LIBERTY UNIVERSITY

Liberty University Law Review

Volume 11 | Issue 1 Article 4

September 2016

And Then It Was Gone: a Critique of Section 10(B) Collective Scienter Pleading in the Sixth Circuit's Bondali Decision

Brock K. Bales

NOTE

AND THEN IT WAS GONE: A CRITIQUE OF SECTION 10(B) COLLECTIVE SCIENTER PLEADING IN THE SIXTH CIRCUIT'S *BONDALI* DECISION

Brock K. Bales[†]

ABSTRACT

"Well . . . we are [all] against fraud, aren't we?"[1] *But how do we channel our shared repulsion of fraud into an effective legal standard? This Note posits that pleading collective scienter under a Section 10(b) and Rule 10b-5 is a step in the wrong direction. A step opposite that of the majority of circuit courts. The Sixth Circuit should abandon its collective scienter pleading standard following its recent decision in Bondali v. Yum! Brands, Inc., and adopt a felicitous legal standard like the Second or Seventh Circuit's.*

The issue of collective scienter is best described with a question: if no single individual employee or officer within a corporation possesses the scienter necessary for pleading corporate liability under Rule 10b-5 and the Private Securities Litigation Reform Act (PSLRA), may a plaintiff survive a motion to dismiss by pleading the collective scienter of many individuals within the corporation? Collective scienter aggregates the collective knowledge of a corporation's employees for the purpose of pleading that the corporate defendant possessed the requisite scienter for a Section 10(b) and Rule 10b-5 private cause of action.

Collective scienter is a useless addendum to an already complicated pleading analysis, and it creates disunity among the circuit courts. Congress intentionally raised the bar for pleading corporate securities fraud with the PSRLA's strong inference language, and the Supreme Court intentionally limited the scope of the private cause of action it created. Collective scienter is a judicial construct designed to circumvent the heightened pleading standard,

---

† *Notes and Comments Editor*, LIBERTY UNIVERSITY LAW REVIEW, Volume 11. J.D. Candidate, Liberty University School of Law (2017); BS, Business Administration: Finance, Liberty University, 2014. Soli Deo Gloria. All I am and ever hope to be I owe to my darling parents—a father who taught me how the mind thinks, and a mother who taught me how the heart cares.

1. Milton V. Freeman, *Conference on Codification of the Federal Securities Laws: Administrative Procedures*, 22 BUS. LAW. 793, 922 (1967) (statement made by Sumner Pike upon approving Section 10(b)).

and as such, it is contrary to congressional intent and Supreme Court precedent in limiting the Section 10(b) private cause of action.

The Sixth Circuit should retain a focus on the strong inference language to the exclusion of inquiring into collective scienter. The plaintiff would plead the required state of mind of the corporation itself in accordance with the strong inference language as the Second Circuit held in Teamsters Local 445 Freight Division Pension Fund v. Dynex Capital, Inc., and the Seventh Circuit held in Tellabs, Inc. v. Makor Issues and Rights, Ltd. When specific individual officers cannot be named for the imputation of scienter to the corporation, it is much simpler to argue that the singular defendant, the corporation, made misstatements—which, in the end, it did through its employees—rather than to inquire into whether multiple individuals can be located in the corporation who together possess the requisite scienter to plead Section 10(b) liability. In this manner, the language of the PSLRA—a singular defendant and a strong inference standard—maintains its full effect without confusion.

I. INTRODUCTION

"Well . . . we are [all] against fraud, aren't we?"[2] But how do we channel our shared repulsion of fraud into an effective legal standard? This Note posits that pleading collective scienter under a Section 10(b)[3] and Rule 10b-5[4] is a step too far in the wrong direction. Most circuit courts agree that collective scienter is not the proper means of pleading corporate scienter when the plaintiff cannot identify a specific individual corporate officer.[5] Rather, the focus should be on respondeat superior liability and the strong inference language of the Private Securities Litigation Reform Act

---

2. Milton V. Freeman, *Conference on Codification of the Federal Securities Laws: Administrative Procedures*, 22 BUS. LAW. 793, 922 (1967) (statement made by Sumner Pike upon approving Section 10(b)).

3. Securities Exchange Act of 1934, ch. 40, tit. I, §10 (codified as amended at 15 U.S.C. § 78j(b) (2011)).

> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement[,] 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.

4. 17 C.F.R. § 240.10b-5 (2011).

5. *See infra* Part IV.

(PSLRA).[6] Two circuits reject collective scienter, and three circuits reject collective scienter as a matter of emphasizing the strong inference language of the PSLRA.[7] The latter appears to be closest to Supreme Court precedent.[8]

The Sixth Circuit stands alone in its adoption of the collective scienter standard.[9] It is the position of this Note that the Sixth Circuit should abandon collective scienter after its recent decision in *Bondali v. Yum! Brands, Inc*.[10] After providing a background for the collective scienter issue, this Note will support its position with the following arguments: collective scienter does not comport with congressional intent circumscribing corporate liability under Section 10(b) through the PSLRA;[11] the strong inference standard as adopted by the Second and Seventh Circuits provides a better solution to the respondeat superior problem than collective scienter; the strong inference focus comports with congressional intent;[12] collective scienter does little to solve the respondeat superior underinclusion problem;[13] collective scienter creates confusion when trying to level it against the language of the PSLRA;[14] and the Sixth Circuit's collective scienter precedent lacks the stability that allows corporations to manage their exposure to risk.[15]

If corporations are to orient their behavior when faced with a cause of action as fact sensitive as securities fraud, the pleading standard must be stable and coherent. By abandoning collective scienter, the Sixth Circuit would align its pleading standard with the congressional intent of the PSLRA and the Supreme Court's intentional restriction of the Section 10(b) private cause of action.

II. BACKGROUND

A person is a person no matter how big,[16] and unfortunately, any size person is capable of naughtiness. By creating the person of the

---

6. Private Securities Litigation Reform Act, 109 Stat. 737 (1995); *see infra* Part II.
7. *See infra* Part IV.
8. *See infra* Section II.E.
9. *See infra* Section IV.C.
10. Bondali v. Yum! Brands, Inc., 620 F. App'x 483 (6th Cir. 2015).
11. *See infra* Section II.C.
12. *See infra* Section IV.A.
13. *See infra* Section IV.B.
14. *See infra* Section IV.D.
15. *See infra* Section IV.D.
16. DR. SEUSS, HORTON HEARS A WHO! (1954).

corporation,[17] the American legal system faces the problems of a creator. It must understand what it has created and learn how to regulate its often officious and complex offspring. Sadly, the past decade is ripe with examples of corporate fraud.[18] The Enrons and WorldComs of the world have left the American public in awe of the potential of corporate depravity.[19] Along with the creation of heightened fraud pleading standards under the PSLRA, it is this public outcry that is, at least in part, responsible for the rise of collective scienter theory under the judicially created Section 10(b) private cause of action.[20] But the justifiable desire to hold a corporation liable went too far when it developed collective scienter.

A. Collective Scienter and Definitions of Terms

A corporation is a single person created by legal fiction that represents a collective of individuals.[21] The issue of collective scienter is best described with a question: if no single individual employee or officer within a corporation possesses the scienter necessary for pleading corporate liability under Rule 10b-5[22] and the PSLRA,[23] may a plaintiff survive a motion to dismiss[24] by pleading the collective scienter of many individuals within the corporation? Corporate scienter is the knowledge of wrongdoing by the corporation itself that "'is necessarily derived from its employees' or

17. 1 U.S.C. § 1 (2012) states, "In determining the meaning of any Act of Congress, unless the context indicates otherwise . . . the words 'person' and 'whoever' include corporations, companies . . . as well as individuals . . . ." *See Corporation*, BLACK'S LAW DICTIONARY (10th ed. 2014).

18. Patricia S. Abril & Ann M. Olazábal, *The Locus of Corporate Scienter*, 2006 COLUM. BUS. L. REV. 81, 121-22 (2006).

19. Ashley S. Kircher, Note, *Corporate Criminal Liability Versus Corporate Securities Fraud Liability: Analyzing the Divergence in Standards of Culpability*, 46 AM. CRIM. L. REV. 157, 172 (2009); *see generally* Marianne M. Jennings, *A Primer on Enron: Lessons From A Perfect Storm of Financial Reporting, Corporate Governance and Ethical Culture Failures*, 39 CAL. W. L. REV. 163 (2003).

