

## Securities Law Update

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### US Supreme Court Declines to Expand Liability to Secondary Actors in Securities Cases

In December 2010, the U.S. Supreme Court heard oral arguments in *Janus Capital Group, Inc. v. First Derivative Traders*. The Court considered whether Janus Capital Group (“JCG”), as an investment adviser to Janus Investment Fund, may be sued as a primary violator of Section 10(b) and Rule 10b-5. Last week, the Court issued a 5-4 decision and declined to expand 10b-5 liability to JCG. The Court held that JCG could not be sued as a primary violator of federal securities laws because it did not have the “ultimate authority” to make the allegedly misleading statement issued by the Janus Investment Fund. The Court’s decision rejects a significant expansion of potential federal securities law liability for a broad range of secondary actors and advisers who do not control the content of the issuer’s allegedly misleading statement, including attorneys, accountants and others.

JCG is a publicly traded financial services company that created and manages the Janus family of mutual funds through its subsidiary, Janus Capital Management LLC (“JCM”). The shares purchased by the plaintiff investors in this case were those offered by one of the parent company’s mutual funds. The putative class of investors included those who bought shares of common stock between July 21, 2000, and September 2, 2003, and still held those shares on September 2, 2003, when the stock price fell, allegedly as a result of public disclosure of JCG and JCM’s alleged misrepresentations.

The prospectus for the funds stated that the shares were “not intended for market timing or excessive trading” and that the Janus Investment Fund had measures in place to stop and deter market timing trading. Plaintiffs alleged that these statements were misleading and that the parent company was a service provider involved in the preparation and dissemination of its subsidiaries’ prospectuses. Although the parent company’s name was not associated with the filing, the plaintiffs alleged that JCG and JCM wrote the policies regarding market timing that were included in the funds’ prospectuses and that they caused the funds to include this language.

The district court dismissed the plaintiff investors’ claims by stating that there were no allegations showing that JCG made or prepared the allegedly misleading statements with the result that the statements were not attributable to JCG. The court also dismissed the claims against JCM finding that it did not owe any duties to the shareholders.

The Fourth Circuit reversed, ruling that JCM participated in writing and disseminating the prospectus, which is sufficient to establish 10b-5 liability. The Fourth Circuit further held that investors would infer that JCG played a role in preparing the prospectuses that contained the allegedly fraudulent information. Significantly, the Fourth Circuit's decision could have undermined the Supreme Court's prior decisions in *Central Bank* and *Stoneridge*, which held that there is no secondary liability for aiding and abetting in a Rule 10b-5 private action.

On appeal, the Supreme Court reversed the Fourth Circuit and held that because the allegedly false statements in the prospectuses were made by Janus Investment Fund, not by JCM or JCG, JCM and JCG could not be held liable in a private action under Rule 10b-5. The Court went on to state that for Rule 10b-5 purposes, the maker of a statement with potential primary 10b-5 liability is the person/entity with "ultimate authority" over the statement, including the content of the statement and whether and how to communicate it. Without such control, a person or entity can suggest what to say, but cannot "make" a statement in its own right. The Court therefore rejected the argument that the "maker" of a statement should be defined expansively to include those who "created" the statement, which would allow a private plaintiff to sue a person who authors or provides the allegedly false or misleading information. Even if JCM or JCG were significantly involved in preparing the prospectuses, the Court found that their assistance in crafting the statement was subject to Janus Investment Fund's ultimate control.

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