University of Michigan Journal of Law Reform

Volume 47 | Issue 3 Article 8

2014

The Two Faces of Janus: The Jurisprudential Past and New Beginning of Rule 10b-5

John Patrick Clayton
University of Michigan Law School

Recommended Citation
John P. Clayton, *The Two Faces of Janus: The Jurisprudential Past and New Beginning of Rule 10b-5*, 47 U. MICH. J. L. REFORM 853 (2014).
Available at: https://repository.law.umich.edu/mjlr/vol47/iss3/8

THE TWO FACES OF *JANUS*: THE JURISPRUDENTIAL PAST AND NEW BEGINNING OF RULE 10b-5

John Patrick Clayton*

Section 10(b) of the Securities Exchange Act and its implementing Rule 10b-5 are the primary antifraud provisions for both private and public enforcement of the federal securities laws. Neither the statute nor the rule expressly provides for a private right of action, but federal courts have long recognized such an implied right, and the Securities and Exchange Commission has supported the implied private right of action as a "necessary supplement" to its own efforts. However, after a decade of applying an expansive interpretation to Section 10(b), in the early 1970s the U.S. Supreme Court began to narrowly interpret this implied private right of action, citing concerns about the costs that frivolous litigation may impose on capital markets. Most recently, in Janus Capital Group, Inc. v. First Derivative Traders*, the Supreme Court constricted the ambit of Rule 10b-5(b)—which imposes liability for fraudulent misstatements—by narrowly interpreting the word "make" in a way that effectively removes entire categories of plaintiffs from liability under Rule 10b-5(b). While* Janus *involved private plaintiffs, the Court's interpretation cannot easily be distinguished on the basis of the plaintiff's identity. Therefore,* Janus *appears to limit the Commission to the same extent that it does private plaintiffs, even if such a limitation was not the Court's intent.*

This Note offers a solution to the Commission's Janus *problem, whereby the Commission could use its rulemaking authority to implement a "New Rule 10b-5." This New Rule 10b-5 would be drafted so that only the Commission could use it to prosecute fraud, addressing the Court's concern about the potential costs of expanding private litigation. Additionally, the New Rule 10b-5 could substitute different language for the word "make" so that the Commission could sidestep the Court's restrictive interpretation of that word's meaning. Going forward, this bifurcated approach to Section 10(b)—with separate rules for private and public enforcement—would allow the courts to interpret the contours of each cause of action without inadvertently restricting or expanding the scope of the other.*

* Associate, Corporate and Securities Practice, Akin Gump Strauss Hauer & Feld LLP; J.D., 2013, University of Michigan Law School; M.A., 2007, New York University; B.M., 2005, University of North Texas. The author would like to thank the *Journal of Law Reform* editors, Professor Adam C. Pritchard, Frances and George Skestos Professor of Law at the University of Michigan Law School, and Michael C. Baker, Enforcement Attorney at the Securities and Exchange Commission, all of whom provided helpful comments and suggestions during the writing of this Note. The views expressed in this Note are those of the author and are not necessarily shared by any others, including Akin Gump Strauss Hauer & Feld LLP or the Securities and Exchange Commission.

Introduction

In ancient Roman mythology, Janus was the god of both beginnings and transitions.[1] Because he simultaneously looked to the past and to the future, Janus was usually depicted as having two faces.[2] The name Janus is significant in the world of securities law because of the pivotal Supreme Court case *Janus Capital Group, Inc. v. First Derivative Traders*.[3] In *Janus*, the Court attempted to create a bright-line rule for deciding who "makes" a material misstatement for the purposes of securities fraud liability under Section 10(b) and Rule 10b-5. Specifically, in *Janus*—a private lawsuit—the Court limited the category of defendants subject to Rule 10b-5(b) by holding that only those with "ultimate authority" over the content of a materially misleading statement can be liable as the "maker" of the statement.[4] This strict approach contrasts with the more broadly construed "creation" standard, which would have allowed misstatement liability to attach to an individual as long as a plaintiff established that the individual "create[d]" the misstatement.[5] Considering the Supreme Court's Section 10(b) and Rule 10b-5 jurisprudence,[6] it was no surprise that the Court opted for the more stringent interpretation in this private action.

However, the Court's reasoning is potentially problematic for the Securities and Exchange Commission ("the Commission"). The Court based its entire decision on a restrictive interpretation of the word "make" that, because it is contained in Rule 10b-5(b), is used by both private plaintiffs and the Commission alike when bringing actions pursuant to Section 10(b). While the Court's concern for confining the reach of the implied private right of action clearly underlay its interpretive approach,[7] there is no way to meaningfully distinguish the holding's application on the basis of the plaintiff's identity.[8] Therefore, *Janus* appears to restrict the Commission when

1. *See* Edith Hamilton, Mythology 51 (Back Bay Books 1998) (1942).
2. *See id.*
3. 131 S. Ct. 2296 (2011).
4. *Janus*, 131 S. Ct. at 2302 ("For purposes of Rule 10b-5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it.").
5. *See, e.g.*, Brief for the United States as Amicus Curiae Supporting Respondent at 8, Janus Capital Group, Inc. v. First Derivative Traders, 131 S. Ct. 2296 (2011) (No. 09-525), 2010 WL 4339892, at *8 ("The Commission has construed the term 'make' as providing for primary liability when a person 'creates' a misrepresentation either by writing or speaking it, providing false or misleading information for another to put into it, or allowing it to be attributed to him.").
6. *See* discussion *infra* Part I.
7. *See* discussion *infra* Parts I, II.
8. *See* discussion *infra* Part III.B.

it brings actions pursuant to Rule 10b-5(b) to the same extent that it restricts private plaintiffs.[9] Accordingly, the Commission—like a private plaintiff—must demonstrate that the "maker" of a material misstatement is a person with "ultimate authority" over the statement at issue, even if the Supreme Court did not intend this outcome.[10]

Like its mythological namesake, *Janus* looks both to the past and future. The decision embodies the past jurisprudential confusion surrounding Section 10(b) of the Securities Exchange Act[11] and its implementing regulation, Rule 10b-5, a single statute which provides for both private and public enforcement of securities fraud.[12] At the same time, *Janus* may provide the catalyst for a future transition from the burdens on public enforcement imposed by the decision to a "New" Rule 10b-5 for the Commission that avoids those limitations.

One must simultaneously look to the past and consider the future to properly understand *Janus*. Looking to the past, Part I will analyze securities law cases decided prior to *Janus* and argue that what underlies the Court's interpretations of Section 10(b) and Rule 10b-5 is its desire to curtail the expansion of an implied private right of action and reduce the perceived costs of frivolous private litigation. As explained in Part II, which analyzes the *Janus* decision itself, such considerations clearly motivated the interpretation of Rule 10b-5 in that case. As a policy matter, these considerations should not apply to public enforcement cases brought by the Commission.

---

9. *See* discussion *infra* Part III.B.

10. *See* discussion *infra* Part III.B.

11. Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b) (2012). Section 10(b) makes it:

> [U]nlawful for any person, directly or indirectly, . . . [t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Id.

12. 17 C.F.R. § 240.10b-5 (2013). Rule 10b-5 provides that:

> It shall be unlawful for any person, directly or indirectly, . . . (a) To employ any device, scheme, or artifice to defraud, (b) [t]o make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or (c) [t]o engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Id.

The holding in *Janus*, however, cannot be convincingly distinguished on the basis of who is bringing the action. Looking forward, Part III will thus explore the extent to which this inability to distinguish frustrates the Commission's public enforcement efforts by examining various legal theories, statutes, and rules that the Commission is either attempting to use or could possibly use to overcome the limitations imposed by *Janus*. Part III will also describe the potential drawbacks of each approach.

Finally, Part IV will propose a new rule that the Commission could issue that would adopt the "creation" standard exclusively for public enforcement actions. Such a rule would be consistent with the holding and policy considerations in *Janus*. Most importantly, it would create a framework that bolsters public enforcement while maintaining *Janus's* reduction in unwarranted private litigation. In this way, the proposed rule could contribute to the creation of more efficient capital markets, thereby fulfilling the Commission's Section 10(b) mandate to "prescribe as necessary or appropriate" rules and regulations that are "in the public interest."[13]

I. Looking to the Past: Cases before *Janus*

In *Janus*, the Supreme Court applied a restrictive interpretation of Rule 10b-5(b), which effectively narrowed the actors that could be held liable for securities fraud.[14] By exploring the Court's evolving interpretation of Section 10(b) and Rule 10b-5, Part I will place the *Janus* decision in its proper context. This Note argues that *Janus* was the next step in a progression of Supreme Court cases reacting to an antifraud jurisprudence the Court perceived as unduly expansive. More importantly, however, this history will show that these concerns were entirely founded on abuses of private litigation through the implied private right of action, rather than on the Commission's public enforcement actions. Acknowledging the Court's rationale is important in evaluating the various approaches the Commission may take to bypass *Janus*, whether the Commission brings actions under alternative statutes and regulations[15] or issues an entirely new rule.[16]

13. Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b).
14. *See* discussion *infra* Part II.B.
15. *See* discussion *infra* Part III.C.
16. *See* discussion *infra* Part IV.

A. *Two Distinct Periods: Before and After* Blue Chip

Supreme Court decisions prior to *Janus* reveal two distinct periods of securities fraud jurisprudence: the period of time before *Blue Chip Stamps v. Manor Drug Stores*[17] and the period of time afterward. Before *Blue Chip*, the Court focused on the federal securities laws' remedial purpose of investor protection,[18] which afforded a flexible, expansive approach to the securities laws.[19] Although the number of Supreme Court cases arising under Section 10(b) between 1946 and 1972 were few in number,[20] the Court's nonrestrictive approach furthered the agenda of both the Commission and private plaintiffs in securities fraud actions by broadly interpreting words and phrases like "security,"[21] "purchase,"[22] "in

17. 421 U.S. 723 (1975).

18. In *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 195 (1963), a case interpreting the antifraud provision of the Investment Advisors Act, the Supreme Court said that securities laws passed for the remedial purpose of combatting fraud should not be "construed . . . technically and restrictively, but flexibly to effectuate its remedial purposes." The Court's emphasis on the remedial purpose and the need for interpretive flexibility became the judicial leitmotiv in subsequent cases that expanded the scope of Section 10(b) and Rule 10b-5. *See infra* notes 19–26 and accompanying text.