20. O'Riordan, *supra* note 20, at 1623.

21. 1 U.S.C. § 1; Burwell v. Hobby Lobby Stores, Inc., 134 S. Ct. 2751 (2014) (affirming the legal rights of corporations as people in terms of free speech and religious rights); Citizens United v. FEC, 558 U.S. 310 (2010) (affirming a broad conception of corporate personhood); Abril & Olazábal, *supra* note 18, at 84-85, 103; Kircher, *supra* note 19.

22. 17 C.F.R. § 240.10b-5 (2011).

23. Private Securities Litigation Reform Act, 109 Stat. 737 (1995).

24. FED. R. CIV. P. 12(b)6.

directors.'"[25] The law of agency makes it clear that the knowledge of a single corporate officer acting within the scope of his employment is imputed to the corporation.[26] Therefore, if a plaintiff can identify a corporate actor who committed fraud while acting within the scope of his employment, the corporation may be held liable for the fraud.[27] Collective scienter refers to the aggregation of the scienter possessed by a group of employees in a corporation.[28] Only one circuit adopted collective scienter, leaving an unresolved circuit split.[29]

B. Statutory Roots of Collective Scienter

Collective scienter theory did not develop in a vacuum; it is the product of a complicated legislative and judicial background. Securities regulation came into being on the heels of the Great Depression with the Securities Exchange Act of 1934 ("1934 Act") and the creation of Securities and Exchange Commission ("SEC").[30] The 1934 Act and the SEC were meant to curb corporate corruption.[31] In terms of fraud regulation, the heart of the 1934 Act is Section 10(b).[32] Section 10(b) defends against fraud by prohibiting the use of manipulative or deceptive devices "in connection with the purchase or sale of any security."[33] The purpose of Section 10(b) is primarily deterrence,[34] and Section 10(b) finds its constitutional teeth in the Commerce Clause.[35] Section 10(b) is "nonself-operative"[36] without regulations provided by the SEC,[37] but it is still the 1934 Act's general

---

25. 4 THOMAS LEE HAZEN, TREATISE ON THE LAW OF SECURITIES REGULATION 43 (West Practitioner's Ed. 6th ed. 2009) (quoting In re Marsh & McClennan Cos. Sec. Litig., 501 F. Supp. 2d 452, 481 (S.D.N.Y 2006)).

26. *Id.* at 43-44.

27. *Id.*

28. *Id.* at 44.

29. *Id.* at 44-45.

30. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 194-95 (1976); Justin Marocco, Comment, *When Will It Finally End: The Effectiveness of the Rule 10b-5 Private Action as a Fraud-Deterrence Mechanism Post-Janus*, 73 LA. L. REV. 633, 635 (2013).

31. O'Riordan, *supra* note 20, at 1599.

32. 15 U.S.C. § 78j(b).

33. 15 U.S.C. § 78j(a)(1).

34. Abril & Olazábal, *supra* note 18, at 101; Bradley J. Bondi, *Dangerous Liaisons: Collective Scienter in SEC Enforcement Actions*, 6 N.Y.U. J.L. & BUS. 1, 24 (2009).

35. 15 U.S.C. § 78j; 3 HAZEN, *supra* note 25, at 523.

36. Marocco, *supra* note 30, at 636.

37. 15 U.S.C. §78j. "Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." *Id.*

antifraud provision.[38] With little ado, the SEC gave Section 10(b) operation with the SEC's "broad anti-fraud provision," Rule 10b-5.[39] Rule 10b-5 proved to be a "powerful antifraud weapon."[40] Still, neither Section 10(b) nor Rule 10b-5[41] provides for a private cause of action.[42] Accordingly, the Court constructed a Section 10(b) private cause of action.[43] The private cause of action itself is not questioned.[44] As will become clear, the private cause of action can be difficult to plead,[45] but it is purposefully so.[46]

---

38. 3 HAZEN, *supra* note 25, at 520.

39. 17 C.F.R. § 240.10b-5; Milton V. Freeman, Colloquium Foreword, 61 FORDHAM L. REV. S1, S1-S2 (1993); Marocco, *supra* note 30, at 633-634.

40. 3 HAZEN, *supra* note 25, at 521.

41. 17 C.F.R. § 240.10b-5 (2011).

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
> (a) To employ any device, scheme, or artifice to defraud,
> (b) To 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 the light of the circumstances under which they were made, not misleading, or
> (c) To 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.

42. Janus Capital Grp., Inc. v. First Derivative Traders, 131 U.S. 2296, 2301 (2011) ("Although neither Rule 10b-5 nor § 10(b) expressly creates a private right of action, this Court has held that 'a private right of action is implied under § 10(b).'") (quoting Superintendent of Ins. of N. Y. v. Bankers Life & Casualty Co., 404 U.S. 6, 13, n. 9 (1971)).

43. Stoneridge Inv. Partners, LLC. v. Scientific-Atlanta, Inc., 552 U.S. 148, 157, 163-65 (2008); Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 313 (2007); Superintendent of Ins. of New York v. Bankers Life & Casualty Co., 404 U.S. 6, 13 n.9 (1971); *see* 3 HAZEN, *supra* note 25, at 522-23; O'Riordan, *supra* note 20, at 1599. The first case to impose a private cause of action under § 10 (b) was Kardon v. National Gypsum Co., 69 F. Supp. 512, 513-14 (1946) (allowing a private cause of action where three defendants used fraudulent misrepresentation convinced the plaintiffs to sell their stock to them for much less than fair market value). *See also Ernst*, 425 U.S. at 196 n.16.

44. *Ernst*, 425 U.S. at 196 (stating that "the existence of a private cause of action for violations of [§ 10 (b) and Rule 10b-5] is now well established") (citing Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 730 (1975)); *see generally* O'Riordan, *supra* note 20, at 1599. The Supreme Court prescribes that the elements of this private cause of action should start with the language of § 10 (b). *Ernst*, 425 U.S. at 196-97 (citing Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 756 (1975)).

45. 3 HAZEN, *supra* note 25, at 522 (stating that "not much can be gleaned from the history of the [Rule 10b-5])." In providing support for the *Birnbaum* rule, the Supreme Court stated,

C. Section 10(b) and Rule 10b-5 Private Cause of Action

Although the private cause of action exists, the Supreme Court has limited its scope.[47] In *Stoneridge Inv. Partners, LLC v. Scientific—Atlanta, Inc.*, the Supreme Court laid out the generally accepted elements of a Section 10(b) and Rule 10b-5 private cause of action as follows: "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation."[48] For purposes of this Note, the main element for consideration is element two: scienter. Scienter is "a mental state embracing intent to deceive, manipulate, or defraud."[49] The requisite

---

> *We quite agree that if Congress had legislated the elements of a private cause of action for damages, the duty of the Judicial Branch would be to administer the law which Congress enacted*; the Judiciary may not circumscribe a right which Congress has conferred because of any disagreement it might have with Congress about the wisdom of creating so expansive a liability. But as we have pointed out, we are not dealing here with any private right created by the express language of § 10 (b) or of Rule 10b-5. No language in either of those provisions speaks at all to the contours of a private cause of action for their violation. However flexibly we may construe the language of both provisions, nothing in such construction militates against the Birnbaum rule. We are dealing with a private cause of action which has been judicially found to exist, and which will have to be judicially delimited one way or another unless and until Congress addresses the question. Given the peculiar blend of legislative, administrative, and judicial history which now surrounds Rule 10b-5, we believe that practical factors to which we have adverted, and to which other courts have referred, are entitled to a good deal of weight.

Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 748-49 (1975) (emphasis added). The *Birnbaum* rule limits the potentially broad liability and extensive litigation provided by "liberal discovery provisions" by "permit[ting] exclusion prior to trial of those plaintiffs who were not themselves purchasers or sellers of the stock in question." *Id.* at 741-42.

46. 109 STAT. 737. Title I of the Private Securities Litigation Reform Act of 1995 is "Reduction of Abusive Litigation." *Id. See infra* Section II.C.

47. 3 HAZEN, *supra* note 25, at 522-23.

48. Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, 552 U.S. 148, 157 (2008); *Bondali*, 620 F. App'x at 489 (citing *Stoneridge Inv. Partners*, 552 U.S. at 157); KBC Asset Mgmt. N.V. v. Omnicare, Inc., 769 F.3d 455, 469 (2014); 3 HAZEN, *supra* note 25, 531-32; *see generally* Glazer Capital Mgmt., LP v. Magistri, 549 F.3d 736, 741 (9th Cir. 2008); Southland Sec. Corp. v. Inspire Ins. Sols., Inc., 365 F.3d 353, 362 (5th Cir. 2004); O'Riordan, *supra* note 20, at 1600.

