 303, and scienter.



Susan Saltzstein



Tansy Woan



William J. O'Brien

In an unpublished summary order, the U.S. Court of Appeals for the Second Circuit reversed in part, holding that the plaintiffs pled adequately that Macquarie made affirmative misstatements in the form of "half-truths" that required disclosure, and that Macquarie violated Item 303.

As to the latter, the panel ruled that failing to make a material disclosure required by Item 303 can serve as a predicate for a Section 10(b) claim, so long as the claim's other elements are well pled.

In the present appeal, the Supreme Court is poised to resolve a circuit split concerning whether an Item 303 violation can serve as a basis for Section 10(b) liability.

The U.S. Court of Appeals for the Ninth Circuit, contrary to the Second Circuit, has held that "Item 303 does not create a duty to disclose for purposes of Section 10(b) and Rule 10b-5." [4] The U.S. Court of Appeals for the Third Circuit and the U.S. Court of Appeals for the Eleventh Circuit have also weighed in and held that an Item 303 violation does not give rise automatically to Section 10(b) liability. [5]

Should the Supreme Court endorse the Second Circuit's framework, shareholders might explore other avenues for asserting 10b-5 claims, citing other SEC disclosure obligations.

We also await the Supreme Court's decision in SEC v. Jarkesy. While not a class action, the court has been asked to determine, among other things, whether the SEC's existing statutory and regulatory authority to initiate and adjudicate administrative enforcement proceedings seeking civil penalties violates the Seventh Amendment and the nondelegation doctrine.

The nondelegation claim would likely have consequences for other SEC rulemaking. At oral argument, however, the justices focused on the Seventh Amendment claim.

If the court rules in Jarkesy's favor on his Seventh Amendment claim, the SEC may be required to bring certain civil penalty actions for securities violations in federal court.

The ramifications of this decision could be significant, as the SEC often uses its in-house courts to seek monetary penalties, and studies reveal that the SEC wins cases it brings in its in-house courts at a much higher rate than those it tries in federal court. [6]

We also should expect plaintiffs to attempt to maneuver in light of the Supreme Court's decision in Slack Technologies LLC v. Pirani. [7]

Decided last term, the court in Slack unanimously rejected the Ninth Circuit's holding that under Section 11 of the Securities Act, plaintiffs may recover even when shares owned are not traceable to a defective registration statement. [8] Or as Pirani argued, when the shares "bear some sort of minimal relationship" to a defective registration statement. [9]

Instead, a plaintiff must plead and prove that the securities held are traceable to the particular registration statement alleged to be false or misleading. [10]

Courts will continue to assess short-seller reports underlying securities complaints.

As 2023 confirmed, short-seller reports are increasingly being used by the plaintiffs bar to form the basis of securities complaints. [11] It is estimated that short-seller reports have underpinned at least 75 securities class actions filed against public companies in roughly the last three years.

Given the recent proliferation of these suits, a body of law has developed around the extent to which allegations derived from such reports should be credited on a motion to dismiss.

The better-reasoned opinions discount allegations where they lack independent corroboration or verification citing a short-seller's motivation to drive down the target's stock price. Accordingly, these courts equate short-sellers to confidential witnesses and apply the Private Securities Litigation Reform Act's heightened pleading standard. [12]

In January 2023, in *In re: DraftKings Inc.*, for example, the Southern District of New York analyzed

the credibility of a short-seller report and concluded that the plaintiffs' reliance on the allegations in the report — which were largely unsourced or anonymously sourced — was "a global deficiency" spanning the complaint that mandated dismissal.[13]

Similarly, in *Hershewe v. Jooy Inc.* last year, the Ninth Circuit discredited a short-seller report because it lacked "indicia of reliability" and "failed to substantiate [plaintiffs] allegations of falsity." [14]

Separately, courts have also held that shareholders cannot rely on short-seller reports as corrective disclosures if they are based on public information because a corrective disclosure "must by definition reveal new information to the market that has not yet been incorporated into the price." [15]

We note that some courts have credited short-seller reports under particular circumstances at the pleading stage.[16] This line of cases often cites older decisions, which rejected the premise that short-sellers are the functional equivalent of confidential witnesses and must be evaluated under the PSLRA's pleading standard for confidential sources.

According to these older decisions, short-seller reports do "not implicate the same skepticism as a 'traditional' anonymous source." [17]

Defendants have introduced a roadmap for challenging price impact at class certification.

In 2023, the Second Circuit was called upon — yet again — to adjudicate the plaintiffs' multiyear quest for class certification in *Arkansas Teacher Retirement System v. Goldman Sachs Group Inc.*

This time, the Second Circuit reversed the trial court and denied class certification.[18] In so holding, the court determined that the defendants had rebutted the basic presumption of reliance because there was an "insufficient link between the alleged misrepresentations and corrective disclosures" in the Section 10(b) claim.[19]

While the alleged misstatements were generic — for example, "integrity and honesty are at the heart of our business"[20] — the corrective disclosures were specific, such as an SEC enforcement action against the defendant company for purportedly failing to disclose a conflict of interest.[21]

The Second Circuit determined that the Southern District of New York had failed to apply the Supreme Court's guidance — that when there is a gap in generality between the front- and back-end disclosures, the Vivendi back-end-front-end price inflation inference starts to "break down." [22]

Rather than ask what would have happened if the company had spoken truthfully, at an "equally generic level," the district court allowed the "details and severity ... of the corrective disclosure to do the work of proving front-end price impact." [23]

This violated Supreme Court precedent because "utilizing a back-end price drop as a proxy for [a] front end misrepresentation's price impact works only if, at the front end, the misrepresentation is propping up the price." [24] Thus, the proper inquiry is "whether the disclosure as written is specific enough to evoke investor reliance." [25]

We will be watching to see if the business community can replicate elsewhere the defendants' hard-earned victory in *Arkansas Teacher*. [26] At minimum, the plaintiffs cannot demonstrate price impact merely by showing a subject-matter match between a front-end misstatement and back-end corrective statements where, as in *Arkansas Teacher*, there was a significant mismatch in specificity. [27]

"Materialization of Risk" Will Remain in Focus After the Ninth Circuit's Decisions in Facebook and Glazer Capital Management

We anticipate plaintiffs will continue to press securities fraud claims under a materialization of risk theory — in which plaintiffs allege that defendants have framed a risk in purely hypothetical terms when in fact it has already occurred.