19. *See, e.g.*, Superintendent of Ins. of N.Y. v. Bankers Life & Cas. Co., 404 U.S. 6, 12 (1971) ("Section 10(b) must be read flexibly, not technically and restrictively.").

20. 1946 was the year that *Kardon v. National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946), was decided, which was the first time a federal court recognized the implied private right of action under Section 10(b) and Rule 10b-5. 1972 was the year that the last pre-*Blue Chip* securities law case, *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128 (1972), was decided. During this period of time, the Supreme Court decided only four cases that directly interpreted Section 10(b), including *Affiliated Ute*. The other three were *Superintendent of Insurance of New York v. Bankers Life & Casualty Co.*, 404 U.S. 6 (1971), *SEC v. National Securities, Inc.*, 393 U.S. 453 (1969), and *Tcherepnin v. Knight*, 389 U.S. 332 (1967).

21. In *Tcherepnin*, the Court noted that the Exchange Act "clearly falls into the category of remedial legislation," and that protecting investors by requiring full disclosure is "[o]ne of its central purposes." 389 U.S. at 336. Accordingly, the Court explained that Congress did not adopt a "narrow or restrictive concept" of security, *id.* at 338, and that the term security "embodies a flexible rather than a static principle." *Id.* (quoting SEC v. W.J. Howey Co., 328 U.S. 293, 299 (1946)). Thus, the Court held that the financial instruments at issue in the case (withdrawable capital shares) were investment contracts, a category of securities that allowed the investors to bring their action under Rule 10b-5. *See id.* at 339.

22. In *SEC v. National Securities, Inc.*, 393 U.S. 453 (1969), the Court held that the word "purchase" encompassed the exchange by shareholders of their old stock for stock in a new company, explaining that the "broad antifraud purposes of the [Securities Exchange Act] and [Rule 10b-5] would clearly be furthered by their application to this type of situation." *Id.* at 467.

connection with,"[23] and "any."[24] While the Supreme Court never explicitly addressed the question of whether an implied private right of action actually existed, it appeared to assume as much.[25] In addition to strengthening the plaintiffs' bar, this assumption arguably reinforced public enforcement by supplementing the Commission's own efforts to expose wrongdoing and increase deterrence. Consistent with this expansive approach, courts also recognized "aiding and abetting" liability,[26] which allowed the Commission and private litigants to sue those who substantially assisted primary violators.

Then, in 1975, the Court's decision in *Blue Chip* set a new course for interpreting Section 10(b).[27] By acknowledging the costs associated with the uncertainty and abuse of securities litigation,[28] the Court introduced a new theme that would underlie its securities fraud jurisprudence for the next thirty years.

In *Blue Chip*, the Supreme Court first questioned the legitimacy of Rule 10b-5's implied private right of action.[29] Referring to what

---

23. *See Bankers Life*, 404 U.S. at 12. In *Bankers Life*, the Court once again enunciated its then-familiar refrain: "Section 10(b) must be read flexibly, not technically and restrictively." *Id.* According to the Court, this meant that Section 10(b) barred "deceptive devices and contrivances in the purchase or sale of securities whether conducted in the organized markets or face to face." *Id.* Here, the defendant misappropriated the proceeds from a private sale of securities, and the Court held that the deception was "in connection with" the sale of securities. *Id.* ("Since there was a 'sale' of a security and since fraud was used 'in connection with' it, there is redress under [Section] 10(b) . . . ."). Essentially, the court expanded the "in connection with" requirement, making it easier for plaintiffs to recover under Section 10(b).

24. *Affiliated Ute*, 406 U.S. at 151 ("These proscriptions, by statute and rule, are broad and, by repeated use of the word 'any,' are obviously meant to be inclusive."). In *Affiliated Ute*, the Court reiterated the necessity of interpreting securities legislation "flexibly" when the purpose of the legislation is to thwart securities fraud. *Id.* One of the issues in *Affiliated Ute* was whether the plaintiffs must demonstrate reliance on material misstatements or omissions in order to succeed in an action that alleged a violation of Rule 10b-5. *Id.* at 152. Although the Court of Appeals had held that demonstrating reliance was necessary, the Supreme Court noted that it "[did] not read Rule 10b-5 so restrictively." *Id.* Accordingly, the Court held that in a case "involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery." *Id.* at 153.

25. Although the Court did not address the implied private right of action directly, both *Tcherepnin* and *Affiliated Ute* were actions brought by private plaintiffs pursuant to Section 10(b) and Rule 10b-5's implied private right of action. *See supra* notes 21 & 24.

26. *See, e.g.*, 4 Thomas Lee Hazen, Treatise on the Law of Securities Regulation § 12.25[1] (6th ed. 2009) ("For years, the district and circuit courts assumed, without really ever questioning, that private plaintiffs could bring securities fraud actions against aiders and abettors. This was the generally accepted law notwithstanding the absence of an express right of action.").

27. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975).

28. *Id.* at 739–48 (discussing the various costs associated with vexatious law suits).

29. *Id.* at 737. Milton Freeman, one of the drafters of Rule 10b-5, frequently insisted that the Commission staff never contemplated a private right of action when they wrote the Rule. Milton V. Freeman, *Foreward*, 61 Fordham L. Rev. S1, S2 (1993) ("Obviously neither I, nor the Commission that promulgated the Rule, had any such idea [that the Rule would provide

the Court considered a scant legislative history, Justice Rehnquist described the implied action as "a judicial oak which has grown from little more than a legislative acorn."[30] Rather than eliminating the implied private right of action altogether, however, the Court would prospectively impose a narrower, more restrictive interpretation.[31] Whereas the Court's earlier decisions endorsed a flexible approach that was guided by the remedial purpose of investor protection,[32] after *Blue Chip* the Court would invoke a rigid textualism to exclude entire categories of defendants and potential plaintiffs from the ambit of Rule 10b-5 in cases involving private litigants.[33]

In its post-*Blue Chip* decisions, the Court has gradually chipped away at the expansive interpretation of Section 10(b) established by earlier decisions, justifying its narrow approach by strictly construing the language of the statute.[34] In fact, a year after *Blue Chip*, the Court articulated an important limitation on the scope of Rule 10b-5.[35] It noted that the Rule—which the Commission issued pursuant to its rulemaking authority—could be no broader than Section 10(b), which Congress passed.[36] This is important because any Rule issued by the Commission pursuant to Section 10(b), such as the one proposed in Part IV, cannot exceed the bounds established by the statutory language.[37]

---

the basis for a private law suit] when the Rule was adopted."). However, only a few years after Rule 10b-5 was promulgated, a federal district court judge recognized such a right. *See* Kardon v. Nat'l Gypsum Co., 69 F. Supp. 512, 513–14 (E.D. Pa. 1946). Because it perceives private litigation as a necessary supplement to its own efforts, the Commission has consistently supported the private right of action along with other measures to expand the rights of private litigants. *See, e.g.*, *Securities Litigation Abuses: Hearing Before the Subcomm. on Sec. of the S. Comm. on Banking, Hous. & Urban Affairs*, 105th Cong. (1997) (statement of Arthur Levitt, Chairman, U.S. Securities and Exchange Commission), *available at* http://www.banking.senate.gov/97_07hrg/072497/witness/levitt.htm ("The Commission has long maintained that private actions provide valuable and necessary additional deterrence against securities fraud, thereby supplementing the Commission's own enforcement activities.").

30. *Blue Chip*, 421 U.S. at 737.

31. *See, e.g.*, Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976) (holding that private actions under Section 10(b) and Rule 10b-5 require a showing of scienter, rather than mere negligence, as argued in the Commission's amicus curiae brief).

32. *See supra* notes 18–26 and accompanying text.

33. *See, e.g.*, *infra* Part I.B. However, not all decisions during the period following *Blue Chip* were unfavorable to plaintiffs. For instance, in *Basic Inc. v. Levinson*, 485 U.S. 224, 245–47 (1988), the Court adopted the fraud-on-the-market theory, which created a presumption of reliance in suits brought pursuant to Section 10(b) and Rule 10b-5 when the securities at issue are traded in a liquid market. This presumption obviously makes it easier for plaintiffs to bring lawsuits.

34. *See infra* Part I.B.

35. *Hochfelder*, 425 U.S. at 214.

36. *Id.* ("Thus, despite the broad view of the Rule advanced by the Commission in this case, its scope cannot exceed the power granted the Commission by Congress under § 10(b).").

37. *See infra* Part IV.

B. Secondary Liability and the Road to Janus

Since *Blue Chip*, the Supreme Court has effectively eliminated entire categories of defendants by limiting plaintiffs' ability to sue secondary actors under Section 10(b) and Rule 10b-5. For instance, in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*,[38] the Court held that a private plaintiff may not maintain an aiding and abetting action against secondary actors under Section 10(b).[39] The Court explained that the language of the statute "prohibits only the making of a material misstatement (or omission) or the commission of a manipulative act,"[40] and that nothing in the text of Section 10(b) imposed liability on those who aid and abet primary violators.[41]

---

38. 511 U.S. 164 (1994).

39. *Id.* at 191. The dissenting opinion pointed out that the majority's holding similarly affected the Commission's ability to pursue aiders and abettors. *Id.* at 200 (Stevens, J., dissenting) ("The majority leaves little doubt that the Exchange Act does not even permit the SEC to pursue aiders and abettors in civil enforcement actions under § 10(b) and Rule 10b-5."). However, Congress made clear that the Commission could bring actions against aiders and abettors by explicitly granting the Commission this authority when Congress passed the Private Securities Litigation Reform Act of 1995. *See* Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, § 104, 109 Stat. 737, 757 (1995) (codified as amended at 15 U.S.C. § 78t(e) (2012)).

40. *Central Bank*, 511 U.S. at 177; *see also id.* at 173 ("We have refused to allow 10b-5 challenges to conduct not prohibited by the text of the statute."); *id.* at 175 ("Our consideration of statutory duties, especially in cases interpreting § 10(b), establishes that the statutory text controls the definition of conduct covered by § 10(b)."); *id.* at 177 ("It is inconsistent with settled methodology in § 10(b) cases to extend liability beyond the scope of conduct prohibited by the statutory text.").