49. O'Riordan, *supra* note 20, at 1600 (citing *Ernst*, 425 U.S. at 193-94 n. 12); 3 HAZEN, *supra* note 25, at 535-36; 4 HAZEN, *supra* note 25, at 23; *see Scienter*, BLACK'S LAW DICTIONARY (10th ed. 2014).

scienter for a Section 10(b) action need not be shown only by proof of negligence; recklessness can be sufficient to show scienter as well.[50] Scienter may be shown by circumstantial evidence.[51]

For a shareholder to withstand a motion pursuant to Federal Rule of Civil Procedure 12(b)(6)[52] in a Section 10(b) suit, a plaintiff faces a higher pleading threshold than a general FRCP 9(b)[53] claim.[54] The PSLRA[55] goes beyond the particularity pleading requirements of FRCP 9(b).[56] The PSLRA requires that a plaintiff in a Section 10(b) action prove "that *the defendant* acted with a particular state of mind . . . with respect to each act or omission

---

50. 3 HAZEN, *supra* note 25, at 536; 4 HAZEN, *supra* note 25, at 40-41. The Supreme Court asserts that the intentional and willful language of § 10(b) and Rule 10b-5, especially "manipulative," showed that Congress did not adopt a negligence standard of liability, and the Court rejects the "gloss" that the Commission sought to impose on the language that it was just the damaging effect on the shareholders that mattered to Congress, not the whether the conduct was knowing or intentional. *Ernst*, 425 U.S. at 198-200. Whether recklessness is enough under § 10(b) and Rule 10b-5, the Supreme Court left undecided. *Id.* at 193-94 n.12 (stating that the Court "need not address here the question of whether, in some circumstances reckless behavior is sufficient for civil liability under § 10(b) and Rule 10b-5."); O'Riordan, *supra* note 20, at 1601 n.32 (2007). The Supreme Court again avoided deciding whether or not recklessness satisfied the scienter element of § 10(b) in *Tellabs, Inc.*, 551 U.S. at 319 n.3. Despite this, "[e]very Court of Appeals that has considered the issue has held that a plaintiff may meet the scienter requirement by showing that the defendant acted intentionally or recklessly, though the Circuits differ on the degree of recklessness required." *Id.* (citing Ottmann v. Hanger Orthopedic Grp., Inc., 353 F.3d 338, 343 (2003)). Regardless of whether recklessness is enough, the Supreme Court holds that Congress clearly intended to circumscribe intentional conduct. *Ernst*, 425 U.S. at 201, 208, 214.

51. 4 HAZEN, *supra* note 25, at 39-40 (stating that all Circuits agree that scienter may be shown by circumstantial evidence, but "the courts are split on whether motive and opportunity standing alone are sufficient"). The Supreme Court gave guidance here by holding that motive and opportunity is a factor in the analysis that is not by itself dispositive. *See Makor*, 437 F.3d at 601; *Tellabs, Inc.*, 551 U.S. at 325; 4 HAZEN, *supra* note 25, at 28.

52. FED. R. CIV. P. 12.

53. FED. R. CIV. P. 9. "Fraud or Mistake; Conditions of Mind. In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally." *Id.* Pleading a survivable FRCP 9(b) cause of action is already difficult, but just like the PSLRA, it is purposefully so. *See generally* 27 A.L.R. Fed. 407. The purposes of the rule are: "to apprise other party of claim," "[t]o permit drafting of responsive pleading," "[t]o protect individuals from baseless claims," and "[t]o minimize number of 'strike suits.'" *Id.*

54. 4 HAZEN, *supra* note 25, at 20-21; O'Riordan, *supra* note 20, at 1601-02. For the Second Circuit, the PSLRA only raised the bar for pleading particularity, not the requirements for pleading the scienter requirement. 3 HAZEN, *supra* note 25, at *22*.

55. Private Securities Litigation Reform Act, 109 Stat. 737 (1995).

56. 4 HAZEN, *supra* note 25, at 30-31. The courts are split on how the particularity requirements affect scienter pleading. *See id.*

. . . [and to] state with particularity facts giving rise to a strong inference that *the defendant* acted with the required state of mind."[57] The purpose of the PSLRA was to curb "shoot first and ask questions later"[58] litigation that had become rampant and economically damaging to corporations.[59] As the Supreme Court stated in *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*,[60] "[t]he 'strong inference' standard 'unequivocally raise[d] the bar for pleading scienter,'"[61] and it was meant to "promote greater uniformity among the Circuits."[62] The purpose of the PSLRA is to clarify the pleading requirements of Section 10(b) lawsuits and to make it harder for a plaintiff to meet the pleading requirements.[63] Congress intended the "strong inference" threshold of the PSLRA to be difficult to satisfy.[64] The Supreme Court has been careful to restrain the private cause of action and maintain heightened pleading requirements.[65]

D. Pleading Under the PSLRA and Corporations as Persons Gave Birth to Collective Scienter

The high PSLRA threshold sparked the collective scienter debate because it raised the threshold for pleading a Rule 10b-5 cause of action that could survive.[66] Basically, a corporation is a single "person" created by legal fiction,[67] but a corporation is a group of individuals that legally act as one entity.[68] A corporation is both one and many, and so the problem is, "how

---

57. Private Securities Litigation Reform Act, 109 Stat. 737, 747 (1995) (emphasis added); 4 HAZEN, *supra* note 25, at 37. The PSLRA basically adopted the Second Circuits view that pleading a "strong inference" of scienter requires pleading facts with particularity. *Id.*

58. O'Riordan, *supra* note 20, at 1614.

59. *Id.* at 1600, 1623 (2007). *See Tellabs, Inc.*, 551 U.S. at 323-24.

60. *Tellabs, Inc.*, 551 U.S. 308.

61. *Id.* at 321 (quoting *Makor*, 437 F.3d at 601).

62. *Id.* (citations omitted); *see* 4 THOMAS LEE HAZEN, TREATISE ON THE LAW OF SECURITIES REGULATION 27 (West Practitioner's Ed. 6th ed. 2009). The PSLRA does not provide specific statutory guidelines as to scienter, and as such, the courts must determine whether the pleading standards have been met on a case-by-case basis. *Id.*

63. O'Riordan, *supra* note 20, at 1623; 4 HAZEN, *supra* note 25, at 37-38.

64. *Id.* at 1623.

65. *See Stoneridge Inv. Partners, LLC*, 552 U.S. at 164-65; *see infra* Section II.E.

66. O'Riordan, *supra* note 20, at 1602.

67. 1 U.S.C. § 1; Burwell v. Hobby Lobby Stores, Inc., 134 U.S. 2751 (2014) (affirming the legal rights of corporations as people in terms of free speech and religious rights); Citizens United v. FEC, 558 U.S. 310 (2010) (affirming a broad conception of corporate personhood); Abril & Olazábal, *supra* note 18, at 84-85; Kircher, *supra* note 19.

68. Abril & Olazábal, *supra* note 18, at 103.

does one properly ascribe intent to a corporation; and . . . [m]ust the imputed corporate action and the imputed corporate intent intersect in one individual actor?"[69] The courts deviate in answering these questions.[70] The issue is further complicated by the modern corporate structure, which makes it hard for a plaintiff to locate a single individual who committed the fraudulent act and also possessed the requisite scienter.[71]

The dual nature of the corporation—entity and aggregate of individuals—affects how the plaintiff must plead scienter.[72] Essentially, whether a corporation is an entity or an aggregate of individuals determines whether a type of respondeat superior liability argument or a collective knowledge theory of liability, like collective scienter, is proper. Under a theory of respondeat superior, a single individual in the corporation must have engaged in the alleged misrepresentation and also possessed the requisite scienter for the purposes of a Section 10(b) action.[73] Respondeat superior liability for a corporation has its roots in common law.[74] Essentially, a corporation is liable for the criminal acts of its agents when they are acting within the scope of their employment.[75]

Some consider respondeat superior type liability both "overinclusive" and "underinclusive."[76] Respondeat superior is overinclusive because a whole corporation can be held liable for the rogue actions of a single criminal agent.[77] Still, the concept of holding a corporation liable for the

---

69. *Id.* at 85; 4 HAZEN, *supra* note 25, at 36.