Two recent Ninth Circuit decisions have brought this topic into sharper view. In *In re: Facebook Inc.*

Securities Litigation, the Ninth Circuit, in a split decision, revived Exchange Act and Rule 10b-5 claims, holding that because "Facebook was aware of Cambridge Analytica's misconduct [before it filed its 10-K], ... Facebook's statements about risk management 'directly contradict[ed]' what the company knew when it filed its [10-K]."[28]

The Ninth Circuit credited the plaintiffs' allegation that Facebook's 10-K had described a particular risk — specifically, third-party misuse of Facebook users' personal data — as one that could harm the company if it materialized, when in fact the alleged misuse had already transpired. Accordingly, the Ninth Circuit concluded that the district court had "overlook[ed] the reality of what Facebook knew." [29]

Earlier in 2023, the Ninth Circuit addressed a similar issue in *Glazer Capital Management LP v. Forescout Technologies*. [30] In *Glazer*, the plaintiffs alleged that Forescout had made materially false or misleading statements relating to the likelihood of its merger closing, in violation of the Exchange Act and Rule 10b-5. [31]

In particular, they claimed that Forescout was in possession of information that its counterparty was considering not closing the merger, yet stated it "look[ed] forward to completing our pending transaction." [32]

Although Forescout provided risk disclosures about the transaction, "including that the timing of the closing was uncertain and closing conditions might impact the deal's course," the Ninth Circuit reversed the district court's dismissal, holding that a company "cannot rely on boilerplate language describing hypothetical risks to avoid liability for the failure to disclose ... [when] the company already had information suggesting the merger might not ensue." [33]

This holding may conflict with other circuits, which hold that the disclosure of facts is necessary under the securities laws only when the risk has materialized or where there is a "near certainty" of its occurrence. [34] That said, after *Glazer*, we expect the plaintiffs in the Ninth Circuit to pursue materialization of risk cases even where the risk has not yet occurred.

As 2024 continues, all signs indicate that plaintiffs will continue bringing securities class actions at elevated levels consistent with what we have seen in the past several years. What the filing data suggests is that the securities plaintiffs bar has proven adept at shifting theories and areas of focus when circumstances warrant.

We saw this in 2020 and 2021, when plaintiffs brought an onslaught of COVID-focused suits in response to the coronavirus pandemic; or more recently, in 2021 and 2022, when plaintiffs reacted to the rise in SPACs by filing scores of SPAC-focused securities suits.

Now, as we begin a new year, we expect plaintiffs will continue following the headlines — whether they be based on legal decisions, legislative amendments, macroeconomic developments or world events. And although the theories might change, the end result will be the same: numerous newly filed securities class actions targeting public companies.

Susan L. Saltzstein and Tansy Woan are partners, and William J. O'Brien is counsel, at Skadden Arps Slate Meagher & Flom LLP.

Skadden associate Emily B. Kaplan and law clerks Klara Bieniasz and Carl Wu contributed to this article.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of their employer, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] *Macquarie Infrastructure Corp. v. Moab Partners, L.P.* , No. 22-1165 (2023).

[2] Item 303 obligates a company to describe in its SEC filings "any known trends or uncertainties that have had or that are reasonably likely to have a material favorable or unfavorable impact on net

sales or revenues or income from continuing operations." 17 C.F.R. §229.303. At the time of the alleged violation in this case, Item 303 obligated a company's SEC filings to "[d]escribe any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations." SEC Final Rule Release No. 33-10890, Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information. The SEC explained that the purpose of the amendment from "reasonably expects" to "reasonably likely to have" was to provide "specific guidance" and "a tailored and meaningful framework" for issuers to "objectively analyze whether forward looking information is required" where the likelihood of "known events or uncertainties" cannot be determined. *Id.*

[3] The Court granted certiorari on this exact question in 2017 in *Leidos Inc. v. Ind. Public Retirement Sys.* , No. 16-581 (2017), but the case settled before argument. In *Macquarie*, the government filed an amicus curiae brief in support of Moab, requested divided argument, and reframed the question presented as "[w]hether an issuer's submission of a Form 10-K or Form 10-Q that discloses some but not all of the known trends or uncertainties the issuer was required to disclose under Item 303 . . . can give rise to liability under Section 10(b) . . . and SEC Rule 10b-5." *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, No. 22-1154 (2023) (Brief for the United States as Amicus Curiae Supporting Respondent Moab Partners, L.P., at (I)).

[4] *In re NVIDIA Corp. Sec. Litig.* , 768 F.3d 1046, 1056 (9th Cir. 2014).

[5] See *Oran v. Stafford*, 226 F.3d 275, 288 (3d Cir. 2000) (Item 303 violation "does not automatically give rise to a material omission under Rule 10b-5"); *Carvelli v. Ocwen Fin. Corp.* , 934 F.3d 1307, 1331 (11th Cir. 2019) (Item 303 violation "does not ipso facto indicate a violation of the latter").

[6] See Jean Eaglesham, SEC Wins With In-House Judges, *The Wall Street Journal*, May 6, 2015, <https://www.wsj.com/articles/sec-wins-with-in-house-judges-1430965803>.

[7] *Slack Techs., LLC v. Pirani* , 598 U.S. 759 (2023).

[8] *Id.* at 762.

[9] *Id.* at 768.

[10] *Id.* at 1442.

[11] In addition to their impact on falsity and scienter, short-seller reports may also bear on loss causation if their allegations are drawn from publicly available (i.e., previously disclosed) facts.

[12] See *Leacock v. IonQ, Inc.* , No. 22-1306, at *22 (D. Md. Sep. 28, 2023) (granting motion to dismiss because of plaintiffs' reliance on short-seller report with unsourced allegations) (citing *Tchrs.' Ret. Sys. of La. v. Hunter* , 477 F.3d 162, 174(4th Cir. 2007) ("Under the PSLRA, '[w]hen the complaint chooses to rely on facts provided by confidential sources, it must describe the sources with sufficient particularity.'")).

[13] *In re DraftKings Inc. Sec. Litig.* , 2023 WL 145591, at *18 (S.D.N.Y. Jan. 10, 2023).

[14] *Hershewe v. Joyy, Inc.* , 2023 WL 3316328, at *1 (9th Cir. 2023).