41. *Id.* at 177 ("[T]he text of the 1934 Act does not itself reach those who aid and abet a § 10(b) violation."). The Court in *Central Bank* also outlined the analytical steps that guide its decisions in cases interpreting implied causes of action under Section 10(b). First, the Court reviews the text of the statute. *See id.* at 178. If the text resolves the question, there is no need to inquire further. However, when the text does not resolve the question, the Court attempts to infer how the 1934 Congress would have resolved the question if the Rule 10b-5 private right of action had been included in the Exchange Act. *Id.* To do this, the Court relies on the express causes of action in other provisions of the Exchange Act, because Congress "likely would have designed it in a manner similar to the other private rights of action in the securities Acts." *Id.* at 178 (citation omitted). Although the Court in *Central Bank* found the text of the statute sufficiently clear to establish that no liability extended to aiders and abettors, the Court proceeded to demonstrate that, even under this second layer of analysis, there would be no aiding and abetting liability. *Id.* at 179 ("From the fact that Congress did not attach private aiding and abetting liability to any of the express causes of action in the securities Acts, we can infer that Congress likely would not have attached aiding and abetting liability to § 10(b) had it provided a private § 10(b) cause of action."). This is because, according to the Court, none of the express causes of action impose further liability on those who aid and abet the primary violation. *Id.* at 180 ("Here, it would be just as anomalous to impute to Congress an intention in effect to expand the defendant class for 10b-5 actions beyond the bounds delineated for comparable express causes of action.").

While the Court noted that "[p]olicy considerations cannot override [its] interpretation of the text and structure of the Act,"[42] the Court did list many policy concerns underlying its interpretation. In general, the Court voiced its concern that the costs associated with secondary liability for aiders and abettors "may disserve the goals of fair dealing and efficiency in the securities markets."[43] The need for certainty in business transactions, according to the Court, militated against the expansion of liability to cover aiders and abettors.[44] The Court also pointed out that the indeterminate rules for deciding aiding and abetting liability led to settlements in suits that might otherwise be meritless.[45] This, in turn, encouraged strike suits and other vexatious litigation to extract settlement fees.[46] According to the Court, the "ripple effect" of costs associated with this uncertainty and excessive litigation is that newer and smaller companies would be unable to retain advice from professionals who fear that the company may not survive.[47] The professional would then be the scapegoat after whom the frustrated investors go to recover their losses.[48] Additionally, the costs incurred by professionals to hedge against the risk of vexatious litigation may be passed on to their client companies, and in turn passed on to innocent investors.[49] As discussed later, this same concern for abusive private litigation lies beneath the Court's interpretive approach in *Janus*.[50]

While *Central Bank* eliminated aiding and abetting liability, that decision indicated that, when secondary actors engage in primary violations, they may be held liable under Section 10(b).[51] In *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*,[52] the Supreme Court again narrowed the scope of liability for secondary actors.

The issue before the Court in *Stoneridge* was whether the investors in a company that was allegedly engaging in various accounting frauds could also bring an action against the company's suppliers

42. *Id.* at 188.
43. *Id.*
44. *See id.* at 188–89.
45. *See id.* at 189.
46. *See id.*
47. *Id.*
48. *Id.*
49. *Id.*
50. *See* discussion *infra* Part II.B.
51. *Central Bank*, 511 U.S. at 191 ("The absence of § 10(b) aiding and abetting liability does not mean that secondary actors in the securities markets are always free from liability under the securities Acts. Any person or entity, including a lawyer, accountant, or bank, who employs a manipulative device or makes a material misstatement (or omission) on which a purchaser or seller of securities relies may be liable as a primary violator under 10b-5, assuming *all* of the requirements for primary liability under Rule 10b-5 are met.").
52. 552 U.S. 148 (2008).

who, by entering into bogus transactions with the company, helped the company inflate its revenues and falsely capitalize certain advertising expenses.[53] The plaintiffs in *Stoneridge* argued that the "causal link" between the suppliers' assistance and the creation of the false financial statements was sufficient to presume reliance.[54]

The Court, however, disagreed. In its decision, the Court noted that whether liability extends to a secondary actor depends on whether the plaintiff establishes reliance.[55] Although courts presume reliance in two situations,[56] the Court found that neither presumption applied in *Stoneridge*.[57] Additionally, the secondary actors had no actual knowledge of the deceptive acts.[58] As a result, the Court held that the plaintiff-investors could not demonstrate reliance "except in an indirect chain that [the Court found] too remote for liability."[59] While the Court noted that reliance and causation were closely related, in *Stoneridge* the deceptive acts were "too remote to satisfy the requirement of reliance."[60] Anticipating its "ultimate authority" language in *Janus*, the Court wrote that "nothing [the suppliers] did made it *necessary or inevitable* for [the company] to record the transactions as it did," and thus reliance could not be shown.[61]

Although the Court grounded its decision in *Stoneridge* in the text of Section 10(b), it managed once again to spend the largest portion of the opinion discussing the statute's legislative history and the various policy considerations supporting its interpretation. As in *Central Bank*, these policy considerations included concerns about extending the coverage of Section 10(b) into the realm of ordinary business and the effect of frivolous lawsuits brought by private plaintiffs on the costs of raising capital.[62]

---

53. *See Stoneridge*, 552 U.S. at 153–56. Specifically, the Court framed the issue as whether "an injured investor may rely upon § 10(b) to recover from a party that neither makes a public misstatement nor violates a duty to disclose but does participate in a scheme to violate § 10(b)." *Id.* at 156.

54. *Id.* at 160.

55. *Id.* at 157–59 ("Reliance by the plaintiff upon the defendant's deceptive acts is an essential element of the § 10(b) private cause of action.").

56. Reliance is presumed first when one has a duty to disclose information but fails to do so and, second, under the fraud-on-the-market theory. *Id.* Under the fraud-on-the-market theory, when statements are made publicly and the company's securities trade in an active market, it is presumed that the public statement is reflected in the price of the security and is therefore relied on. *Id.*

57. According to the Court, the suppliers in *Stoneridge* had no duty to disclose material information, and their acts, even if deceptive, were never communicated to the public. *Id.*

58. *Id.*

59. *Id.*

60. *Id.* at 161.

61. *Id.* (emphasis added).

62. *Id.* at 163–64.

Central Bank and *Stoneridge* are important for understanding *Janus* because, as in *Janus*, the Court's concern for preventing the expansion of the implied private right of action—and its concomitant costs—underlay its narrow approach to Rule 10b-5. Neither *Central Bank* nor *Stoneridge*, however, affected the Commission's ability to prosecute securities fraud. After *Central Bank*, Congress passed a law as part of the Private Securities Litigation Reform Act of 1995 that explicitly allowed the Commission to pursue aiders and abettors.[63] So, even if *Central Bank*'s rejection of aiding and abetting liability initially applied to the Commission prior to 1995, it no longer does. No action to preserve the Commission's powers was needed in the wake of *Stoneridge* because that decision was based on a failure to demonstrate reliance, and the Commission does not have to prove reliance in actions it brings pursuant to Section 10(b).[64]

II. THE *JANUS* DECISION

In *Janus*, the Court once again limited the class of persons that can be sued for securities fraud under Section 10(b) and Rule 10b-5. Specifically, the Court interpreted Rule 10b-5 to mean that only a person with "ultimate authority" over a statement can be the "maker" of the statement.[65] This further limited plaintiffs' ability to bring actions against secondary actors, even if those actors provided substantial assistance in the creation of the materially misleading statement. This is problematic for the Commission because it also relies on Rule 10b-5 when bringing actions under Section 10(b), and the Court did not distinguish its holding on the basis of the plaintiff's identity.

A. *The Facts of* Janus

Janus involved material misstatements allegedly made by Janus Investment Fund ("the Fund") in its mutual fund prospectus.[66] The Fund was advised by Janus Capital Management LLC (JCM), which was a wholly owned subsidiary of Janus Capital Group, Inc. (JCG), a publicly traded company.[67] The plaintiffs in *Janus*, First Derivative

63. Pub. L. No. 104-67, § 104, 109 Stat. 737, 757 (codified as amended at 15 U.S.C. 78t(e) (2012)).
64. 4 HAZEN, *supra* note 26, at § 12.10[1][A] ("Reliance is an element of a private suit under Rule 10b-5, but not in enforcement actions brought by the government.").
65. Janus Capital Grp., Inc. v. First Derivative Traders, 131 S. Ct. 2296, 2302 (2011).
66. *Id.* at 2299.
67. *Id.*

Traders, were investors in the parent company, JCG.[68] In the investment funds industry, it is common for a fund to be advised and operated by a separate legal entity. In this case, that separate legal entity was JCM. Additionally, JCM was JCG's primary operating company, and the two entities shared many of the same executives.[69]

First Derivative Traders brought a claim under Section 10(b) and Rule 10b-5 against JCG and JCM—but not the Fund—for the material misstatements contained in the Fund's prospectus. First Derivate Traders based their suit on the theory that JCG and JCM, by actually *creating* the statements filed by the Fund, also "made" the alleged material misstatements.[70] Importantly, the plaintiffs—who were not investors in the Fund—could not sue the Fund itself, which was the entity the Court found to have "ultimate authority" over the misleading statements.

B. The Janus *Opinion*

The *Janus* decision, written by Justice Thomas, framed the issue as whether JCM could be held liable in a private action under Rule 10b-5 for a false statement included in the Fund's prospectuses.[71] To answer the question, the Court looked first to the text—a familiar interpretive procedure.[72] In prior cases dealing with secondary liability, however, the statute—rather than Rule 10b-5— had driven the Court's decisions.[73] In *Janus*, however, the Court scrutinized the text of Rule 10b-5 itself.[74]

As described by the Court, Rule 10b-5 makes it "unlawful for 'any person, directly or indirectly, . . . [t]o make any untrue statement of

68. *Id.* at 2300.

69. *See* In re Mut. Funds Inv. Litig., 566 F.3d 111, 115 (4th Cir. 2009), *overruled by Janus*, 131 S. Ct. 2296.