70. Kircher, *supra* note 19, at 157 n.5; *see infra* Section II.E.

71. Abril & Olazábal, *supra* note 18, at 121; Kircher, *supra* note 19, at 159.

72. There are two views of the corporation that affect pleading corporate scienter. First, under the nominalist view, a corporation is a collective of individuals under the umbrella of the entity corporation. Abril & Olazábal, *supra* note 18, at 103; O'Riordan, *supra* note 20, at 1603. Under this view, a corporation is just an aggregate of individuals. Abril & Olazábal, *supra* note 18, at 103. Second, in contrast, the realists view a corporation as a unique entity apart from the individuals that make it up. *Id.* at 104; O'Riordan, *supra* note 20, at 1603. Realists view corporations as entities that can be held individually liable. Abril & Olazábal, *supra* note 18, at 104; O'Riordan, *supra* note 20, at 1603. Whether a court takes a realist or a nominalist view will affect its approach to collective scienter, because it will either see a corporation as a single entity or an aggregate of many individuals.

73. Abril & Olazábal, *supra* note 18, at 144.

74. Bradley J. Bondi, *Dangerous Liaisons: Collective Scienter in SEC Enforcement Actions*, 6 N.Y.U. J.L. & BUS. 1, 5 (2009).

75. Kircher, *supra* note 19, at 158.

76. Abril & Olazábal, *supra* note 18, at 112; Kircher, *supra* note 19, at 158-59.

77. Abril & Olazábal, *supra* note 18, at 113.

acts of single employee does not seem to be without support.[78] It is underinclusive because respondeat superior requires a single culpable actor to possess the requisite scienter, and it is often very difficult, given the modern corporate structure, to identify a single culpable actor.[79]

It is this underinclusion that propagated the collective knowledge theories as a way to solve the single actor difficulty under respondeat superior, and as such, collective scienter is an inherently expansive theory of liability. Under a collective knowledge theory, the scienter of one individual employee may intersect with the act of representation by another individual employee who did not possess scienter for the purposes of imputing liability to the corporation.[80] In this way, a collective knowledge theory aggregates the knowledge and states of mind of the individuals that make up the corporation so that the whole corporation possesses the requisite scienter to satisfy the PSLRA.[81] The purpose is to remedy the underinclusion problem of respondeat superior by allowing the elements of a Section 10(b) cause of action to intersect in more than one individual.[82]

While collective knowledge theories address the underinclusion problem, they do little to solve the overinclusion problem. Under collective knowledge theories, a plaintiff can avoid the single culpable defendant issue, but the door is still left open for a single rogue actor producing false information that is then published down the line by an unwitting employee or officer of the corporation. Because collective scienter is an expansive theory of liability, it is contrary to the purpose of the PSLRA.[83]

E. Supreme Court Guidance on Collective Scienter and Section 10(b)

The Supreme Court cultivated a proverbial "judicial oak" tree out of the "congressional acorn" of Section 10(b) and Rule 10b-5.[84] Consider the following cases. It will become clear that the Supreme Court strictly limits

---

78. The massive corporate conglomerate, Exxon Mobile, was held liable to the tune of billions of dollars because of the actions of single drunk tanker captain. Exxon Shipping Co. v. Baker, 554 U.S. 471 (2008).

79. Abril & Olazábal, *supra* note 18, at 113 .

80. Abril & Olazábal, *supra* note 18, at 115-16; *see* Private Securities Litigation Reform Act, 109 Stat. 737, 746-47 (1995).

81. *See* Private Securities Litigation Reform Act, 109 Stat. 737, 746-47 (1995).

82. O'Riordan, *supra* note 20, at 1605.

83. *See supra* Section II.C. Some argue that the collective knowledge theories are incompatible with the PSLRA. *See* O'Riordan, *supra* note 20, at 1623.

84. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 737 (1975).

the Section 10(b) cause of action and maintains the difficulty of pleading a survivable cause of action.

1. *Stoneridge*

In *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*,[85] the Supreme Court explored the reach of the Section 10(b) private cause of action[86] in the context of a scheme produced by Charter Communications, Inc., to fraudulently manipulate its quarterly reports to meet market analyst expectations.[87] Stoneridge Investment Partners, LLC, led this class action because of the affect the scheme had on Charter's stock price.[88] The question before the Court was the liability of two corporations, Scientific-Atlanta, Inc., and Motorola, Inc., who participated in Charter's scheme.[89]

The scheme went like this: Charter was set to miss its projected operating cash flows by millions of dollars.[90] In order to make up this difference and meet expectations, Charter re-contracted with Motorola and Scientific-Atlanta to purchase certain digital cable converter boxes for twenty dollars more than usual price.[91] In consideration, Motorola and Scientific-Atlanta would overpay for advertising provided by Charter, and in this way, the deal "had no economic substance."[92] The rub was that Charter was able to meet its earnings expectations by capitalizing the excessive costs of purchasing the converter boxes and increasing its revenues because of the additional advertising bought by Motorola and Scientific-Atlanta, but this scheme violated GAAP principles.[93] Motorola and Scientific-Atlanta agreed to the scheme,[94] but did not participate in "preparing or disseminating Charter's financial statements."[95] The Supreme Court granted certiorari to decide "when, if ever, 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)."[96]

---

85. Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc., 552 U.S. 148 (2008).

86. *Id.* at 152.

87. *Id.* at 152-53.

88. *Id.* at 152.

89. *Id.* at 153.

90. *Id.* at 153.

91. *Stoneridge Inv. Partners, LLC*, 552 U.S. at 154.

92. *Id.* at 154-55.

93. *Id.* at 154.

94. *Id.*

95. *Id.* at 155; *see supra* Section II.E.3.

96. *Id.* at 156.

The Court quoted the language of both Section 10(b) and Rule 10b-5, and clarified that "Rule 10b-5 encompasses only conduct already prohibited by § 10(b)."[97] The Court then described the existence of the Section 10(b) private cause of action and its six elements.[98] The Court noted a previous holding,[99] and stated that "[t]he § 10(b) implied private right of action does not extend to aiders and abettors. The conduct of a secondary actor must satisfy each of the elements or preconditions for liability; and we consider whether the allegations here are sufficient to do so."[100]

The Court held that the plaintiff did not show that it relied on the acts or statements of Motorola and Scientific-Atlanta.[101] The Court engaged in the three-tiered analysis: First, the plaintiff must demonstrate that it relied on the deceptive acts of the defendants.[102] This plaintiff could not demonstrate that, because the defendants did not communicate their deceptive acts to the public or investors.[103] Without knowledge of the acts, the plaintiff could not rely on them.[104] Second, the Court rejected the concept of "scheme liability," because if plaintiffs were able to rely not only on disseminated misstatements, but also on the transactions the statements reflect, the effect "would reach the whole marketplace in which the issuing company does business."[105] This the Court would not allow.[106]

Essentially, a Section 10(b) private cause of action "does not reach all commercial transactions that are fraudulent and affect the price of a security in some attenuated way."[107] This limitation on liability supports the

---

97. *Stoneridge Inv. Partners, LLC*, 552 U.S. at 156-57.

98. *Id.* at 157 (citing Superintendent of Ins. of New York v. Bankers Life & Casualty Co., 404 U.S. 6, 13 n.9 (1971)); *see supra* Section II.D.

99. Cent. Bank, N.A. v. First Interstate Bank, N.A., 511 U.S. 164, 180 (1994).

100. *Stoneridge Inv. Partners, LLC.*, 552 U.S. at 158; 3 THOMAS LEE HAZEN, TREATISE ON THE LAW OF SECURITIES REGULATION 507-08, 507 n.5 (West Practitioner's Ed. 6th ed. 2009) (citing Central Bank of Denver v. First Interstate Bank of Denver, 511 U.S. 164 (1994) (holding that there is no implied remedy for aiders and abettors)).

101. *Stoneridge Inv. Partners, LLC*, 552 U.S. at 158-59.

102. *Id.* at 159.

103. *Id.*

104. *Id.*

105. *Id.* at 159-60.

106. *Id.* 160.The Court held that the "in connection with" language of § 10(b) does not extend so far as to include the defendants in this case. *Id.* at 160-61. State law governs the "realm of financing business—to purchase and supply contracts." *Id.* at 161. There is not congressional intent that securities law was to provide a "broad federal remedy for all fraud." *Id.* (citing Santa Fe Indus. v. Green, 430 U.S. 462, 479 (1977).