[15] *In re Bolf Holding, Inc. Secs. Litig.* , 977 F.3d 781, 794 (9th Cir. 2020); see also *Macphee v. MiMedx Grp.* , 73 F.4th 1220, 1245 (11 Cir. 2023) ("[T]he mere repackaging of already-public information by an analyst or short-seller is simply insufficient to constitute a corrective disclosure." (citing *Meyer v. Greene* , 710 F.3d 1189, 1199 (11th Cir. 2013))). However, in a footnote, the Meyer court left open the possibility that a short-seller opinion could constitute a corrective disclosure if it reveals "to the market something previously hidden or actively." See *id.* n.10; see also *Bishins v. CleanSpark, Inc.* , 2023 WL 112558, at *13 (S.D.N.Y. 2023) (rejecting that third party analysis of already-public financial information cannot contribute new information and holding that plaintiffs can plead a short-seller report containing such analysis as a corrective disclosure); *In re Chi. Bridge & Iron Co. N.V. Sec. Litig.* , 2020 WL 1329354, at *8 (S.D.N.Y. 2020) (holding short-seller report

could constitute a corrective disclosure because it provided several new pieces of information to the market although it otherwise consisted of public information).

[16] See, e.g., *In re Cassava Scis., Inc. Sec. Litig.* , 2023 WL 3442087, at *8 (W.D. Tex. May 11, 2023); *Handal v. Tenet Fintech Grp. Inc.* , 2023 WL 6214109, at *12 (E.D.N.Y. Sept. 25, 2023) (accepting as true factual allegations contained in the short-seller reports because "the truth or accuracy" of the short-seller reports "are factual disputes not appropriate for resolution at this stage").

[17] See *McIntire v. China MediaExpress Holdings.* , 927 F. Supp. 2d 105, 124 (S.D.N.Y. 2013) (citation omitted); accord *In re Hebron Tech. Co.* , 2021 WL 4341500, at *13 (S.D.N.Y. 2021); see also *In re Cassava Scis., Inc. Sec. Litig.* , 2023 WL 3442087, at *8 ("Other courts have found it permissible to rely on short-seller reports to allege falsity at the motion to dismiss stage" (citing *McIntire*, 927 F. Supp. 2d at 123-24)).

[18] *Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc.* , 77 F.4th 74 (2d Cir. 2023).

[19] *Id.* at 105.

[20] *Id.* at 94.

[21] *Id.* at 83.

[22] *Id.* at 81 (citing *Goldman Sachs Grp., Inc. v. Ark. Tchr. Ret. Sys.* , 141 S. Ct. 1951 (2021)).

[23] *Id.* at 99.

[24] *Id.* at 100.

[25] *Id.* at 101.

[26] Jessica Corso, Goldman's 2nd Circ. Win Opens Path to Class Action Defense, Law360, Aug. 14, 2023, <https://www.law360.com/articles/1710686/goldman-s-2nd-circ-win-opens-path-to-class-action-defense> ("[I]t's up for debate whether other corporations can replicate the fact pattern the investment bank used to win its appeal."). The challenged statements at issue in *Arkansas Teacher* were "highly generic" and being able to point to 36 media reports discussing the alleged conflicts of interest before the SEC settlement helped demonstrate the disclosures had no impact on the company's stock price. See *id.*

[27] In another decision this year, the Second Circuit further clarified its interpretation of *Omnicare*. See *New Eng. Carpenters Guaranteed Annuity & Pension Funds v. DeCarlo* , 80 F.4th 158 (2d Cir. 2023). There, the court considered whether defendant company's historical financial statements, which reflected discretionary decisions, were actionable under the securities laws. The Second Circuit reversed the district court's ruling and held that a statement of opinion that reflects some subjective judgment can nevertheless be actionable under the securities laws if it misleads investors into thinking that the issuer had historical or factual support for the judgment made. See *id.* at 176. According to the court, because the challenged statements incorrectly presupposed the existence of historical evidence for a chosen accounting treatment and implied an "erroneous fact" that payment of discretionary bonuses was not "probable," plaintiffs could proceed with their claim. See *id.* at 172-76.

[28] *In re Facebook, Inc. Sec. Litig.* , 84 F.4th 844, 867 (9th Cir. 2023), opinion amended and superseded on denial of reh'g, 2023 WL 8365362 (9th Cir. Dec. 4, 2023).

[29] *Id.* at 858. The SEC is likewise focused on similar issues. It has promulgated and proposed risk disclosure obligations in cybersecurity and climate change, respectively. And it recently brought an enforcement action against a company and its CISO, alleging that they defrauded investors by, among other issues, understating or failing to disclose known risks.

[30] *Glazer Cap. Mgmt. L.P. v. Forescout Techs., Inc.* , 63 F.4th 747 (9th Cir. 2023).

[31] Id. at 781.

[32] Id. at 780.

[33] Id. at 779 (emphasis added). That said, the decision also stated that "Forescout was aware of a significant likelihood that the risk would materialize." Id. at 781.

[34] See, e.g., *Mia. Firefighters & Police Officers' Ret. Tr. v. CBS Health Corp.*, 46 F.4th 22, 35 (1st Cir. 2022) (speaker only has a duty to disclose facts affecting the likelihood of that risk when the alleged risk had a "near certainty" of occurring or when the warned-of-risk had begun to materialize); *Ind. Pub. Ret. Sys. v. Pluralsight, Inc.*, 45 F.4th 1236, 1254-57 (10th Cir. 2022) (materially misleading risk factors exist where "the risk had materialized or was virtually certain to occur").

All Content © 2003-2024, Portfolio Media, Inc.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Boston Says Pharmacy Benefits Cos. Fueled Opioid Crisis

By Julie Manganis

Law360 (January 12, 2024, 6:01 PM EST) -- Pharmacy benefit managers Express Scripts Inc. and OptumRx allowed opioids to flow into the city of Boston for years, creating a public health crisis for the sake of profit, city officials alleged in a suit filed Friday in state court.

The city's complaint against the two companies and several affiliated entities, including Medco Health Solutions, alleges they created a "public nuisance" by ignoring opportunities to identify the diversion, misuse and abuse of opioids being prescribed to Boston residents, and instead worked with drug manufacturers to boost sales.

It is similar to a **suit filed in California** last August by Los Angeles County against some of the same defendants.

"This case arises from the worst man-made epidemic in modern medical history — an epidemic of addiction, overdose and death caused by an oversupply of opioids flooding communities from powerful corporations who sought to profit at the expense of the public," Boston claims.