70. *Janus*, 131 S. Ct. at 2300.

71. *Id.* at 2299 ("This case requires us to determine whether Janus Capital Management LLC (JCM), a mutual fund investment adviser, can be held liable in a private action under Securities and Exchange Commission (SEC) Rule 10b-5 for false statements included in its client mutual funds' prospectuses.").

72. *See supra* Part I.

73. For instance, in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, the Court began its analysis of "the scope of conduct prohibited by § 10(b)" by announcing that "the text of the statute controls [the Court's] decision." 511 U.S. 164, 173 (1994). Similarly, in *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, the Court said that the scope of actionable conduct is "delimited" by the text of the statute: "Rule 10b-5 encompasses only conduct already prohibited by § 10(b)." 552 U.S. 148, 157 (2007).

74. *Janus*, 131 S. Ct. at 2301–03.

a material fact' in connection with the purchase or sale of securities."[75] From this language, the Court held that JCM could only be liable if it had "made" the material misstatements found in the prospectus.[76] The Court held that JCM had not.[77]

1. The Court's Narrow Interpretation of "Make" and the Ultimate Authority Requirement

In its decision, the Court once again acknowledged its hesitation to expand a private right of action created by the courts, rather than by Congress.[78] Thus, in interpreting the word "make," the Court resolved to "give 'narrow dimensions . . . to a right of action Congress did not authorize when it first enacted the statute and did not expand when it revisited the law.'"[79] Relying on definitions found in both the Oxford and Webster's dictionaries, Justice Thomas explained the meaning of the word "make" as it was understood in the 1930s,[80] clarifying that "to make" in rule 10b-5 means roughly the same thing as "to state."[81]

More crucially, the Court held that "[f]or purposes of Rule 10b-5, the maker of a statement is the person or entity with *ultimate authority* over the statement, including its content and whether and how to communicate it."[82] According to the Court, one could not have control without ultimate authority, and, when control was absent, "a person or entity can merely suggest what to say, not 'make' a statement in its own right."[83] Therefore, even if one prepares or publishes a statement *on behalf of* the primary actor, only the primary actor can be the maker of the statement.[84] To illustrate the rule, the Court analogized to the relationship between a speaker and speechwriter.[85] Even though the speechwriter drafts the speech, the speaker controls the content ultimately contained in

---

75. *Janus*, 131 S. Ct. at 2301 (footnote omitted) (quoting 17 CFR § 240.10b-5(b) (2010)).
76. *Id.*
77. *Id.*
78. *Id.* at 2302 ("[C]oncerns with the judicial creation of a private cause of action caution against its expansion.") (quoting *Stoneridge*, 552 U.S. at 165).
79. *Id.* (quoting *Stoneridge*, 552 U.S. at 167).
80. This is notable considering that Rule 10b-5, which contains the word "make," was not passed until the 1940s.
81. *Janus*, 131 S. Ct. at 2302 ("The phrase at issue in Rule 10b-5, '[t]o make any . . . statement,' is thus the approximate equivalent of 'to state.'").
82. *Id.* (emphasis added).
83. *Id.*
84. *See id.*
85. *Id.*

the speech.[86] Notably, the Court indicated that a statement attributed to a party, either explicitly or implicitly, is ordinarily "strong evidence" that the statement was "made by—and only by—the party to whom it is attributed."[87]

2. Justification for the "Ultimate Authority" Requirement through *Central Bank* and *Stoneridge*

After defining the word "make," the Court then explained how imposing an "ultimate authority" requirement was consistent with its prior decisions. The Court stated that, in *Central Bank*, it had "held that Rule 10b-5's private right of action does not include suits against aiders and abettors."[88] According to the Court, if "make" were read more broadly than the meaning imposed by the "ultimate authority" standard, then the category of primary violators would expand to include aiders and abettors, which would "substantially undermine *Central Bank*."[89]

The Court stated that its interpretation in *Janus* was also supported by *Stoneridge*, which had emphasized that "nothing [the defendants] did made it *necessary or inevitable* for [the company] to record the transactions as it did."[90] Whenever an entity lacked the ultimate authority over a statement's content and the manner in which that content would be communicated, then it was neither "necessary [nor] inevitable" that the statement would be materially misleading.[91] In *Stoneridge*, the Court had found the conduct by secondary actors too remote to create reliance because, among other reasons, the conduct did not necessarily and inevitably lead to fraudulent financial statements.[92]

By citing *Stoneridge*, the *Janus* Court effectively folded *Stoneridge*'s reliance requirement into the word "make." Thus, one possible reading of *Janus* is that (1) plaintiffs can only bring a Rule 10b-5 action when they can demonstrate reliance, (2) plaintiffs can never demonstrate reliance when it is not necessary or inevitable that a particular statement will be made, (3) the making of a statement is

---

86. *Id.*

87. *Id.* The degree to which this statement can be used by the Commission to overcome the restrictive language of *Janus* is explored *infra* Part III.

88. *Id.* (citing Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 511 U.S. 164, 180 (1994)).

89. *Id.*

90. *Id.* at 2303 (emphasis added) (quoting Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc., 552 U.S. 148, 161 (2007)).

91. *Id.*

92. *Stoneridge*, 552 U.S. at 159–61.

never necessary or inevitable when the person that created the statement lacks ultimate authority, and (4) therefore, there will never be any reliance when there is no ultimate authority. Reliance, of course, is an element that private plaintiffs—but not the Commission—must prove in Rule 10b-5 actions.[93] By merging its understanding of reliance into the definition of "make," however, the Court has—perhaps inadvertently—allowed its concern for demonstrating reliance in private suits to limit public enforcement by the Commission.

The Court concluded its interpretation of the word "make" by reiterating that the Court's holding "accord[ed] with the narrow scope that [it] must give the *implied private right of action*."[94] The Court recognized that the existence of the private right is settled, but insisted that it would "not expand liability beyond the person or entity that ultimately has authority over a false statement."[95]

3. The Court's Holding

Having established its "ultimate authority" interpretation of the word "make," the Court held that "JCM did not 'make' any of the statements in the Janus Investment Fund prospectuses."[96] Rather, only Janus Investment Fund made the statements, because "[o]nly Janus Investment Fund—not JCM—bears the statutory obligation to file the prospectuses with the SEC."[97] Apparently, according to the Court's reasoning the sole entity with "ultimate authority" is the entity with the "statutory obligation" to file the prospectus, which means that such an entity is the only one that can "make" a statement for the purposes of misstatement liability under Rule 10b-5.

The Court anticipated scenarios that could dim this bright-line rule by highlighting facts that were *not* present in *Janus*. For instance, the Court noted that in *Janus* there was "no allegation that JCM in fact filed the prospectuses and falsely attributed them to Janus Investment Fund."[98] The Court also stated that its application relied on the fact that nothing "on the face of the prospectuses indicate[d] that any statements therein came from JCM rather than Janus Investment Fund, a legally independent entity with its own

93. 4 HAZEN, *supra* note 26, at § 12.10[1][A] ("Reliance is an element of a private suit under Rule 10b-5, but not in enforcement actions brought by the government.").
94. *Janus*, 131 S. Ct. at 2303 (emphasis added) (citing *Stoneridge*, 552 U.S. at 167).
95. *Id.*
96. *Id.* at 2304 (majority opinion).
97. *Id.*
98. *Id.* at 2305.

board of trustees."[99] The Court's reliance on the absence of any attribution seems to leave open the possibility of holding a secondary actor liable for misstatements, even when it does not have "ultimate authority" over the content of the statement, if the particular portion of the statement is explicitly attributed to it. In a footnote, the Court wrote that it is not necessary to "define precisely what it means to communicate a 'made' statement indirectly, because none of the statements in the prospectuses were attributed, explicitly or implicitly, to JCM. Without attribution, there is no indication that Janus Investment Fund was quoting or otherwise repeating a statement originally 'made' by JCM."[100]

III. Looking Forward: The Effect of *Janus* on the Commission's Enforcement Capabilities

Both private plaintiffs and the Commission use Rule 10b-5. It is not obvious, therefore, why the Court's justification for its definition of "make"—a policy of narrowly construing the scope of implied *private* rights of action—should apply equally to Commission actions that are explicitly authorized. Although the Court did not address the consequences of this problem, the dissent noted that "under the majority's rule it seems unlikely that the SEC itself . . . could . . . pursue primary violators who 'make' false statements or . . . prosecute aiders and abettors to securities violations."[101]

A. *Cases that* Janus *Does Not Appear to Affect*

Although the Court in *Janus* held that the "maker" of a statement must have "ultimate authority" over its contents, it added that "attribution within a statement . . . is strong evidence that a statement was made by . . . the party to whom it is attributed."[102] Not surprisingly, much of the post-*Janus* case law has analyzed such scenarios, particularly situations in which written statements are issued in the name of a corporation or some other business entity but contain signatures by individuals in either their official or personal capacity. To date, courts have interpreted *Janus* to mean that, when individual corporate officers sign company documents that are filed with

99. *Id.* (footnote omitted).
100. *Id.* at 2305 n.11 (citation omitted).
101. *Id.* at 2310 (Breyer, J., dissenting).
102. *Id.* at 2302.

the Commission, these officers can be primarily liable for statements contained within those documents.[103]

Courts have also held that individuals can be primarily liable for documents other than SEC filings that they sign. For instance, in one case the court held that the defendant was a "maker" of statements contained in an email that the defendant sent to investors.[104] In another, a court held a complaint sufficient to survive summary judgment where it alleged that the defendant—the chief executive officer of a mortgage lender and issuer of mortgage-backed securities—had signed and submitted an application for participation in a federal securitization program which falsely represented that the