107. *Stoneridge Inv. Partners, LLC*, 552 U.S. at 162.

policy of preventing plaintiffs from "extort[ing] settlements from innocent companies."[108] Third, because the Section 10(b) private cause of action is a judicial construct and it is the duty of Congress to decide the extent of the cause of action, the Court stated that it is careful to restrain the cause of action to prevent the extension of federal regulation without congressional intent.[109] The heightened pleading requirements support the fact that Congress intended the Section 10(b) cause of action to be restrained.[110]

The Court finished its analysis by noting that the SEC enforcement power is not without teeth[111] and that some secondary actors like accountants and underwriters can be held liable under certain circumstances.[112] Because the acts of Motorola and Scientific-Atlantic were that of suppliers and customers in the marketplace of goods and services, not investment securities, the Court held that the defendants were not liable to the plaintiffs.[113] The plaintiffs cannot hold suppliers and customers liable for the financial statements of another company when they have no control over preparing its financial statements and disclosures under Section 10(b).[114] The Supreme Court affirmed the dismissal of the Motorola and Scientific-Atlantic by the Eighth Circuit Court of Appeals.[115]

Ultimately, *Stoneridge* stands for the proposition that a plaintiff must show reliance on the acts and statements of the defendant in a survivable Section 10(b) cause of action. Furthermore, it demonstrated the Supreme Court's unwillingness to extend corporate liability under securities regulation without congressional intent. *Stoneridge* shows the limitation on the liability of participating actors who are not responsible for disclosures to the public. Accordingly, participating actors like Motorola are not

---

108. *Id.* at 163 (citing *Blue Chip Stamps*, 421 U.S. at 740). In *Blue Chip*, two grounds for support of the public policy against vexatious litigation are given. First, the value of the lawsuit at the pleading and discovery stage may be worth more to the plaintiff than an actual trail where the plaintiff may lose drastically outweighs the value to the defendant corporation who will suffer business disruption purely because of the pending suit. *Blue Chip Stamps*, 421 U.S. at 740. The Court has no interest in allowing "strike suits" by lawyers trying shake down corporations. *Id.* at 740-41 (1975). Second, the *Birnbaum* rule that prevents myriads of lawsuits bought by those who did not buy stock but would have if not for the defendant's conduct protects valid limits on liability. *Id.* at 743-49 (1975); *see* DR. SEUSS, *supra* note 16.

109. *Stoneridge Inv. Partners, LLC.*, 552 U.S. at 164-65.

110. *Id.* at 165.

111. *See* 3 HAZEN, *supra* note 25, at 518-19.

112. *Stoneridge Inv. Partners, LLC*, 552 U.S. at 166.

113. *Id.* at 166-67.

114. *Id.* at 166-67.

115. *Id.* at 153, 167.

responsible for the disclosures made by another corporation even though Motorola was involved in the same fraudulent scheme as Charter. The difference is control.[116]

2. *Makor Issues & Rights Ltd.*

In *Tellabs, Inc. v. Makor Issues & Rights Ltd.*, the Supreme Court provided guidance on pleading a "strong inference" of scienter.[117] The Court held that motive and opportunity to commit fraud are not by themselves dispositive, but are still factors in satisfying heightened pleading requirements.[118] A strong inference of scienter is drawn from many plausible inferences including opposing ones, but in order for the inference of scienter to be strong, it must be "cogent," not merely plausible.[119] Accordingly, "To qualify as 'strong' . . . [the Court] h[e]ld, an inference of scienter must be more than merely plausible or reasonable—it must be cogent and at least as compelling as any opposing inference of nonfraudulent intent."[120] This "at least as compelling" analysis is not a bright line rule; rather it "appears to strike a balance by requiring more than speculative or reasonable inferences but not imposing a requirement for unequivocal allegations of a 'smoking gun.'"[121] Although under this standard the tie goes to the plaintiff,[122] the standard is still quite high because the Court rejected a "more liberal pleading standard."[123]

3. *Janus Capital Group, Inc.*

In *Janus Capital Group, Inc. v. First Derivative Traders*,[124] the Supreme Court provided guidance on what it means for a corporation to "make" a statement pursuant to Rule 10b-5.[125] Simply put, "[o]ne 'makes' a statement

---

116. *Id.* at 166-67.

117. *Tellabs, Inc. v. Makor Issues & Rights Ltd.*, 551 U.S. 308, 313 (2007).

118. *Tellabs, Inc.*, 551 U.S. at 325; *Makor*, 437 F.3d at 601; 4 HAZEN, *supra* note 25, at 28; *see also* Novak v. Kasaks, 216 F.3d 300 (2000).

119. *Tellabs, Inc.*, 551 U.S. at 314; 4 HAZEN, *supra* note 25, at 28.

120. *Tellabs, Inc.*, 551 U.S. at 314; 4 HAZEN, *supra* note 25, at 29.

121. 4 HAZEN, *supra* note 25, at 29 (quoting ACA Financial Guaranty Corp. v. Advest, Inc., 512 F.3d 46, 59 (1st Cir. 2008)); *see also Tellabs, Inc.*, 551 U.S. at 323-24.

122. *Tellabs, Inc.*, 551 U.S. at 330 (Scalia, J., concurring); 4 HAZEN, *supra* note 25, at 30.

123. *Tellabs, Inc.*, 551 U.S. at 328-29. "The presence of inquiry notice or 'red flags' of material misstatements can be the basis for pleading sufficient recklessness to establish scienter." 4 HAZEN, *supra* note 25, at 30 (citing Katz v. Image Innovations Holdings, Inc., 542 F. Supp. 2d 269 (S.D.N.Y. 2008)).

124. Janus Capital Grp., Inc. v. First Derivative Traders, 564 U.S. 135 (2011).

125. 17 C.F.R. § 240.10b-5.

by stating it."[126] The statement maker is the person or entity "with ultimate authority over the statement . . . . Without control, a person or entity can merely suggest what to say, not 'make' a statement in its own right. One who prepares or publishes a statement on behalf of another is not its maker."[127] In other words, the speechwriter does not control the content of the speech; the speaker controls the content of the speech, and, therefore, it is the speaker who takes the blame.[128] The Supreme Court reasoned that its *Janus* rule was supported by its decision in *Stoneridge* where only those with control[129] over the statements, not aiders and abettors, are liable for the statements.[130]

III. COLLECTIVE SCIENTER: OFF THE BEATEN PATH

A. Agency Law Perspective

The most basic form of corporate liability is common law agency. "Agency is the fiduciary relationship that arises when one person (a 'principal') manifests assent to another person (an 'agent') that the agent shall act on the principal's behalf and subject to the principal's control, and the agent manifests assent or otherwise consents so to act."[131] The element of control is the most important element for a discussion on collective

---

126. *Janus Capital Grp., Inc.*, 564 U.S. at 142.

127. *Id.* at 142. Accordingly, "Rule 10b-5's private right of action does not include suits against aiders and abettors." *Id.*

128. *Id.* at140. Some argue that the Supreme Court's holding in *Janus* all but destroys the deterrent effect of Rule 10b-5. *See* Marocco, *supra* note 30, at 634. The author disagrees. He believes that this shows a move by the Supreme Court to putting emphasis on the control part of the liability analysis. *Id.* at 662-63.

129. A discussion involving the interrelatedness of control person liability under 15 U.S.C.S. § 78t(a) would be an interesting comment or note, but such a discussion is beyond the scope of this note. *Janus* briefly discusses control person liability in the context of a wholly owned subsidiary. *Janus Capital Grp., Inc.*, 564 U.S. at 141 n.5. All that is necessary for this Note is that a plaintiff states a claim against the controlled entity in order to hold the defendant liable as a control person. *Id.*; *see Liability of Brokerage Firm, Securities Underwriter, Investment Advisor, or Similar Entity, or Individual Affiliated with Such Entity, as "Control Person" Under § 15 of Securities Act (15 U.S.C.A. § 77o) and § 20(a) of Securities Exchange Act (15 U.S.C.A. § 78t(a))*, 186 A.L.R. FED. 169 (2003).

130. *Janus Capital Grp., Inc.*, 564 U.S. at 143-44; *Stoneridge Inv. Partners, LLC.*, 552 U.S. at 152-53.