The complaint says the defendants and their affiliated entities are "at the center of the opioid-dispensing chain," contracting with pharmacies that dispense them, manufacturers and insurance companies.

Express Scripts and OptumRx are responsible for managing pharmacy benefits for more than 100 million Americans, the complaint says, not only for their corporate parents Cigna and United Healthcare, but for other insurers, including until last year Blue Cross Blue Shield of Massachusetts.

The city says the two companies have "unique insight" into prescribing practices and when patients try to fill multiple prescriptions — or when they seek treatment for addiction or overdose.

The companies "could effectively track the opioid epidemic, pill by pill, as it unfolded," the city contends, yet they failed to use that knowledge.

The companies' role in developing formularies, or lists of covered drugs, also gave them an opportunity to control access in various ways, the city claims. It says the companies were incentivized by manufacturers to place certain drugs on those formularies through rebates and other financial arrangements.

Opioid medications like OxyContin, Opana, Vicodin, Subsys, Duragesic, Ultram and their generic counterparts have been blamed for a steady climb in the number of overdose deaths among Americans since the 1990s, the complaint notes. That has led to a decrease in life expectancy and has made overdose the leading cause of death for adults between 22 and 68, the complaint says.

Messages seeking comment from the city, as well as from Express Scripts and OptumRx late Friday, did not immediately receive a response.

The city of Boston, its Public Health Commission and Housing Authority are represented by Christopher C. Naumes and Robert T. Naumes Sr. of Naumes Law Group LLC, Vincent Greene, Linda Singer and Elizabeth Smith of Motley Rice LLC, as well as the city's Adam Cederbaum, the Public Health Commission's Batool Raza and the Housing Authority's Caesar P. Cardozo.

Counsel information for the defendants was not immediately available.

The case is The City of Boston et al., v. Express Scripts Inc., et al., case number 2484CV00107, in the Suffolk County Superior Court of the Commonwealth of Massachusetts.

--Editing by Philip Shea.

All Content © 2003-2024, Portfolio Media, Inc.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Gatos Silver Brass Sued Over Lowering Of Mining Estimates

By **Katryna Perera**

Law360 (January 12, 2024, 6:39 PM EST) -- Officers and board members of precious metals producer Gatos Silver Inc. have been hit with a shareholder derivative suit in Delaware federal court over claims that their Mexican operation fell far short of expectations.

Noah Orozco filed a **complaint** on Thursday against Gatos' former CEO Stephen Orr and several board members alleging breaches of fiduciary duties, unjust enrichment and other counts for misconduct that allegedly occurred between March 2021 and January 2022 in connection with the company's initial and secondary public offerings.

According to the complaint, Gatos produces, develops and explores for precious metals, primarily focusing on silver and zinc, and much of the company's operations involve the exploration and development of the Cerro Los Gatos mine in Mexico.

In October 2020, Gatos conducted its IPO and **raised \$156 million** by listing 24 million shares — nearly 2.7 million more than expected — for \$7 each, the low end of the \$7 to \$9 price range it determined in its SEC filings.

The company told the SEC it would use the money to repay debt, increase its stake in a joint venture, further develop an existing mine and open new ones.

The IPO registration statement and prospectus "heavily cited" a July 2020 technical report published by Tetra Tech Inc., according to the complaint. Orozco says that although the registration statement cautioned that the mineral reserve estimates and economic analyses contained in the report were merely estimates, the individual defendants represented that the start of mining operations would allow Gatos to assess the accuracy of the estimates.

The company conducted an SPO in July 2021. It raised over \$118 million from an offer of roughly 9 million shares priced at \$14 per share, the complaint states, and the registration statement for the SPO also referenced the technical report.

Orozco claims that throughout the relevant period, the defendants misrepresented that the activities and results at the Mexico mine "would not result in a material change to the information contained in the Los Gatos Technical Report," thereby supporting the purported reliability of the estimates in the Los Gatos Technical Report."

However, on Jan. 25, 2022, the company disclosed errors in the report and indications that there had been overestimations in the report's resource model, according to the complaint.

The company also revealed that it had overestimated the metal content in the Mexico mine by 30% to 50%, according to the complaint.

On this news, Orozco says Gatos' stock price fell 69% in one day, closing at \$3.17 per share on Jan. 26, 2022. On Friday, Gatos' stock was trading around \$6.50.

As a result of the defendants' alleged misconduct, the company is also now facing a securities class action, according to Orozco.

The suit seeks damages, disgorgement, attorney fees and a jury trial.

Representatives for the parties did not immediately respond to requests for comment on Friday.

Orozco is represented by Phillip Kim and Erica L. Stone of The Rosen Law Firm PA and Brian E. Farnan and Michael J. Farnan of Farnan LLP.

Counsel information for the defendants was not immediately available.

The case is Orozco v. Stairs et al., case number 1:24-cv-00040, in the U.S. District Court for the District of Delaware.

--Editing by Jeremy Abrams.

All Content © 2003-2024, Portfolio Media, Inc.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Scrubs Co. Investors Sue Board, Insiders In Del. After Losses

By **Jeff Montgomery**

Law360 (January 12, 2024, 7:38 PM EST) -- Stockholders of Figs, a supplier of clothing for healthcare workers, have sued insiders of the business in Delaware's Court of Chancery, seeking to recover, for the company, what they allege are mismanagement losses and massive unfair trading gains benefiting controlling investors and directors.

In a stockholder derivative complaint filed Wednesday, investor Lloyd Kimmen said Figs' troubles were partly tied to misleading claims about strategies that purportedly allowed the company to reliably predict clothing supply decisions by healthcare companies and workers, minimizing inventory costs and the expenses of shipping from manufacturers in China.

Those achievements touted by management, however, were illusory, with costly truths undisclosed, Kimmen told the Chancery Court.

"Since its IPO, the company's inventories ballooned from 164 average days inventory outstanding as of fiscal 2020 up to 350 days inventory outstanding as of fourth quarter 2022," the investor said. "Figs' average days of inventory outstanding increased almost every quarter since its IPO and reached a peak of 365 days for third quarter 2022."