103. *See, e.g.*, SEC v. Brown, 878 F. Supp. 2d 109, 115–16 (D.D.C. 2012) (denying defendant's motion for summary judgment because genuine issues of material fact existed as to whether, under *Janus*, defendant CFO was a maker of statements in SEC periodic reports that she signed); SEC v. Carter, No. 10 C 6145, 2011 WL 5980966, at *1–3 (N.D. Ill. Nov. 28, 2011) (pointing out that a CEO's electronic signature on Form 8-K, which was accompanied by the press releases that were alleged to contain material misstatements, indicated that the statements were "made" by the CEO defendant); SEC v. Mercury Interactive, LLC, No. 5:07–cv–02822–WHA, 2011 WL 5871020, at *2 (N.D. Cal. Nov. 22, 2011) (finding, for purposes of motion to dismiss, that, under *Janus*, defendant was maker of statements in proxy statements where she signed a notice to shareholders on the first page of the proxy package; she was not maker of statements in Forms 10-K and 10-Q that she did not sign); SEC v. Das, No. 8:10CV102, 2011 WL 4375787, at *6 (D. Neb. Sept. 20, 2011) (holding, under *Janus*, that defendant CFOs were makers of statements contained in Forms 10-K and 10-Q on which their signatures and certifications appeared); *see also* SEC v. Daifotis, No. C 11–00137 WHA, 2011 WL 3295139, at *3 (N.D. Cal. Aug. 1, 2011) (noting concession by defendant that, under *Janus*, he was maker of statements in registration statement that he signed). In addition to cases brought by the Commission, courts have held that, in cases brought by private plaintiffs, an officer that signs a document filed with the Commission can be considered a "maker" of the statements contained in the document. *See, e.g.*, *In re* Smith Barney Transfer Agent Litig., 884 F. Supp. 2d 152, 163–65 (S.D.N.Y. 2012) (finding, under *Janus*, that defendant officer was maker of statement in SEC filings that he signed); *In re* Stillwater Capital Partners Inc. Litig., 858 F. Supp. 2d 277, 287–88 (S.D.N.Y. 2012) (finding, under *Janus*, that defendant president was maker of statements in proxy statement and SEC filings that he signed); *In re* Pfizer Inc. Sec. Litig., Nos. 04 Civ. 9866(LTS)(HBP), 05 MD 1688(LTS), 2012 WL 983548, at *4 & n.3 (S.D.N.Y. Mar. 22, 2012) (finding, under *Janus*, that defendant corporate officer was maker of statements in SEC filings that he signed); City of St. Clair Shores Gen. Emps.' Ret. Sys. v. Lender Processing Servs., Inc., No. 3:10–cv–1073–J–32JBT, 2012 WL 1080953, at *3 (M.D. Fla. Mar. 20, 2012) (finding, for purposes of a motion to dismiss, that defendant corporate officers, under *Janus*, could be considered makers of statement in SEC filings that they certified under Sarbanes-Oxley); City of Roseville Emps.' Ret. Sys. v. Energy Solutions, Inc., 814 F. Supp. 2d 395, 416–18 (S.D.N.Y. 2011) (finding, under *Janus*, that defendants were makers of statements in registration statements that they signed); *In re* Merck & Co., Inc. Sec., Derivative, & ERISA Litig., MDL No. 1658 (SRC), Civil Action Nos. 05–1151 (SRC), 05–2367(SRC), 2011 WL 3444199, at *25 (D.N.J. Aug. 8, 2011) (holding that, by signing the documents in his capacity as a company executive, the defendant "made the statements pursuant to his responsibility and authority to act as an agent of [the company], not as in *Janus,* on behalf of some separate and independent entity.").

104. Red River Res., Inc. v. Mariner Sys., Inc., No. CV 11–02589–PHX–FJM, 2012 WL 2507517, at *6 (D. Ariz. June 29, 2012).

underlying loans would be eligible for Federal Housing Authority insurance.[105]

Courts have also generally accepted the argument that individuals should be considered "makers" of statements that are specifically attributed to them even if the statements are contained within a larger statement "made," according to *Janus*, by another entity. For example, courts have held that, when larger documents—such as company press releases, offering documents, news articles, and advertisements—contain written statements specifically attributed to individuals, those individuals can be "makers" of those statements.[106]

At least two cases have addressed the issue of whether an underwriter can be held primarily liable for misstatements contained within a document on which the underwriter's name conspicuously appears.[107] Both cases suggest that the prominent display of an underwriter's name in the offering materials may be sufficient for the plaintiff in a suit against the underwriters to withstand a motion for summary judgment.[108] Of course, even when attribution is sufficient

105. SEC v. Radius Capital Corp., No. 2:11–cv–116–FtM–29DNF, 2012 WL 695668, at *4–5 (M.D. Fla. Mar. 1, 2012); *see also In re* Flannery, SEC Release No. 438, 2011 WL 5130058, at *35, *46 (ALJ Oct. 28, 2011) (initial decision) (finding that *Janus* applies to claims under Section 17(a) of the Securities Act, and that defendant, under *Janus*, had ultimate authority over— and therefore was maker of—statements in letter that he wrote, signed, and directed be sent to investors).

106. *See* SEC v. Daifotis, 874 F. Supp. 2d 870, 877 (N.D. Cal. 2012) (denying defendant's motion for summary judgment and holding as a triable issue whether defendant, under *Janus*, was maker of statements specifically attributed to him in company advertisement); *In re* Allstate Life Ins. Co. Litig., Lead Case No. CV–09–8162–PCT–GMS, No. CV–09–8174–PCT–GMS, 2012 WL 1900560, at *4–5 (D. Ariz. May 24, 2012) (denying defendants' motion to dismiss and holding that defendants, under *Janus*, could be makers of statements that were attributed to them in Official Statements for municipal offerings); City of St. Clair Shores Gen. Emps.' Ret. Sys., 2012 WL 1080953, at *3 (finding, for purposes of defendant's motion to dismiss, that defendant corporate officers, under *Janus*, could be considered makers of statements that were attributed to them in company press releases and news articles); Lopes v. Viera, No. 1:06–CV–01243 JLT, 2012 WL 691665, at *6 (E.D. Cal. Mar. 2, 2012) (finding, for purposes of a motion in limine, that defendant organizer of company, under *Janus*, could be maker of financial information in offering document where document stated the financial information had been provided to the company by him); *Daifotis*, 2011 WL 3295139, at *3 (detailing concession, by defendant, that, under *Janus*, he was maker under advertisement that included his picture but did not otherwise attribute statements to him).

107. *See In re* Nat'l Century Fin. Enters., Inc. Inv. Litig., 846 F. Supp. 2d 828, 861 (S.D. Ohio 2012); *In re* Allstate Life Ins. Co. Litig., Nos. CV–09–8162–PCT–GMS, CV–09–8174–PCT–GMS, 2012 WL 176497, at *5 (D. Ariz. Jan. 23, 2012).

108. *See In re* Nat'l Century Fin. Enters., Inc. Inv. Litig., 846 F. Supp. at 861 (finding that it was "a triable issue as to whether [the underwriter could] be held liable for the misrepresentations in the [offering materials]" when the underwriter's name was "prominently" displayed on the front pages of the offering materials and the underwriter was "specifically designated" to make representations about the securities); *In re* Allstate Life Ins. Co. Litig., 2012 WL 176497, at *5 (holding that, when underwriters' names were displayed in bold and

at pre-trial stages of litigation, mere attribution may still be insufficient to satisfy the ultimate authority definition.

B. Can the Holding in Janus *Be Limited to Private Suits?*

One obvious way the Commission can bypass *Janus* is to argue that the holding applies only to private actions. In its opinion in that case, the Court framed the issue by stating that "[t]his case requires us to determine whether . . . a mutual fund investment adviser can be held liable in a *private action* under . . . Rule 10b-5."[109] The Court was also "mindful" of giving the word "make" a "narrow" interpretation because of its concerns about expanding a *private* right of action that was created by the courts rather than Congress.[110]

Additionally, in its extratextual justification, the Court repeatedly focused its discussion on continuing concerns about the scope of private actions brought under Rule 10b-5. For instance, in discussing *Janus*'s lineage from recent precedent, the Court described *Central Bank* as a case in which it "held that Rule 10b-5's *private right of action* does not include suits against aiders and abettors."[111] The Court then noted that a "broader reading of make"—one that expanded the class of plaintiffs in private actions—would "substantially undermine *Central Bank*," presumably because it would allow private plaintiffs to bring suits in situations otherwise barred by *Central Bank*.[112] The Court noted that, despite its ruling in *Central Bank*, the Commission can still bring suits against aiders and abettors.[113] So, when the Court discusses a holding that would undermine *Central Bank*, it is obviously not speaking of an interpretation that would undermine *Central Bank* as it pertains to enforcement actions brought by the Commission.

Finally, the Court concluded its legal analysis by discussing *Stoneridge*—a case that only affects private plaintiffs—and reiterating the "narrow scope that [the Court] must give the implied private right

---

in a prominent position on certain offering materials, the plaintiffs had adequately alleged that the underwriters made the material misstatements).

109. Janus Capital Grp., Inc. v. First Derivative Traders, 131 S. Ct. 2296, 2299 (2011) (emphasis added); *see also id.* at 2301 ("We granted certiorari to address whether JCM can be held liable in a *private action* under Rule 10b-5 for false statements included in Janus Investment Fund's prospectuses." (emphasis added)).

110. *Id.* at 2302.

111. *Id.* (emphasis added) (citing Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 511 U.S. 164, 180 (1994)).

112. *Id.*

113. *Id.* ("Such [aiding and abetting] suits may be brought by the SEC.").

of action."[114] Clearly, it is the Court's concern for limiting private actions that drove its decision in *Janus*, not a desire to subdue public enforcement.

An interpretation that applies *Janus* differently depending on the plaintiff's identity is also consistent with the policy concerns the Court has enunciated in its decisions since *Blue Chip*. As described in Part I, the Court's narrow approach to Section 10(b) grew out of a desire to quell what it considered frivolous lawsuits being brought by private plaintiffs: because the Court doubted the legitimacy of the private right of action, going forward it would no longer expand it.[115] *Janus* obviously embodies this approach insofar as the decision limits private actions. However, the Court has never enunciated a similar approach to actions brought by the Commission, which are expressly created under Section 10(b) and Rule 10b-5. Therefore, cabining *Janus* as a decision concerning only private actions would not conflict with the Court's primary concern of restricting private actions.