131. RESTATEMENT (THIRD) OF AGENCY § 1.01 (AM. LAW INST. 2006); *see also* RESTATEMENT (SECOND) OF AGENCY § 1 (AM. LAW INST. 1958); RESTATEMENT (FIRST) OF AGENCY § 1 (AM. LAW INST. 1933).

scienter.[132] Accordingly, the pleading analysis under the PLSRA should be demarcated such that only those in control are held liable for fraud.

While the Supreme Court does not graft all common law principles into Section 10(b), it appears clear that the Court considers the doctrine of respondeat superior integral to understanding Section 10(b).[133] Under respondeat superior, it is not so much apparent[134] or actual[135] authority of the agent as it is the employment relationship between principal and agent that produces liability.[136] The principal's liability depends on whether the employee acted within the scope of their employment.[137] The resulting liability is both vicarious and strict in the sense that the employer did nothing wrong but is still liable. Judge Learned Hand described the respondeat superior based corporate liability as "imput[ing] to the corporation . . . the mental condition of its agents."[138] In the context of corporate liability, imputation encourages a corporate employer to structure itself for efficient control of employees and communication channels between principal and agent.[139]

---

132. *See supra.* Section II.E.

133. *Makor*, 513 F.3d at 708 (citing AT&T v. Winback & Conserve Program, Inc., 42 F.3d 1421, 1429-33 (3d Cir. 1994)). Common law agency spawned the theory of respondeat superior. Bondi, *supra* note 74, at 5.

134. RESTATEMENT (THIRD) OF AGENCY § 2.01-2.02 (AM. LAW INST. 2006).

135. *Id.* § 2.03.

136. Bondi, *supra* note 74, at 5.

137. *Id.* at 5; RESTATEMENT (THIRD) OF AGENCY § 2.04 (AM. LAW INST. 2006).

138. United States v. Nearing, 252 F. 223, 231 (S.D.N.Y.1918).

139. RESTATEMENT (THIRD) OF AGENCY § 5.03 cmt. b (AM. LAW INST. 2006).

> Imputation charges a principal with the legal consequences of having notice of a material fact, whether or not such fact would be useful and welcome. If an agent has actual knowledge of a fact, the principal is charged with the legal consequences of having actual knowledge of the fact. If the agent has reason to know a fact, the principal is charged with the legal consequences of having reason to know the fact. A principal may not rebut the imputation of a material fact that an agent knows or has reason to know by establishing that the principal instructed the agent not to communicate such a fact to the principal. Imputation thus reduces the risk that a principal may deploy agents as a shield against the legal consequences of facts the principal would prefer not to know.

Id. Restatement (Third) of Agency provides guidance for determining when information is imputed or attributed to the principal of an agent. *Id.* §§ 1.04(4), 5.01-5.04. Essentially, when an agent receives a notification of a fact, it is the same as the principal receiving notification of a fact. *Id.* §§ 5.01-5.04. The notification is imputed to the principal, and, in this way, the principal can be held liable for the knowledge of the agent. *Id.* The principal is not free of liability just because the agent kept silent. *Id.* § 5.01 cmt. b.

Respondeat superior provides a sufficient and effective legal standard for holding a corporation liable for the fraudulent actions of its employees. Collective scienter goes too far beyond the analysis of respondeat superior by losing the focus on the control exercised by the corporation.[140]

B. Securities Exchange Commission Perspective

Some argue that the SEC's use of collective scienter is inadvisable.[141] If the SEC's use of collective scienter is suboptimal, then its use by the circuits is called into question because the policy issues are much the same. The SEC rarely charges a corporation for fraud without charging individuals in the corporation as well.[142] The SEC predisposition against collective scienter when charging corporations is affirmed by most circuit courts not using collective scienter.[143]

Even if collective scienter were widely accepted, it is suboptimal for the SEC to use collective scienter for several policy reasons. First, the distinction between the negligence standard of Section 17(a)(2) and (3) and "intentional or reckless" standards of Section 10(b) and Section 17(a)(1) would be conflated.[144] The distinction of the 1934 Act's many standards would be irrelevant if Section 10(b) were extended by collective scienter.[145] Second, the purpose of the 1934 Act and the PSLRA—to promote a corporate environment of voluntary disclosure—would be impaired because in order to avoid liability under collective scienter every employee of a corporation would have to be interviewed before any disclosure could be made. Even then, an unknown misstatement could still spark liability.[146]

Third, the central tenant of the SEC is deterring corporations from committing fraud.[147] Effective deterrence only occurs when the principal has control over the agent with knowledge.[148] Because a corporation must

---

140. S*ee Stoneridge Inv. Partners, LLC*, 552 U.S. at 166-67; RESTATEMENT (THIRD) OF AGENCY § 1.01 (AM. LAW INST. 2006); RESTATEMENT (SECOND) OF AGENCY § 1 (AM. LAW INST. 1958); RESTATEMENT (FIRST) OF AGENCY § 1 (AM. LAW INST. 1933); *see supra* Sections II.E.1, II.E.3.

141. Bondi, *supra* note 74, at 17, 30-31.

142. *Id.* at 15-16.

143. *Id.* at 16.

144. *Id.* at 18-20; *see Ernst*, 425 U.S. at 199 (1976).

145. Bondi, *supra* note 74, at 18-20.

146. *Id.* at 21-23; *see supra* Section II.C.

147. Bondi, *supra* note 74, at 24.

148. *Stoneridge Inv. Partners, LLC*, 552 U.S. at 166-67; Bondi, *supra* note 74, at 24; RESTATEMENT (THIRD) OF AGENCY § 1.01 (AM. LAW INST. 2006); RESTATEMENT (SECOND) OF

make disclosures to comport with SEC requirements, a corporate officer would have to interview every employee with knowledge to prevent any misstatement and imputation of scienter of an employee who had knowledge of the misstatement.[149] A corporation and the SEC are not well suited to find the knowledgeable person without exorbitant costs, and therefore, deterrence becomes ineffective due to the weight of impracticality.[150] If the SEC and a corporation cannot do it, how can a court know which people to look for? Fourth, SEC enforcement would become unpredictable under collective scienter, and corporations would lack remedial steps to solve potential problems.[151] Furthermore, penalties sought by the SEC under the 1934 Act would be even more uncertain than they are now, and without even the current level of certainty, the effectiveness of the Act's deterrence would wane.[152] As Bradley Bondi concludes: "The theory of collective scienter is a radical departure from the principles of corporate liability and runs contrary to the objectives of the federal securities laws."[153]

IV. CIRCUIT SPLIT OVERVIEW

The circuits are generally split into two camps: respondeat superior and collective scienter. The Fifth, Seventh, Ninth, and Eleventh Circuits adhere to a type of common law respondeat superior analysis that has evolved due to the PSLRA language.[154] While not rejecting collective scienter per se, the Second Circuit falls into the respondeat superior camp by rejecting collective scienter as a matter of focus.[155] The focus should be on whether

---

AGENCY § 1 (AM. LAW INST. 1958); RESTATEMENT (FIRST) OF AGENCY § 1 (AM. LAW INST. 1933); *see supra* Sections II.E.1, II.E.3.

149. Bondi, *supra* note 74, at 25.

150. *Id.* at 26.

151. *Id.* at 28-30.

152. *Id.*

153. *Id.* at 30.

154. *See supra* Part II; Section IV.A.

155. Some of these circuits arguably fit under collective scienter camp as well, but if one thinks of the two camps, respondeat superior and collective scienter, as a Venn diagram, the larger circle would be respondeat superior and the smaller circle, collective scienter. The overlap by the respondeat superior is minimal because of the focus on whether or not there was a serious inference of scienter. The author places the middle ground courts in the respondeat superior as a matter of focus. Some author's hand this distinction by using the term "semi-strong-form corporate scienter." Paul B. Maslo, *The Case for Semi-Strong-Form Corporate Scienter in Securities Fraud Actions*, 108 MICH. L. REV. FIRST IMPRESSIONS 95, 99-101 (2010). Malso writes,

the plaintiff pleaded a strong inference of scienter,[156] and this does not require that the plaintiff identify specific individuals in every case.[157] Some respondeat superior circuits—the Fifth and Eleventh Circuits—reject collective scienter outright.[158] The collective scienter camp contains only the Sixth Circuit.