The allegations in the Delaware suit closely follow conduct now at issue in a federal securities class action in California federal court. Among other claims, investors in both suits accused four insiders of selling nearly \$1 billion of shares in Figs Inc. during an initial public offering that closed in June 2021 and a special public offering that September at inflated prices, while possessing undisclosed negative information. The California case is now awaiting U.S. District Judge Otis D. Wright II's ruling on a dismissal motion, which he took under consideration without argument.

Those singled out in the Delaware complaint included Figs co-founders and co-CEOs Heather Hasson and Catherine Spear, as well as Thomas Tull, who is founder, chair and CEO of Tulco Holdings, which controlled 51% of the clothing company's voting power prior to its IPO. Together, the trio held 78.3% of Figs' votes before the company went public, according to the complaint. Tull himself owned about 47.3% of Tulco while controlling a significant portion of Figs' voting power through both his personal ownership and Tulco's share of Figs' common stock, investors said.

Kimmen leveled claims of breaches of fiduciary duty against the scrubs distributor's directors and officers, Tull and Tulco, as well as insider trading and unjust enrichment claims against Hasson, Spear, Tull and Tulco.

The Delaware filing noted the medical scrubs supplier's growth ramped up during a period of surging demand fueled by the COVID-19 pandemic, with healthcare professionals turning to easily changed and disinfected scrubs in large numbers.

In 2020, before its IPO, Figs' net revenues more than doubled year-over-year from \$110 million to \$263 million, with 82% of 2020 net revenues stemming from core scrubwear sales, the complaint noted.

The company claimed it rapidly diversified its product lines at the same time, with inventory costs sharply increasing as sales of new, non-core, non-scrubwear products fell behind forecasts, the investors said. Meanwhile, the suit added, shipping costs and delays rose because of a need to rely

on costlier air freight rather than ocean shipping to meet deadlines for core products.

According to the complaint, Figs nevertheless told investors in the months prior to the IPO and secondary public offering that it was managing purchasing and inventory effectively and efficiently, despite ballooning costs. Following the 2021 stock offerings, however, Figs stock fell from more than \$44 per share to \$6.76 per share on March 1, 2023, and continued to slip afterward.

Hasson, Spear, Tulco and Tull timed stock sales to take advantage of the public's ignorance of the concealed facts and obtain a higher price for the shares they sold, the suit alleged. The defendants thereby profited by misappropriating Figs' material nonpublic information, according to the complaint.

At least five of the supplier's directors were accused of allowing the company to rely on materially misleading statements suggesting that the use of more costly air freight was temporary.

"As a result, these five defendants face a substantial likelihood of liability," the suit said. That's a majority of the company's board and enough to "excuse" the stockholders from first demanding that the board itself consider whether to pursue derivative claims against the named individuals and Tulco, and instead sue on the company's behalf, the filing continued.

Hasson and Spear, as co-CEOs, cannot be considered independent under New York Stock Exchange rules, the investors asserted. Both, as employees, "derive substantially all of their income from their employment with Figs, thus could not disinterestedly consider a demand for action that might require them to sue the directors that control their continued employment" and that of fellow managers, they said.

Figs went public in May 2021, **raising \$580 million** in its initial public offering. The company offered 26.4 million shares at \$22 each, above the expected range of \$16 to \$19.

Figs, Tull and Tulco did not immediately respond to requests for comment Friday.

Kimmen and the proposed class of investors are represented by Ryan M. Ernst of Bielli & Klauder LLC, and Gustavo Bruckner, Samuel J. Adams and Ankita Sangwan of Pomerantz LLP.

The case is Kimmen v. Hasson et al., case number 2024-0014, in the Court of Chancery of the State of Delaware.

--Editing by Covey Son.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Up Next At High Court: Chevron Deference, Corp. Filings

By **Katie Buehler**

Law360 (January 12, 2024, 4:38 PM EST) -- The U.S. Supreme Court will be closed Monday for Martin Luther King Jr. Day and will begin a short oral argument week Tuesday, during which the justices will consider overturning Chevron deference, a decades-old doctrine that instructs courts to defer to federal agencies' interpretations of ambiguous statutes.

The justices will also hear arguments over whether investors can sue companies for violating a provision of securities law requiring them to alert investors about possibly harmful trends and uncertainties, and whether individuals can sue states under the Fifth Amendment's takings clause in federal court.

Additionally, the court will issue an orders list Tuesday related to its latest conference.

Here, Law360 breaks down this week's oral arguments.

Corporate Silence

On Tuesday, the justices will first consider **whether investors can sue** under a provision of securities law known as Item 303, which requires management of public companies to alert investors about possible trends or uncertainties that could harm the company down the line.

Macquarie Infrastructure Corp. has asked the Supreme Court to reverse a Second Circuit decision reviving a putative class action brought by lead plaintiff Moab Partners LP seeking to hold Macquarie and its management liable for failing to warn investors that a forthcoming international ban on high-sulfur fuels would hurt the company's bottom line.

The appellate panel held that omissions of impactful trends or uncertainties in securities filings can be the basis for claims under Section 10(b) of the **Securities Exchange Act**, which prohibits deception related to the purchase or sale of securities. Macquarie claims the Second Circuit's ruling contradicts holdings by the Third, Ninth and Eleventh circuits, which have all held that Item 303 doesn't create a duty to disclose that is punishable by Section 10(b).

Macquarie argues that Item 303 "does not create a hard-and-fast rule about what to disclose" and that allowing investors to privately file securities fraud lawsuits would be "crippling." The company also contends that investors shouldn't be allowed to sue over omissions of Item 303 disclosures because omissions, by their nature, include no false or misleading information.

Moab Partners **counters** that the act of failing to inform investors about harmful trends or uncertainties is itself misleading. It also told the justices that the alleged circuit split is "superficial and unimportant in practice" and likely to resolve itself. The Third and Eleventh circuit holdings merely state that an Item 303 violation doesn't automatically create a Section 10(b) claim. Only the Ninth Circuit has said a violation could never create a claim, Moab Partners said.

The U.S. Securities and Exchange Commission **agrees with Moab Partners**, arguing in an amicus brief that investors should be allowed to bring suits over Item 303 violations. Supreme Court precedent — particularly the court's 2016 decision in **Universal Health Services Inc. v. U.S. ex rel. Escobar** — states that claims can be misleading even if they lack falsehoods.

The U.S. Solicitor General's Office will argue for the SEC as amicus in favor of Moab Partners.