Although it may be clear that *Janus* was motivated by a concern for private actions, the simplicity of distinguishing the *Janus* decision on the basis of the plaintiff's identity belies an obvious impediment: the Court based its entire decision on the word "make." Unless the Court adopts the above approach and explicitly differentiates interpretations depending on who is bringing the action, the language and reasoning in *Janus* do not readily support an argument limiting its holding to private litigation.[116] Therefore, it is not likely that lower courts would be willing to widen the narrow path set by the Supreme Court. Additionally, it is not clear how the Court itself could persuasively escape the strictures of *Janus* without expressly overruling it. Thus, going forward, it is likely that the Commission will have to find other ways to circumvent *Janus* besides arguing that the decision does not apply to public enforcement actions brought under Rule 10b-5.

---

114. *Id.* at 2303 (citing Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc., 552 U.S. 148, 167 (2007)).

115. *See supra* Part I.A.

116. At least one article assumes that *Janus* may not apply to actions brought by the Commission and contends that the Commission's interpretation of "make" is "entitled to substantial judicial deference in future enforcement actions" because it "would withstand *Chevron*-style analysis." *See* Matthew P. Wynne, Note, *Rule 10b-5(b) Enforcement Actions in Light of* Janus*: Making the Case for Agency Deference*, 81 Fordham L. Rev. 2111, 2111 (2013). As explained above in Part III.B, *Janus* was written in a way that forecloses any interpretation distinguishing its application on the basis of the plaintiff's identity. Whether *Janus* might apply to actions brought by the Commission is not an open question to which *Chevron* deference may apply. Accordingly, the Commission has not pursued this argument.

C. Actions Brought Under Alternative Statutes and Rules

The Commission can possibly bypass the limitations imposed by *Janus* by bringing actions for fraudulent statements pursuant to statutory provisions other than Rule 10b-5(b). As described below, the Commission is already doing this in some cases. Although alternative provisions may provide a convenient avenue for avoiding the *Janus* roadblock, these detours are accompanied by certain disadvantages. This section describes these alternatives and highlights the principal drawbacks of each.

1. Section 17(a) of the Securities Act of 1933

One way the Commission has coped with *Janus* is by relying on Section 17(a)(2) of the Securities Act.[117] This provision contains language similar to that found in Rule 10b-5(b), with a critical difference. Instead of the verb "make," Section 17(a) makes it unlawful to obtain money or property in the offer or sale of securities "by means of" a fraudulent statement.[118] In its briefs, the Commission has argued that this difference in language supports the view that *Janus*'s "ultimate authority" definition of "make" should not be imported to Section 17(a)(2)'s "by means of" language.[119] The Commission has cited *SEC v. Tambone* for the proposition that the phrase "by means of" captures a broader range of activity than Rule 10b-5's "make."[120] Furthermore, the Commission has pointed out that *Janus* was chiefly concerned with limiting implied private actions.[121] Because such private actions are unavailable in Section 17(a),[122] the Commission has argued that *Janus* does not apply to Section 17(a) claims.[123] So far, the handful of courts that have confronted the issue have agreed with the Commission's

117. Securities Act of 1933 § 17(a)(2), 15 U.S.C. § 77q(a)(2) (2012).

118. *Id.*

119. *See, e.g.*, Plaintiff's Memorandum of Law in Opposition to Motion to Dismiss at 19–21, SEC v. Stoker, 865 F. Supp. 2d 457 (S.D.N.Y. 2012) (No. 11 Civ 07388 (JSR)) 2012 WL 2133431.

120. *See, e.g.*, *id.* According to *SEC v. Tambone*, Section 17(a)(2) claims do not require the seller to have made the untrue statement himself; it is enough that the seller "uses" a false statement—"regardless of its source"—in order "to obtain money or property." *Id.* at 20 (quoting SEC v. Tambone, 550 F.3d 106, 127 (1st Cir. 2008)).

121. *See, e.g.*, *id.* at 19.

122. *See, e.g.*, Touche Ross & Co. v. Redington, 442 U.S. 560, 568–78 (1979).

123. Plaintiff's Memorandum of Law in Opposition to Motion to Dismiss, *supra* note 119, at 19 (citing Finkel v. Stratton Corp., 962 F.2d 169, 174 (2d Cir. 1992)).

position.[124] Therefore, if the early cases are any indicator, the Commission may be able to bypass the "ultimate authority" definition of "make" by bringing actions pursuant to Section 17(a)(2).

Section 17(a)(2) and Rule 10b-5(b), however, are not coextensive, and Section 17(a)(2) therefore does not provide a perfect substitute for misstatement actions brought under Section 10(b). Section 17(a)(2) pertains only to misstatements in connection with the "offer or sale" of securities,[125] whereas Section 10(b) applies to both misstatements made in connection with the "sale" of securities and those made in connection with their "purchase."[126] Nevertheless, this difference may not be a significant limitation on the Commission's enforcement efforts if most cases alleging fraudulent statements are in fact in connection with the "sale" of securities rather than their "purchase."[127]

---

124. For instance, in *SEC v. Daifotis*, the district court noted that, "[i]mportantly, the word 'make,' which was the very thing the Supreme Court was interpreting in *Janus*, is absent from the operative language of Section 17(a)." No. C11–00137 WHA, 2011 WL 3295139, at *5 (N.D. Cal. Aug. 1, 2011). Instead, Section 17(a) makes it unlawful (1) "to employ any device, scheme, or artifice to defraud," (2) "to obtain money or property by means of any untrue statement" or omission of a material fact, or (3) "to engage in" transactions that "would operate as a fraud or deceit upon the purchaser." Securities Act of 1933 § 17(a)(2), 15 U.S.C. § 77q(a)(2) (2012). The court also agreed that the Supreme Court's "stringent" interpretation of the word "'make' followed from [its] prior decisions limiting the scope of *implied* private rights of action under Rule 10b-5." *Daifotis*, 2011 WL 3295139, at *6 (emphasis added). Accordingly, the district court held that *Janus*'s definition of "make" does not apply to Section 17(a), which contains no implied private right of action. *Id.* Relying on analogous reasoning, other courts have similarly declined to apply *Janus* to claims under Section 17(a). *See* SEC v. Sells, No. C 11-4941 CW, 2012 WL 3242551, at *7 (N.D. Cal. Aug. 10, 2012); SEC v. Big Apple Consulting USA, Inc., No. 6:09-cv-1963-Orl-28GJK, 2012 WL 3264512, at *3 (M.D. Fla. Aug. 9, 2012); SEC v. Sentinel Mgmt. Grp., Inc., No. 07 C 4684, 2012 WL 1079961, at *14–15 (N.D. Ill. Mar. 30, 2012); SEC v. Pentagon Capital Mgmt. PLC, 844 F. Supp. 2d 377, 422 (S.D.N.Y. 2012); SEC v. Mercury Interactive, LLC, No. 5:07-cv-02822-WHA, 2011 WL 5871020, at *3 (N.D. Cal. Nov. 22, 2011); SEC v. Geswein, No. 5:10CV1235, 2011 WL 4565861, at *2 (N.D. Ohio Sept. 29, 2011); *see also* SEC v. Radius Capital Corp., No. 2:11-cv-116-FtM-29DNF, 2012 WL 695668, at *7 (M.D. Fla. Mar. 1, 2012) (granting a motion to dismiss a Rule 10b-5(b) claim for failure to allege specific facts showing the defendant had "ultimate authority" over statements while denying a motion to dismiss for Section 17(a) claims against the same defendant based on identical allegations). *But see* SEC v. Perry, No. CV-11-1309 R, 2012 WL 1959566, at *8 (C.D. Cal. May 31, 2012) (holding that *Janus* applies to claims brought by the Commission under Section 17(a) of the Securities Act); SEC v. Kelly, 817 F. Supp. 2d 340, 345 (S.D.N.Y. 2011) (same); *In re* Flannery, SEC Release No. 438, 2011 WL 5130058, at *35 (ALJ Oct. 28, 2011) (initial decision) (same).

125. Securities Act of 1933 § 17(a)(2), 15 U.S.C. § 77q(a)(2).

126. Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b) (2012).

127. Insider trading cases, for example, are probably the most prevalent fraud cases that relate to the "purchase" of securities, and they rely on a theory that is wholly different from the "making" of a statement. *See generally* 4 Hazen, *supra* note 26, at § 12.17[1] (explaining that, while Rule 10b-5(b) has been used to bar insider trading, "[i]n most cases . . . accountability for trading on inside information is premised upon Rule 10b-5(c)'s ban on acts or practices that operate as fraud").

When bringing an action under Rule 10b-5, the Commission must prove scienter.[128] One would expect that scienter-based violations are more likely to carry a social stigma than those based on strict liability or negligence. Thus, the main problem with the substitution of Section 17(a)(2) may be its relative ineffectiveness at deterring fraud. Although Section 17(a)(1), like Rule 10b-5, requires proof of scienter, the Commission must only prove negligence in actions brought pursuant to Sections 17(a)(2) and (3).[129] This does not mean that the Commission must bring actions on the basis of negligent conduct. Given the challenges in proving either intentionality or recklessness, however, the temptation to bring actions under the negligence standard would be understandable. *Janus*, which makes it more difficult for the Commission to prosecute misleading statements under Rule 10b-5, may increase the Commission's tendency to rely on Section 17(a)(2) instead of risking dismissal or loss at trial. And if the Commission's primary tool for prosecuting misleading statements requires only proof of negligence, there is a serious risk of diluting the social stigma associated with violating the securities law. Also, negligence-based violations carry smaller penalties than intentional violations.[130] Thus, the cost of violating Section 17(a)(2) may decrease, which could correspondingly weaken the Commission's ability to deter future violations.[131]

---

128. *See* Aaron v. SEC, 446 U.S. 680, 691 (1980) ("In our view, the rationale of *Hockfelder* [sic] ineluctably leads to the conclusion that scienter is an element of a violation of § 10(b) and Rule 10b-5, regardless of the identity of the plaintiff or the nature of the relief sought.").

129. *See id.* at 695–700.

130. *See* Securities Act of 1933 § 20(d)(2), 15 U.S.C. § 77t(d)(2) (setting forth increased monetary penalties when violations involve "fraud, deceit, manipulation, or reckless disregard of a regulatory requirement").