A. RESPONDEAT SUPERIOR CIRCUITS

The respondeat superior[159] circuits reject collective scienter and require a nexus of scienter and misstatement making that resides in a single individual defendant within the defendant corporation.[160]

1. Fifth and Eleventh Circuits

The Fifth Circuit rejected collective scienter in *Southland Sec. Corp. v. Inspire Ins. Sols., Inc.*[161] The court held that

> "for purposes of determining whether a statement made by the corporation was made by it with requisite Rule 10(b) scienter we believe it appropriate to look to the state of mind of the individual corporate official or officials who make or issue the statement . . . rather than generally to the collective knowledge of all the corporation's officers and employees acquired in the course of their employment."[162]

In *Phillips v. Scientific-Atlanta, Inc.*, the Eleventh Circuit held that "scienter must be found with respect to each defendant and with respect to

---

> Rather than requiring a company to undertake the nearly impossible task of synthesizing the knowledge of its agents prior to making a public statement, semi-strong-form scienter simply requires those executives responsible for the statement to ensure the statement does not contain information that contradicts what they know to be true. This is a reasonable expectation.

Id. at 100.

156. *Makor*, 513 F.3d at 702, 705.

157. *See infra* Section IV.A.2.

158. *See infra* Section IV.A.3.

159. *See supra* Section III.A.

160. In Re Omnicare, Inc. Sec. Litig., 769 F.3d 455, 473-74 (6th Cir. 2014).

161. Southland Sec. Corp. v. Inspire Ins. Sols., Inc., 365 F.3d 353, 366 (5th Cir. 2004) (quoting Nordstrom, Inc. v. Chubb & Son, Inc., 54 F.3d 1424, 1435 (9th Cir. 1995)); *see In Re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 474.

162. *Southland Sec. Corp.*, 365 F.3d at 366 (citing Nordstrom, Inc. v. Chubb & Son, Inc., 54 F.3d 1424, 1435 (9th Cir. 1995); In Re Apple Computer, Inc. Sec. Litig., 243 F. Supp. 2d 1012, 1023 (N.D. Cal. 2002)) (emphasis added).

each alleged violation of the statute."[163] Its reasoning was primarily based on the language of the PSLRA, which requires alleging particular facts against *the defendant*, not *defendants*.[164] The Fifth and Eleventh Circuits held to common law respondeat superior by looking for a singular individual defendant within the corporate body and refusing to look further.[165]

2. Seventh and Ninth Circuits

Several circuits took a middle ground by allowing collective scienter, but only under certain obvious circumstances.[166] With the middle ground circuits, the focus still rested on respondeat superior analysis and whether or not the plaintiff pled a strong inference of scienter. The Seventh Circuit held that it is not necessary to name the individuals in the corporation who committed the fraud in order to plead a strong inference of corporate scienter.[167] The Seventh Circuit then described such a situation:

> "Suppose General Motors announced that it had sold one million SUVs in 2006, and the actual number was zero. There would be a strong inference of corporate scienter, since so dramatic an announcement would have been approved by corporate officials sufficiently knowledgeable about the company to know that the announcement was false."[168]

While the Seventh Circuit did not reject collective scienter, the emphasis was on pleading a strong inference of corporate scienter, not on collective scienter.[169]

In *Glazer Capital Mgmt., LP v. Magistri*,[170] the Ninth Circuit[171] reiterated that, even though it had not previously adopted collective scienter, it also had not categorically rejected it.[172] In accordance with the Seventh Circuit and the Second Circuit, the Ninth Circuit pointed to the hypothetical case in *Makor*.[173]

---

163. Phillips v. Scientific-Atlanta, Inc., 374 F.3d 1015, 1017-18 (11th Cir. 2004).

164. *Id.* at 1018; *see* 15 U.S.C. § 78u-4(b)(2) (2010).

165. *See supra* Section IV.A.1.

166. *In Re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 474.

167. *Makor*, 513 F.3d at 710.

168. *Id.*

169. *Id.* at 710-11.

170. Glazer Capital Mgmt., LP v. Magistri, 549 F.3d 736 (9th Cir. 2008).

171. *In Re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 475.

172. *Glazer Capital Mgmt., LP*, 549 F.3d at 744.

173. *See Makor*, 513 F.3d at 710.

3. Second Circuit[174]

In *Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital, Inc.*,[175] the Second Circuit joined the respondeat superior camp, but maintained a slight caveat.[176] The Second Circuit clarified its position by stating, "Although there are circumstances in which a plaintiff may plead the requisite scienter against a corporate defendant without successfully pleading scienter against a specifically named individual defendant, the plaintiff here has failed to do so."[177] The Second Circuit rejected the defendant's argument that the plaintiff failed as a matter of law to plead scienter against the defendant.[178] Holding to a dismissal analysis focusing on the "strong inference" language of the PSLRA, [179] the Second Circuit would not go so far as to say that corporate scienter requires the identification of an expressly named officer.[180] The PSLRA required dismissal of the complaint because the competing inferences regarding scienter did not rise to the level showing that scienter was "'at least as compelling' as the competing inference."[181] The court inferred that the statements were not misleading or merely the result of negligence.[182] Raising an inference of scienter requires more than simply alleging that the defendant was negligent in reviewing or checking information;[183] the plaintiff must identify specific "reports or statements that would have come to light in a reasonable investigation and that would have demonstrated the falsity of the allegedly misleading statements."[184]

The Second Circuit adhered to the Seventh Circuit's language referenced above.[185] Seemingly following a similar version of respondeat superior, the Second Circuit agreed with the Seventh Circuit that naming a specific individual defendant is not always required, but it generally would be.[186] But

---

174. *See Phillips*, 374 F.3d at 1017-18.

175. Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital, Inc., 531 F.3d 190 (2d Cir. 2008).

176. *In Re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 474-75.

177. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 192.

178. *Id.* at 196.

179. *Id.*

180. *Id.*

181. *Id.* at 197.

182. *Id.* at 197.

183. *See supra* Section II.E.

184. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 196.

185. *Makor*, 513 F.3d at 710.

186. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 195-96.

there are circumstances where drawing a strong inference of corporate scienter makes sense because of the nature of the statement itself and nature of the corporate structure where high-level corporate officials would know the falsity of the statement.[187]

The Second Circuit does not reject corporate scienter or collective scienter.[188] It merely describes the standard of strong inference as enough and avoids the collective scienter discussion of how the plaintiff could plead scienter of various individual employees as a matter of emphasis.[189] The Second Circuit held that the PSLRA required the dismissal of the complaint, but remanded the case because the district court granted the plaintiff leave to replead.[190] As one can see, the Second Circuit's application of PSLRA maintains a high pleading standard while maintaining a focus on the strong inference language to the exclusion of the collective scienter language.

B. Analysis of Respondeat Superior Circuits

The primary critique of a respondeat superior theory of liability under Section 10(b) and Rule 10b-5 is that it appears underinclusive in terms of holding corporations liable for their fraud under Section 10(b) and Rule 10b-5.[191] Collective scienter supposedly steps in to solve this problem.[192] Respondeat superior is deemed underinclusive because it usually requires an individual culpable actor to possess the requisite scienter; this is very difficult, given complicated modern corporate structures, to identify a single culpable actor.[193] But as described in the previous section, this is not always the case.[194]

---

187. *Id.*; *Makor*, 513 F.3d at 710.

188. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 196 ("[W]e do not believe they have imposed the rule urged by defendants, that in no case can corporate scienter be pleaded in the absence of successfully pleading scienter as to an expressly named officer.").

189. *Id.* at 197.

190. *Id.*

191. Kircher, *supra* note 19, at 158-59; Abril, *supra* note 18, at 112. Some even argue that respondeat superior type liability is also overinclusive because a single culpable individual defendant can create liability for an entire corporation. *Id.* at 113. American jurisprudence does not appear offended by this overinclusion. Exxon Shipping Co. v. Baker, 554 U.S. 471 (2008); *see supra* Section III.A.

192. *See supra* Section II.D.

193. Abril, *supra* note 18, at 113-14 (2006); *see* Bondi, *supra* note 74, at 7; *see* Kircher, *supra* note 19, at 158-59.

194. *See supra* Section IV.A.