Winston & Strawn LLP partner Linda T. Coberly will argue for Macquarie, and Kellogg Hansen Todd Figel & Frederick PLLC partner David C. Frederick will argue for Moab Partners. Ephraim McDowell of the U.S. Solicitor General's Office will argue for the SEC.

The case is Macquarie Infrastructure Corp. et al. v. Moab Partners LP et al., case number 22-1165, in the U.S. Supreme Court.

Takings Clause Litigation

Also on Tuesday, the Supreme Court will hear arguments in a dispute stemming from the state's construction of a barrier along Interstate 10 in Texas. Landowners have asked the court to weigh in on whether state or federal courts are the proper venue when **individuals bring** Fifth Amendment takings clause suits against states.

Richard Devillier, a Houston resident who claims his property flooded after the Texas Department of Transportation put up the barrier, has urged the justices to reverse a Fifth Circuit finding that states can't be sued in federal court over takings disputes by private owners because the U.S. Congress hasn't created that right.

Devillier and more than 100 other Texas landowners have asked the high court to find individual suits are allowed because the takings clause is self-executing, or enforceable, despite a lack of related federal legislation. The landowners said the Supreme Court has spoken on the issue before in its 1987 ruling in **First English Evangelical Lutheran Church of Glendale v. County of Los Angeles** , which found claims for just compensation are "grounded in the Constitution itself."

Texas, meanwhile, argues that takings claims filed against states are best handled by state courts. State courts have the authority to hear the inverse condemnation claims in this suit under both the U.S. and Texas constitutions, which have specific provisions giving private individuals the right to seek compensation, Texas said.

The U.S. Solicitor General's Office filed an amicus brief in favor of Texas in the case, supporting the Lone Star State's claim that **state courts are the proper venue** for Devillier's claims. The office noted that the U.S. Constitution's allocation of powers to Congress over fiscal matters is proof the Fifth Amendment was never intended to be self-executing.

The office will argue as amicus in favor of Texas.

Robert J. McNamara, deputy litigation director for the Institute for Justice, will argue for Devillier, and Texas Solicitor General Aaron L. Nielson will argue for Texas. Edwin S. Kneeder of the U.S. Solicitor General's Office will argue for the federal government.

The case is Devillier et al. v. Texas, case number 22-913, in the U.S. Supreme Court.

Chevron Deference

The justices on Wednesday will hear arguments in two of the **most highly anticipated cases** this term, which both ask the court to consider overturning a decades-old doctrine that instructs courts to defer to federal agencies' interpretations of ambiguous statutes.

New England fish companies Loper Bright Enterprises and Relentless Inc., a subsidiary of Seafreeze Fleet LLC, have asked the Supreme Court to reverse two decisions from the D.C. and First circuits, respectively, that applied the court's so-called Chevron deference doctrine in upholding a National Marine Fisheries Service rule requiring fishers to pay part of the cost of having federal compliance monitors aboard their ships.

The circuit courts deferred to NMFS' interpretation of the **Magnuson-Stevens Fishery Conservation and Management Act** , which the agency claims authorizes it to require fishers to pay up to 20% of the salaries of monitors they're forced to host on board their ships.

In addition to challenging the NMFS rule, Loper Bright and Relentless have also encouraged the Supreme Court to overrule its 1984 decision in [Chevron v. Natural Resources Defense Council](#) , which established the doctrine. They argue the Chevron doctrine wrongly protects federal agencies from judicial review and **encourages aggressive rulemaking** by presidential administrations.

The U.S. Department of Commerce has called the Chevron deference doctrine a "bedrock principle of administrative law" that shouldn't be disturbed. The government also contends that fishers' challenges do not warrant the court's forsaking the principle of stare decisis, or honoring a court's previous decisions.

But the federal government may have a tough hill to climb in this case. Several members of the court, including Justices Clarence Thomas, Neil Gorsuch and Brett Kavanaugh, have made their disdain for the Chevron deference doctrine clear in previous writings.

A ruling dismantling the doctrine would reverberate across the federal government and affect agencies that aim to protect civil rights, education, the environment, financial markets, healthcare and workers.

Attorneys on Wednesday will first argue the Relentless case and then will present arguments in the Loper Bright case. Justice Ketanji Brown Jackson has recused herself from the Loper Bright case.

Latham & Watkins LLP partner Roman Martinez will argue for Relentless, and Clement & Murphy PLLC partner Paul D. Clement will argue for Loper Bright Enterprises. U.S. Solicitor General Elizabeth B. Prelogar will argue for the federal government.

The cases are Loper Bright Enterprises et al. v. Gina Raimondo et al., case number 22-451, and Relentless Inc. et al. v. Department of Commerce et al., case number 22-1219, in the U.S. Supreme Court.

--Editing by Khalid Adad.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

High Court Won't Review Rabobank Chicken Price-Fixing Win

By **Matthew Perlman**

Law360 (January 16, 2024, 9:59 AM EST) -- The U.S. Supreme Court refused on Tuesday to review contentions from chicken buyers that a lower court was wrong to toss their claims that Rabobank helped orchestrate an industrywide price-fixing scheme.

The justices denied **a petition** from chicken buyers, including Campbell Soup Co. and Target Corp., that are bringing their own suits in **broader litigation** accusing major chicken producers of fixing prices for broiler chicken.

The buyers were asking to review a Seventh Circuit panel ruling that **affirmed dismissal** of the claims against Rabobank in July. The appeals court found that the buyers had shown only that the agricultural bank knew basic economics — that low supply would lead to higher prices — and not that the bank worked with producers to effectuate supply cuts.

The buyers argued in their petition that the court effectively granted summary judgment in favor of Rabobank even though it moved only for dismissal of the claims, which the buyers said conflicts with Supreme Court precedent and the Federal Rules of Civil Procedure.

Had Rabobank actually moved for summary judgment, the buyers said, they could have responded by requesting to defer consideration of the motion until after they finished negotiating over additional discovery. The petition said this is key because, after the dismissal ruling, a former Pilgrim's Pride CEO invoked his Fifth Amendment right against self-incrimination during a deposition when asked about Rabobank's involvement in the alleged scheme.

The petition also said the appellate panel "overlooked or misapprehended" allegations in the complaint that show Rabobank helped facilitate the activity.

The claims against Rabobank stem from sprawling **antitrust litigation** dating back to September 2016 accusing the nation's largest broiler chicken producers, including Tyson Foods and Pilgrim's Pride, of conspiring to fix, raise and maintain prices for broiler chicken, the industry term for most chicken sold for human consumption.