131. Furthermore, the Commission has already received criticism for its shift to negligence-based claims, which by definition allege less culpability than intent-based claims. The spate of negligence-based claims arising out of the financial crisis led one writer to ask whether Congress and the public might think it "better for the Commission to focus on cases where there is clear cut fraud." Lawrence Iason, *The SEC Should Focus on Fraud, Not Negligence*, Forbes (Nov. 16, 2011, 8:06 AM), http://www.forbes.com/sites/insider/2011/11/16/the-sec-should-focus-on-fraud-not-negligence/; *see also* Russell G. Ryan, *To Err Is Human . . . and Punishable by the SEC*, CFO.com (Nov. 1, 2011), http://www.cfo.com/printable/article.cfm/14606438. Of course, the Commission might respond that it would be much easier to prosecute "clear-cut" fraud if the Supreme Court did not write decisions that had the effect of blunting the Commission's enforcement capabilities. In any case, one article pointed out that the Commission would need to provide clearer standards of care if it intends to bring more actions based on negligent conduct alone. *See* David M. Becker, *What More Can Be Done to Deter Violations of the Federal Securities Laws?*, 90 Tex. L. Rev. 1849, 1882–83 (2012).

2. Exchange Act Rule 10b-5(a) and (c)

Although Rule 10b-5(b) deals with fraudulent statements, the Commission has been successful at prosecuting such fraud when it can prove that the misstatement is part of a larger scheme to defraud investors.[132] Accordingly, the Commission might also bring actions under Rule 10b-5(a) and (c), the so-called "scheme liability" provisions.[133] *Janus* involved a Section 10(b) claim, but the Court decided to focus on the language of the statute's operative rule rather than that of the statute itself.[134] Specifically, the Court focused on subsection (b).[135] Notably, neither subsection (a) nor (c) contains the word "make."[136] So, by bringing a "scheme liability" claim, the Commission would appear to avoid *Janus*'s restrictive definition.[137] Moreover, because Rule 10b-5 covers fraud in the "purchase" of securities, this approach does not suffer from the possible limitations discussed above in relation to claims brought under Section 17(a).[138]

Even before *Janus*, however, some courts had been skeptical of what they viewed as plaintiffs' attempts to circumvent the more stringent requirements of Rule 10b-5(b) by simply recharacterizing a fraudulent statement as part of a "scheme."[139] Therefore, this strategy carries litigation risks for the Commission. There is also no way of distinguishing interpretations of Rule 10b-5(a) and (c) on the basis of the plaintiff's identity. Thus, the expansion of these provisions for the purposes of Commission enforcement would simultaneously encourage private litigants to bring more cases. Because *Janus* is focused on limiting the rights of private plaintiffs,

---

132. *See, e.g.*, SEC v. Brown, 740 F. Supp. 2d 148, 171–72 (D.D.C. 2010) (finding that, for the purposes of a motion to dismiss, the defendant's underlying conduct alleged by the Commission for violations of Rule 10b-5(a) and (c) was more than a reiteration of the misrepresentations establishing the Commission's Rule 10b-5(b) misstatement claim).

133. 17 C.F.R. § 240.10b-5(a), (c) (2013).

134. *See* discussion *supra* Part II.B.

135. *See* discussion *supra* Part II.B.

136. 17 C.F.R. § 240.10b-5(a), (c).

137. In fact, in *SEC v. Sell*, No. C 11-4941 CW, 2012 WL 3242551, at *6–7 (N.D. Cal. Aug. 10, 2012), the court rejected the defendant's argument that *Janus* precluded an SEC action pursuant to Rule 10b-5(a) and (c).

138. *See* discussion *supra* Part III.C.1.

139. SEC v. Lucent Techs., Inc., 610 F. Supp. 2d 342, 361 (D.N.J. 2009); *In re* Alstom SA Sec. Litig., 406 F. Supp. 2d 433, 475 (S.D.N.Y. 2005); Schnell v. Conseco, Inc., 43 F. Supp. 2d 438, 447–48 (S.D.N.Y. 1999) (refusing to characterize allegations as market manipulation claims where the alleged "scheme to defraud" consisted largely of an aggregation of material misrepresentations to inflate stock, such as research reports containing misrepresentations of the underlying facts and use of false names to solicit investors).

it is unlikely that courts would be comfortable construing these subsections in a way that would provide an end run around *Janus* for private plaintiffs.

3. Section 20 of the Exchange Act of 1934

Section 20 of the Exchange Act is concerned with liability against those that control and assist primarily violators.[140] Specifically, Section 20(a) provides for liability against any person who directly or indirectly controls another person when the controlled person is found liable for violating any of the federal securities laws.[141] The statute provides a defense for controlling persons who acted in good faith and neither directly nor indirectly induced the prohibited act.[142] Assuming neither affirmative defense applies, the Commission could possibly rely on this statute to bring cases in situations in which the Commission would have previously relied on Section 10(b).

Similarly, the Commission could perhaps overcome *Janus* by using Section 20(b) of the Exchange Act, which makes it unlawful for a person to directly or indirectly violate the federal securities laws "through or by means of any other person."[143] In fact, the *Janus* Court alluded in a footnote to the possibility that Section 20(b) could have been used in that case.[144] As the *Janus* dissent pointed out, however, the contours of this section have not been fully explored because, in the past, Rule 10b-5 has effectively made Section 20(b) unnecessary.[145] For the same reasons, the Commission has not previously relied heavily on Section 20(a). Indeed, it was not until 2010 that Congress, in its Dodd-Frank legislation, clarified that the Commission could even bring an action under Section 20(a).[146] Before then, there was a circuit split as to whether the Commission qualified as a "person" for purposes of bringing actions under Section 20(a).[147]

---

140. Securities Exchange Act of 1934 § 20, 15 U.S.C. § 78t (2012).

141. *Id.* § 20(a), 78t(a).

142. *Id.*

143. *Id.* § 20(b), 78t(b).

144. Janus Capital Grp., Inc. v. First Derivative Traders, 131 S. Ct. 2296, 2304 n.10 (2011).

145. *Id.* at 2311 (Breyer, J., dissenting) ("'There is a dearth of authority construing Section 20(b),' which has been thought largely 'superfluous in 10b-5 cases.'" (quoting 5B Arnold S. Jacobs, Disclosure and Remedies Under the Securities Laws § 11:8 (2011))).

146. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929P(c), 124 Stat. 1376, 1865 (2010) (amending 15 U.S.C. § 78t(a) (2006)).

147. *Compare* SEC v. Coffey, 493 F.2d 1304, 1318 (6th Cir. 1974) (explaining that the SEC is not a "person") *with* SEC v. First Jersey Sec., Inc., 101 F.3d 1450, 1472 (2d Cir. 1996) (explaining that the SEC is a "person" for purposes of controlling person liability).

More problematic is the fact that Sections 20(a) and 20(b) apply to both the Commission and private litigants. So, as is the case when the Commission brings actions under Rule 10b-5(a) and (c), courts have no way of distinguishing their interpretations on the basis of the plaintiff's identity. Accordingly, the expansion of these provisions for the purposes of the Commission's enforcement would simultaneously expand the ability of private litigants to maintain a cause of action. Such an expansion would empower the Commission, but, as with actions under Rules 10b-5(a) and (c), it is unlikely that courts would be comfortable construing these claims under Section 20 in a way that would also provide an end run around *Janus* for private plaintiffs.

Section 20 also contains subsection (e), which allows the Commission to prosecute those who "substantially assist" others in violating federal securities laws.[148] This provision, which Congress passed shortly after *Central Bank* eliminated aiding and abetting liability,[149] allows the Commission to cast a wider net than is available to private plaintiffs. By bringing actions against secondary actors, the Commission can go after those who may lack "ultimate authority" over a statement. Because secondary liability derives from primary liability, however, the Commission is still limited by the possibility that no person will be responsible for "making" the misstatement in the *Janus* sense. Thus, even though Section 20(e) provides the Commission with an additional prosecutorial weapon, it does not completely replenish the Commission's pre-*Janus* arsenal.

IV. A Possible Solution to the Commission's *Janus* Problem

A. A "New" Rule 10b-5

The Commission's reliance on other statutory provisions may not sufficiently restore its pre-*Janus* enforcement capabilities. Accordingly, the Commission could overcome *Janus* by using its rulemaking authority to simply write a "New Rule 10b-5." Such a new rule could, in addition to being more expansive, govern only public enforcement, while the "Old Rule 10b-5" would continue to limit the parameters of the implied private right of action. Rule 10b-5 was written pursuant to this rulemaking authority.[150] Unlike

148. Securities Exchange Act of 1934 § 20(e), 15 U.S.C. § 78t(e) (2012).
149. *See supra* Part I.B and accompanying text.
150. *See* discussion *supra* Part I.A.

previous decisions limiting actions under Rule 10b-5, *Janus* emphasized a single word contained in the Rule, rather than focusing on the statutory language found in Section 10(b).[151] Because *Janus* does not limit the scope of the statute, it does not prevent the Commission from issuing a new rule. Courts certainly may look askance at a rule that so easily sidesteps the decision in *Janus*, or they may be untroubled by a change in public enforcement under Rule 10b-5, given that, at its core, *Janus* is a decision about limiting the *private right of action* implied under Section 10(b).[152]

In order to restore the Commission's enforcement powers, it could write a rule with language nearly identical to Rule 10b-5, but with two important changes. First, the Commission could change the word "make" to another verb or phrase, like "create," "by means of," or "substantially participates in the creation of." Such a change would allow courts to avoid the interpretive somersaults necessary to explain how *Janus* was really a decision about limiting private actions. Second, the Commission could include language that plainly states that the new rule applies only to public enforcement. Because the Court has never questioned the Commission's power under Section 10(b) to bring actions for fraudulent statements,[153] the new rule would not raise concerns about the Commission writing a rule that exceeds the limits imposed by statute.[154]

More importantly, this new rule would address the Court's concerns about fueling private litigation. As explained in Part I, the Court has begrudgingly conceded the existence of an implied private right of action. But, the Court has vociferously opposed its expansion since *Blue Chip*, stating that such an implied action must be narrowly construed.[155] As the *Janus* decision demonstrates, the Court has not always adequately distinguished its holdings on the basis of the plaintiff's identity. Although a private action under Rule 10b-5 may require a narrower approach, this is problematic when the narrower approach is applied to a word that also applies to public actions.

