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In this issue... yet another securities case will be coming before the U.S. Supreme Court. We look at the case and its possible implications.

Since early 2005 there have been three securities cases — a relative flurry — heard by the U.S. Supreme Court. These cases, Dura, Dabit and Tellabs*, were discussed in previous issues of this newsletter. While no case reaching the Supreme Court can be viewed as insignificant, the questions decided in these cases were largely technical; they modified the securities class action landscape rather than radically reshaping it, and although all the decisions favored the defendants in the original actions, the plaintiffs' bar appeared to suffer no serious setbacks. The frequency of class action filings has been falling, but few commentators have ascribed that decline exclusively to the Supreme Court rulings.

The upcoming case, *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc. et al.** (sometimes also referred to as "Charter Communications," the defendant in the original case), has the potential to make a significant impact on class action filings, investor recourse, American businesses and the insurance industry.

History

In 1994 the U.S. Supreme Court determined that under the federal Securities Acts, shareholders had no cause of action against defendants alleged to have "aided and abetted" a primary violator of those laws (*Central Bank of Denver, N. A. v. First Interstate Bank of Denver, N. A.**). The decision was close: 5 to 4, with the majority opinion conceding that, "To be sure, aiding and abetting a wrongdoer ought to be actionable in certain instances. The issue, however, is not whether imposing private civil liability on aiders and abettors is good policy but whether aiding and abetting is covered by the statute."

For 13 years this decision has effectively shielded alleged secondary participants who might have acted along with primary perpetrators to defraud investors. Such participants could include bankers, investment bankers, accountants, attorneys or, as in *Stoneridge*, third-party suppliers.

A Circuit Split

The *Stoneridge* case was spawned by an earlier securities class action lawsuit in which Charter Communications, a cable TV provider, allegedly entered into a fraudulent pact with the suppliers of its TV set-top boxes. Under this alleged agreement Charter would inflate the price it paid for the boxes, typically by $20 a box. This extra money would then be used by the suppliers (Scientific-Atlanta and Motorola) to buy advertising space with Charter, appearing to increase Charter's advertising revenue and enabling Charter to meet stock analysts' expectations.

Charter's shareholders sued Charter and its alleged co-conspirators in the sham transaction. Charter settled with plaintiffs in 2004 for $144 million* but Scientific-Atlanta and Motorola fought the claims, asserting that shareholders did not have standing to sue. The U.S. Court of Appeals for the 8th Circuit agreed with the suppliers and upheld the district court's rejection of the shareholders' action*.

A similar conclusion was also reached in the 5th Circuit that involved claims originating from the Enron collapse (*Regents of the University of California v. Credit Suisse First Boston**). However, in an earlier decision by the 9th Circuit Court of Appeals (*Simpson v. AOL Time Warner**), the court had indicated that a lawsuit against secondary participants who had not made false or misleading statements might have merit. Faced with this split

between the circuits, the Supreme Court agreed in early 2007 to accept the appeal of Charter investors, led by Stoneridge Investment Advisers, LLC.

The Key Issues

The 1994 *Central Bank* decision specifically protects "aiders and abettors" from private actions. To distinguish their case, plaintiffs in *Stoneridge* have invoked the term "scheme liability" to describe what allegedly happened between Charter and its suppliers that defrauded investors. A "scheme," it is argued, is quite different from aiding and abetting, and so alleged participants in the scheme do not have protection from securities lawsuits afforded under *Central Bank*.

For their part, the defendants stand behind what they see as the critical features of *Central Bank*: that no public statements which could be relied upon by investors were made by the secondary participants. Therefore any claims by shareholders for deceptive conduct are precluded by the absence of such public statements and lack of any consequent reliance upon them.

Battle Lines Drawn

The case has produced an unusually high number of *amicus curiae* filings*. These "friends of the court" briefs show impressive political and economic muscle on both sides. Pro-investor filings include those made by Attorneys General from 30 states, a phalanx of powerful pension funds, the Council of Institutional Investors, the AARP and the Consumer Federation of America. A belated brief was also filed by John Conyers, Jr. and Barney Frank, Chairman of the House Committee on the Judiciary and Chairman of the House Committee on Financial Services, respectively.

Filers supporting the suppliers include the American Bankers Association, the National Association of Manufacturers, the U.S. Chamber of Commerce, NASDAQ and the New York Stock Exchange, the American Institute of Certified Public Accountants, the Business Roundtable and various former Securities and Exchange commissioners.

The Securities and Exchange Commission itself came out in support of the investors* and asked the U.S. Justice Department to file a brief in their support. The Solicitor General declined and instead filed a brief supporting the suppliers*, thereby revealing a rare public rift between the two government agencies and highlighting the confrontational nature of the issue.

Summary

Commentators generally agree that *Stoneridge* could be the most far-reaching securities decision issued by the Supreme Court in decades and will likely have an immediate impact on other similar pending cases. A victory for the *Stoneridge* investors will almost certainly give a significant boost to the plaintiffs' bar by rendering alleged secondary "schemers" open to private shareholder actions. Arguments are scheduled to be heard on October 9th, and many will be watching closely. ❖

* *Links to resource material can be found at:*
www.cug.com/ments/52_notes.html

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