U.S. Circuit Judge Frank H. Easterbrook wrote in the Seventh Circuit panel's opinion in July that several buyers added their claims against Rabobank after discovery in the broader litigation turned up evidence suggesting the agricultural bank, which is a lender to several of the chicken suppliers, urged at least two of the companies to cut production.

But the judge said the lower court **tossed the allegations** after finding the buyers did not allege that Rabobank facilitated an agreement among producers or helped with its enforcement, and instead had only shown that the bank was looking out for its own interests.

In January, the Supreme Court denied a petition from buyers in the broader price-fixing litigation, also including Campbell Soup and Target, that sought to **challenge** a judgment sharing agreement, or JSA, between 14 of the chicken producers. That petition contended the JSA reduces the buyers' leverage in settlement negotiations by preestablishing each chicken producer's potential responsibility in the case.

Other buyers in the broader litigation saw an Illinois jury in October **reject their claims** against the

only producer that had not settled with them, Sanderson Farms. Additional trials for other groups of buyers are slated for later this year, according to court records.

The buyers appealing the Rabobank ruling are represented by Scott E. Gant of Boies Schiller Flexner LLP.

Rabobank was represented in the lower courts by David J. Doyle and Jill C. Anderson of Smith Gambrell & Russell LLP.

The case is Amory Investments LLC et al. v. Utrecht-America Holdings Inc. et al., case number 23-515, at the U.S. Supreme Court.

--Additional reporting by Nadia Dreid, Lauraann Wood, Celeste Bott, Christopher Cole and Katie Buehler. Editing by Daniel King.

All Content © 2003-2024, Portfolio Media, Inc.



Portfolio Media, Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Justices Won't Upend 'Conspiracy Jurisdiction' Claims

By **Bryan Koenig**

Law360 (January 16, 2024, 9:50 AM EST) -- The U.S. Supreme Court rejected an appeal Tuesday from two London-based metals trading banks fighting to upend the Second Circuit revival of antitrust allegations of manipulation of platinum and palladium market values.

The justices' decision leaves intact the Second Circuit's finding that a conspirator's alleged participation was enough to rope them into the litigation.

As is customary, the justices offered no explanation for their decision not to take up the petition from ICBC Standard Bank Plc and BASF Metals Ltd. arguing they should not have been included in the consolidated suit alleging the manipulation of benchmark prices of the precious metals.

The Second Circuit **revived the suit last year**, overruling a district court's ruling that two plaintiffs lacked standing to sue as "efficient enforcers." ICBC and BASF took issue with a different part of the case; the appellate court's affirmance of findings, which they'd cross-appealed, that the two overseas defendants can be sued, even though they ostensibly have no U.S. ties, because the court does have jurisdiction over an alleged conspirator.

"According to the Second Circuit, a defendant can be subject to specific jurisdiction in a forum where the defendant has no contacts at all. This is so because of a jurisdictional theory that this court has never endorsed: conspiracy jurisdiction," the banks said in their September petition. "The question here is whether conspiracy jurisdiction comports with the fundamental requirements of due process."

The petition described the case from plaintiffs KPFF Investment Inc., Larry Hollin and White Oak Fund LP, who also targeted Goldman Sachs International, HSBC Bank, UBS AG and the London Platinum and Palladium Fixing Co., as "an ideal vehicle" to tackle conspiracy jurisdiction because the "issue is outcome determinative and was squarely presented to and addressed by both the district court and the Second Circuit."

According to ICBC and BASF, even the lower court was uneasy about conspiracy jurisdiction.

"As the district court recognized here, 'conspiracy jurisdiction' is 'extraordinarily broad' and allows courts to 'exercise personal jurisdiction over a defendant based on the actions of a co-conspirator who is entirely unknown to that defendant,'" they said. "And as the Second Circuit explained, conspiracy jurisdiction is not 'limited by agency principles.' ... Instead, it has 'expanded beyond its more limited roots,' and now exists even where the defendant has no control over the alleged co-conspirator."

Ultimately, according to the petition, the lower court had its hand forced by a pair of separate Second Circuit decisions called Schwab I and Schwab II. Those decisions represent "a sharp departure from its decades-long rejection of such jurisdiction," according to the petition, which argued of a circuit split over the issue that "is deep, acknowledged, and entrenched."

The Supreme Court had previously **rejected a conspiracy jurisdiction case** in a decision in which Chief Justice John G. Roberts, Justice Elena Kagan and Justice Neil Gorsuch played no part. But here, ICBC and BASF had argued their case "has many fewer parties—presumably would not raise the same recusal considerations."

In opposing high court intervention, the plaintiffs had argued in a December brief that the banks are raising alarm over a circuit split "that does not exist."

"There is nothing unusual about the Second Circuit's conclusion that the U.S. traders harmed by the petitioners' U.S. market manipulation can sue them in the United States. To the contrary, American courts—including this one—have been hearing cases much like this since Congress enacted the antitrust laws over a century ago," they said. "And every circuit to have considered the issue agrees that personal jurisdiction may constitutionally be premised on a defendant's participation in such a conspiracy."

According to the plaintiffs, every circuit has held that personal jurisdiction can be established by a conspiracy.

"The petitioners don't even try to argue that it is somehow unconstitutional for U.S. courts to exercise jurisdiction over a defendant that harms U.S. traders by manipulating a U.S. market," they said. "Instead, they contend that, as a general matter, basing jurisdiction on a defendant's participation in a conspiracy runs afoul of this court's precedent requiring that jurisdiction rest on a defendant's own conduct. But, as the Second Circuit explained, participating in a conspiracy with sufficient forum contacts to support jurisdiction is a defendant's own conduct."

ICBC Standard Bank Plc is represented by Robert G. Houck and John D. Friel of Clifford Chance US LLP. BASF Metals Ltd. is represented by Michael F. Williams, Peter A. Farrell, Jennifer K. Hardy, William P. Kimmitt and Aaron L. Nielson of Kirkland & Ellis LLP.

The plaintiffs are represented by Jennifer Bennett, Eric Citron and Stefanie Ostrowski of Gupta Wessler LLP, Gregory S. Asciolla and Matthew J. Perez of Dicello Levitt LLP and Michael Dell'angelo, Candice Enders and Zachary Caplan of Berger Montague PC.