Having two separate rules would enable the Court to overtly adjust its interpretive approach to Rule 10b-5 depending on whether

151. *See* discussion *supra* Part II.B.

152. *See* discussion *supra* Part III.B.

153. Section 10(b) of the Securities Exchange Act appears to specifically provide for such actions. *See* Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b) (2012).

154. *See, e.g.*, Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc., 552 U.S. 148, 157 (2007) (noting that the scope of Section 10(b) is determined by the text of the statute and the power to extend this scope belongs to Congress).

155. *See supra* Part I.A.

the government or a private plaintiff is bringing suit. Such an approach would allow the Court to continue its practice of narrowly interpreting the statute's language in cases involving private plaintiffs, thereby dealing with the problem and costs of strike suits. At the same time, when deciding cases brought by the Commission, the Court could invoke the pre-*Blue Chip* approach and interpret the statute flexibly with its remedial purpose in mind,[156] strengthening the Commission's enforcement efforts. By explicitly acknowledging this difference, the Court could straightforwardly limit private litigation while freeing public enforcement actions from *Janus*'s inadvertent constraints.

B. The Beneficial Policy Consequences of a Bifurcated Approach to Rule 10b-5

In addition to maintaining the Commission's broad enforcement powers, having both a "private" and "public" Rule 10b-5 could generate a beneficial policy outcome: a bifurcated approach to misstatement liability could result in a more properly calibrated deterrent mechanism. Deterrence is a necessary element of any enforcement regime, but the private attorney general has not necessarily been an effective anti-fraud mechanism.[157] Instead, the current system may actually overdeter, causing companies to incur costs that are ultimately borne by investors.[158] This is a perverse result, considering that investor protection is regarded as one of the primary purposes of the securities laws.[159] While the Commission has argued that private litigation is a "necessary supplement" to public enforcement,[160] it is not clear that this is true as an empirical

156. *See* discussion *supra* Part I.C.

157. For an early article discussing this issue, see John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter is Not Working*, 42 Md. L. Rev. 215 (1983). More recent articles have focused on the costs of private securities litigation and the problem of overdeterrence. *See, e.g.*, Amanda M. Rose, *Reforming Securities Litigation Reform: Restructuring the Relationship between Public and Private Enforcement of Rule 10b-5*, 108 Colum. L. Rev. 1301 (2008).

158. Rose, *supra* note 157, at 1331–37.

159. *See The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, U.S. Sec. & Exchange Commission, http://www.sec.gov/about/whatwedo.shtml (last visited November 29, 2013) ("The mission of the U.S. Securities and Exchange Commission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.").

160. *See* Remarks of Former SEC Chairman Arthur Levitt, http://www.sec.gov/news/testimony/testarchive/1995/spch025.txt ("[P]rivate actions also provide a 'necessary supplement' to the Commission's own enforcement activities by serving to deter securities law violations.").

matter.[161] In any case, this view is predicated on the general consensus that the Commission lacks the necessary resources to prosecute securities fraud alone.[162] Without fomenting private litigation, a bifurcated approach to Section 10(b) liability would allow courts to empower the Commission, giving it the legal resources to prosecute perpetrators of fraud more effectively.

A proposal to shift the balance of private and public enforcement is clearly not new. When Congress passed the Private Securities Litigation Reform Act in 1995 (PSLRA),[163] it attempted to reduce private securities litigation while increasing the Commission's enforcement capabilities. For instance, the PSLRA contained the lead plaintiff provision that was meant to quell "lawyer-driven" litigation by reducing the costs of monitoring "entrepreneurial" attorneys.[164] It also contained a statutory safe harbor for forward-looking statements and imposed heightened pleading standards for complaints alleging violations of the securities laws.[165] But the PSLRA also explicitly granted the Commission the power to bring actions against aiders and abettors because of the concern that *Central Bank* may have restricted the Commission's ability to bring actions against these secondary defendants.[166]

Furthermore, legal scholars have proposed reforms that similarly address the perceived costs of private securities litigation by making it more difficult to bring suits. For example, Professor Joseph A. Grundfest suggested that the Commission "disimply" the private right of action from Section 10(b) and Rule 10b-5.[167] Professor Grundfest explained that, while the implied private of action may be "well established," it "is not immutable."[168] Accordingly, through its rulemaking authority, the Commission could "disimply" private

---

161. *See* Rose, *supra* note 157, at 1347–49 ("*Borak*'s mantra that private enforcement is a 'necessary supplement' to Commission action merely states a conclusion, and the foregoing analysis demonstrates that it is hardly a self-evident one.").

162. *See, e.g.*, Luis A. Aguilar, *Statement by Commissioner: Defrauded Investors Deserve Their Day in Court*, U.S. SEC. & EXCHANGE COMMISSION (April 11, 2012), https://www.sec.gov/News/PublicStmt/Detail/PublicStmt/1365171490204#_ednref20 ("It is unrealistic to expect that the Commission will have the resources to police all securities frauds on its own, and as a result, it is essential that investors be given private rights of action to complement and complete the Commission's efforts.").

163. Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified as amended in scattered sections of 15 U.S.C.).

164. *See id.* § 101 (codified as amended in 15 U.S.C. §§ 77z-1, 78u-4).

165. *See id.* § 102 (codified as amended in 15 U.S.C. §§ 77z-2, 77u-5).

166. *See id.* § 104 (codified as amended in 15 U.S.C. § 78t).

167. *See* John A. Grundfest, *Disimplying Private Rights of Action under the Federal Securities Laws: The Commission's Authority*, 107 HARV. L. REV. 961 (1994).

168. *Id.* at 965.

rights of actions under Section 10(b) and Rule 10b-5 without restricting "[its] own ability to pursue claims of fraud."[169] According to Professor Grundfest, through "disimplication" the Commission would not have to worry about fomenting abusive private litigation and could actually "create new disclosure obligations," which could further protect investor rights.[170] In a more recent article addressing shortcomings of private securities litigation, Professor Amanda M. Rose proposed an "oversight approach" which would grant the Commission "the ability to screen which Rule 10b-5 class actions may be filed, and against whom."[171] According to Professor Rose, because of profit-driven private enforcement, the current regime "leads to excessive enforcement and . . . overdeterrence"[172] that can hamper the system's ability to achieve optimality.[173] Professor Rose's proposal assumes that, because the Commission is not motivated by profit, it may be better suited to determine which suits have merit. Both Professor Grundfest and Professor Rose's proposals attempt to solve what they identify as a problem of too much private litigation by shifting the balance toward public enforcement.

Like these proposals, a bifurcated approach to Rule 10b-5 could potentially achieve a more optimal ratio of private litigation to public enforcement. This could produce a more properly calibrated deterrence mechanism by reducing the incidence of underdeterrence (by increasing public enforcement) while decisions like *Janus* continue to reduce the incidence of overdeterrence (by narrowing the implied private right of action). More importantly, a bifurcated approach to Rule 10b-5 may actually be more feasible than those that overtly abate or potentially eliminate private suits.

The Commission was created and granted broad rulemaking authority with the idea that it could use its expertise to more effectively respond to problems in the securities markets.[174] By passing a new Rule 10b-5, the Commission would simply be exercising this broad rulemaking authority. It would also be creating a new

---

169. *Id.* at 966.

170. *Id.*

171. Rose, *supra* note 157, at 1301.

172. *Id.* at 1327.

173. *See id.* at 1326–27.

174. Steve Thel, *The Original Conception of Section 10(b) of the Securities Exchange Act*, 42 Stan. L. Rev. 385, 454 n.320 (1990) (quoting S. Rep. No. 73-792, at 5–6 (1934)) ("From the outset, the committee has proceeded on the theory that so delicate a mechanism as the modern stock exchange cannot be regulated efficiently under a rigid statutory program. Unless considerable latitude is allowed for the exercise of administrative discretion, it is impossible to avoid, on the one hand, unworkable 'strait-jacket' regulation and, on the other, loopholes . . . .").

rule to help restore its own enforcement capabilities. The public would arguably be less likely to perceive such a move as an overt threat to the securities class action system than would be the case if the Commission decided to "disimply" the private right of action or announce that it would begin screening securities class actions. Furthermore, public support for a new rule that increases the Commission's ability to prosecute fraud would likely be easy to garner, given the blame the Commission has received for not doing enough to prevent fraud in light of recent financial scandals.[175]

Conclusion

Based on the Supreme Court's gradual narrowing of the implied private right of action in securities fraud cases, it was no surprise that in *Janus*—a private party suit—the Court opted for an interpretation that narrowed the pool of potential defendants in actions brought under Section 10(b) and Rule 10b-5. Unlike prior decisions, however, the Court based its decision on an interpretation of a single word that restricts the Commission in the same way that it does private plaintiffs. Although the Commission may be able to bypass *Janus* by bringing actions under statutes or rules other than Rule 10b-5, those rules and statutes are not coextensive with Rule 10b-5 and raise additional complications.

Thus, the Commission's best option for adequately restoring its pre-*Janus* arsenal may be to exercise its rulemaking authority to issue a new Rule 10b-5. The rule would make two important changes to the original Rule 10b-5. First, it should change the word "make" to a more expansive word or phrase that captures those individuals that substantially participate in the creation of a material misleading statement, even if they lack "ultimate authority." Second, the new rule should only apply to public enforcement actions. Such a rule would be consistent with *Janus* because it would avoid the "make" issue and would not expand the implied private right of action.

Going forward, this new rule would allow courts to adjust their approach based on the plaintiff's public or private identity, leading to clearer decisions and permitting courts to narrowly construe the implied private right of action without restricting the Commission's ability to prosecute fraud. This would address the problems of both

175. *See, e.g.*, Patrick Jennings, *SEC Blamed for Failing to Spot Madoff Fraud*, Financial Times (July 3, 2009, 3:01 AM), http://www.ft.com/cms/s/0/ee1591a2-6726-11de-925f-00144feabdc0.html#axzz2rrECsALk.

underdeterrence and overdeterrence. In this way, the Commission would be fulfilling its Section 10(b) mandate to "prescribe as necessary or appropriate" rules and regulations that are "in the public interest."[176]

176. Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b) (2012).