The case is BASF Metals Limited, et al. v. KPFF Investment Inc., et al., case number 23-232 in the U.S. Supreme Court.

--Additional reporting by Elliot Weld, Hailey Konnath and Dave Simpson.

All Content © 2003-2024, Portfolio Media, Inc.

Morgan Stanley To Pay \$249M In Block Trading Probe

By **Pete Brush, Elliot Weld and Frank G. Runyeon**

Law360 (January 12, 2024, 10:09 AM EST) -- Morgan Stanley will pay \$249 million to resolve allegations that it and a former supervisor made false statements and misused information about block trades — large, market-moving stock purchases — that allowed others to profit, according to agreements announced Friday by New York criminal prosecutors and securities regulators.



Ex-Morgan Stanley executive Pawan Passi leaves Manhattan federal court Friday after inking a deferred prosecution agreement with prosecutors. (Frank G. Runyeon | Law360)

Under a non-prosecution agreement, the bank is paying fines, penalties, interest and disgorgement after instituting remedial measures to prevent what Manhattan U.S. Attorney Damian Williams characterized as "serious" misconduct in securities markets. The penalties are made up of a \$136.5 million payment to resolve the probe by Williams' office and \$112.8 to resolve related civil claims by the U.S. Securities and Exchange Commission.

Williams credited Morgan Stanley for its "extraordinary cooperation and remediation" but said the misconduct had been uncovered by the government's investigation, rather than disclosed by the company.

"This fact serves as a reminder that we are watching," Williams said in a statement. "And we will continue to use all the tools at our disposal to root out fraud in our financial markets."

Morgan Stanley said in a statement that it was "pleased to resolve these investigations and are confident in the enhancements we have made to our controls around block trading, including strengthening our policies, procedures, training and surveillance."

"The core of this matter is the misconduct of two employees who violated the firm's policies, procedures and our core values, as outlined in the settlement documents," the company added.

One of those employees, the former supervisor of Morgan Stanley's block trades business, Pawan Passi, entered into a deferred prosecution agreement under which he will avoid criminal charges if he complies with the terms of the six-month deal. Passi admitted that from 2018 to August 2021, he disclosed confidential block trading information to prospective buyers for them to trade on.

The ex-Morgan Stanley executive was arraigned Friday morning before U.S. Magistrate Judge Robyn F. Tarnofsky after signing the agreement.

"You are charged with securities fraud," Judge Tarnofsky said, citing the information filed with the court. "What is your plea?"

"Uh, not guilty," Passi said quietly.

Judge Tarnofsky told the former Morgan Stanley executive that he would be free to go under the terms of the deal but must stay in the Southern District of New York, Eastern District of New York and New Jersey. With a few months of good behavior, she said, his criminal case would be gone.

"You have been given a real opportunity here today to avoid a criminal conviction," Judge Tarnofsky told the defendant. "I hope that this is the only time I see this case again and that in the future the judge will dismiss these charges against you."

"Thank you," Passi said. He declined to comment as he left the courthouse.

A block trade generally involves the sale of a large quantity of shares of an issuer's stock, privately arranged and executed outside the public markets.

"In block trading, confidentiality is sacrosanct and it's hard to predict whether this type of conduct has been widespread," said Kurt Gotschall of Haynes & Boone, who was not involved in the case. "We can expect that the SEC Examinations and Enforcement's Market Abuse Unit will be on the lookout for similar conduct at other firms."

From at least June 2018 through August 2021, Passi and an unnamed subordinate on Morgan Stanley's equity syndicate desk disclosed non-public, potentially market-moving information concerning impending block trades to select buy-side investors despite the sellers' confidentiality requests and Morgan Stanley's own policies, the SEC said.

The information shared by Passi and the subordinate employee included the precise timing of upcoming trades and the expected size and prices, the SEC said. The hedge funds that received the information were able to trade on it, generally by taking large short positions in the relevant stock and, according to the release, Passi would sometimes guide the funds in how the information would be best used in the market.

The hedge funds, in return, would buy large amounts of shares from Morgan Stanley when it executed the block trades, according to the release. The SEC said the unit under Passi's supervision generated over \$72 million in profits from the blocks, to the detriment of the block sellers.

Potential block sellers were told that because Passi's unit was located on the private side of Morgan Stanley's business, they could rest assured that news of their block would not leak, according to the SEC. A seller was allegedly sent promotional information that said Morgan Stanley "continues to be #1 by a wide margin" in the "block space."

"As far as what differentiates us, we're the only shop who does everything (pricing/sizing) fully on the private side," a Morgan Stanley employee allegedly wrote to a potential seller. "All others will wall-cross traders to inform views, which leads to leaks/selloffs."

Passi allegedly had a group of "favored investors" whom he called multiple times per day in the buildup to block trades.

In one example given by the SEC, Passi held a series of conversations with a New York-based hedge fund trader about an impending block trade, sharing detailed information about it. The trader, in turn, told Passi details of a short sale of 1.5 million shares of relevant stock and was reassured by Passi once the block trade occurred that Passi would give the trader a block allocation large enough to cover the trader's short position, according to the SEC.

In April 2021, Greece-based shipping company Star Bulk Carriers Corp. began expressing interest in selling block shares and was assured by multiple employees, Passi among them, that the upcoming sale would be kept confidential, according to the SEC.

However, Passi kept the founder of a different New York-based hedge fund updated almost daily on the details of his communication with Star Bulk Carriers, the SEC said. In May of that year, Morgan Stanley executed a block trade of 10.6 million Star Bulk Carriers shares after the markets closed for the day and allocated 2 million of those shares to the hedge fund founder, according to the SEC. The hedge fund used some of those shares to cover a short position that he'd entered, allegedly at Passi's recommendation.

Passi is represented by James G. Cavoli, George S. Canellos, Samantha Lovin and Emily Scarisbrick Weisberg of Milbank LLP.

Morgan Stanley is represented by Steven R. Peikin and Alexander J. Willscher of Sullivan & Cromwell LLP.

The government is represented by Margaret Graham, Sam Rothschild and Justin Rodriguez of the U.S. Attorney's Office for the Southern District of New York.

--Additional reporting by Jessica Corso. Editing by Alyssa Miller.

Update: This story has been updated with more details and counsel information.

All Content © 2003-2024, Portfolio Media, Inc.