The underinclusive critique forgets congressional intent circumscribing any relative ease of pleading a cause of action under Section 10(b) and Rule 10b-5.[195] The purpose of the PSLRA was to limit litigation rather than make it easier to create.[196] The "strong inference" language makes it intentionally more challenging for fraud actions to survive the pleadings standard.[197] In sum, the argument that collective scienter can help solve the underinclusion problem forgets congressional intent. Furthermore, the argument that a respondeat superior theory of liability is more underinclusive than a collective scienter theory goes against the reality of the decisions made by the collective scienter Sixth Circuit.[198] It appears that even under collective scienter the plaintiff will not survive pleading.[199] Collective scienter appears inadequate at solving the underinclusion created by a respondeat superior theory, and is thus ineffective at its intended purpose.

The underinclusion critique relies on the respondeat superior requirement of locating an individual agent within the principal corporation, and in this manner, the scienter of the agent is imputed to the corporation.[200] This requirement does not actually create an underinclusion problem under the PSLRA. Several respondeat superior courts avoid potential underinclusion by looking to the "strong inference" language of the PSLRA.[201] Essentially, an individual named officer or agent of a corporation is not needed for the type of liability prescribed by the PSLRA.[202] When the nature of the statement is such that the corporate officials would know it to be false, (e.g. General Motors announcing it sold millions of cars when it sold none)[203] then it makes sense to hold the

---

195. *See supra* Section II.D.

196. O'Riordan, *supra* note 20, at 1600, 1614; s*ee* Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 323-24 (2007).

197. Private Securities Litigation Reform Act, 109 Stat. 737, 746-47 (1995) (emphasis added); *Tellabs, Inc*., 551 U.S. at 321-22; 4 HAZEN, *supra* note 25, at 27, 37.

198. *Bondali*, 620 F. App'x at 493; *In Re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 484; *Cf.* City of Monroe Emps. Ret. Sys. v. Bridgestone Corp., 399 F.3d 651 (6th Cir. 2005). The Sixth Circuit quickly stepped away from its stronger collective scienter position in *City of Monroe*. *In Re Omnicare, Inc. Sec. Litig*., 769 F.3d at 475-76.

199. *Bondali*, 620 F. App'x at 493; *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 484.

200. *See supra* Section II.D.

201. *See supra* Section IV.A; *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 195-96; *Makor*, 513 F.3d at 710.

202. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 195-96; *Makor*, 513 F.3d at 710.

203. *Id.*

corporation liable for the misstatement.[204] Because of the prominence of the announcement, imputing the scienter of the corporate officers to the corporation is simple because the officers must have known of the statement and its falsity.[205]

The Supreme Court's focus on the control aspect of whether a corporation can be held liable justifies any potential for underinclusion by a respondeat superior theory.[206] The Supreme Court's focus on control parses nicely with the strong inference standard.[207] Couching the General Motors analogy in terms of control brings this point out.[208] An announcement alleging the production of millions of cars when none were produced is obviously within the control of the corporation and its corporate officers. Basically, the strong inference language translates into what can practically be controlled. Not every employee can be interviewed before every announcement because this is practically beyond the control of the corporation and its officers. But requiring a corporation to interview certain employees before certain announcements makes sense because this is within the conceivable corporate sphere of control.[209]

Under this strong inference focus, rather than collective scienter, corporate scienter can be pled against a defendant corporation while maintaining congressional intent that Section 10(b) causes of action be circumscribed.[210] While liability is limited in the sense that the plaintiff may not survive pleading, it is purposefully limited. Therefore, the respondeat superior theory is not underinclusive, but rather comports with the limiting nature of the PSLRA.

C. Collective scienter Sixth Circuit

1. *Monroe* and *Omnicare*

In *City of Monroe Emps. Ret. Sys. v. Bridgestone Corp.*, the Sixth Circuit took a stand closer to pure collective scienter than the other circuits by

---

204. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 195-96; *Makor*, 513 F.3d at 710.

205. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 195-96; *Makor*, 513 F.3d at 710.

206. S*ee supra* notes 114, 116, 131, 132, 148 and accompanying text; *see supra* Sections II.E.1, II.E.3, III.A.

207. *See supra* Sections II.E.1, II.E.3

208. *See infra* note 211.

209. S*ee supra* notes 114, 116, 131, 132, 148 and accompanying text; *see supra* Sections II.E.1, II.E.3, III.A.

210. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 195.

allowing the knowledge of an officer who did not issue the false statement to be imputed to the corporation.[211] In *Monroe*, the CEO of the defendant corporation knew of actionable[212] misleading statements, and the Sixth Circuit held that the CEO's knowledge could be imputed to the corporation even though the CEO did not himself issue the statements.[213] In essence, the Sixth Circuit adopted pure collective scienter and strayed from common law respondeat superior.[214] The Sixth Circuit allowed the plaintiff's claim to survive pleading and proceed.[215]

In 2014, the Sixth Circuit embarked on a more qualified approach to collective scienter theory in *KBC Asset Mgmt. N.V. v. Omnicare, Inc.*[216] First, the Sixth Circuit labeled neither the *Southland* nor *Monroe* approaches as perfect.[217] The respondeat superior type approach in *Southland* ran contrary to the purpose of the 1934 Act of promoting full voluntary disclosure by the corporation.[218] Where the court requires a single culpable actor, the corporation may avoid liability for culpable actions by conscious ignorance.[219] The Sixth Circuit then stepped back from its decision in *Monroe* because it thought such a broad expectance of collective scienter "could expose corporations to liability far beyond what Congress has authorized."[220] Basically, the corporation could be held liable because some low-level employee, possibly from another country, knew the statement made by the corporation was false or misleading; this broad liability is contrary to the PSLRA.[221]

---

211. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 474; *City of Monroe Emps. Ret. Sys.*, 399 F.3d at 688-90.

212. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 474; *City of Monroe Emps. Ret. Sys.*, 399 F.3d at 680-01.

213. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 474; *City of Monroe Emps. Ret. Sys.*, 399 F.3d at 688-89.

214. *See supra* Section III.A.

215. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 474; *City of Monroe Emps. Ret. Sys.*, 399 F.3d at 688-90 (citing Adams v. Kinder-Morgan, Inc., 340 F.3d 1083, 1106 (10th Cir. 2003)).

216. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 455.

217. *Id.* at 475.

218. *Id.* (citing Heather F. Crow, *Riding the Fence on Collective Scienter: Allowing Plaintiffs to Clear the PSLRA Pleading Hurdle,* 71 LA. L. REV. 313, 317 (2010)).

219. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 475 (citing Abril & Olazábal, *supra* note 18, at 113-14; Craig L. Griffin, Note, *Corporate Scienter Under the Securities Exchange Act of 1934*, 1989 BYU L. REV. 1227, 1244).

220. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 475.

221. *Id.* at 475-76 (citing O'Riordan, *supra* note 20, at 1613-14; *see supra* Section II.D.

The Sixth Circuit then adopted a middle ground to collective scienter somewhere between *Southland* and *Monroe*.[222] Word for word, the Sixth Circuit embraced a rule prescribed by Patricia Abril and Ann Olazábal in the *Locus of Corporate Scienter*, as follows:[223]

The individual agent who uttered or issued the misrepresentation;

> b. Any individual agent who authorized, requested, commanded, furnished information for, prepared (including suggesting or contributing language for inclusion therein or omission therefrom), reviewed, or approved the statement in which the misrepresentation was made before its utterance or issuance;
> c. Any high managerial agent or member of the board of directors who ratified, recklessly disregarded, or tolerated the misrepresentation after its utterance or issuance . . . .[224]

The Sixth Circuit found that: first, the rule consisted with the precedent set by *Monroe* because the knowledge of the CEO would still be imputed to the corporation under the new rule.[225] Second, the rule prevents corporations from evading liability through the willful ignorance that was supposedly allowed under respondeat superior approaches.[226] The rule would prevent corporations from shielding management from bad news from lower level employees.[227] Third, the Sixth Circuit held that the rule would protect corporations from liability that would otherwise exist under *Monroe*.[228] Under the new rule, the courts would only look to the "states of mind of lower-level employees connected to the statements," not to just any employee.[229]

Pursuant the new rule, the Sixth Circuit held that the knowledge of single employee because the employee "furnished information for" and "reviewed" the statement that was the basis for the misrepresentation by the corporation.[230] Still, even though the employee's knowledge could be imputed, the Sixth Circuit still held that the plaintiff did not plead enough

---

222. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 476.

223. Abril & Olazábal, *supra* note 20, at 135.

224. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 476-77 (2014); Abril & Olazábal, *supra* note 18, at 135.

225. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 477.

226. *Id.*

227. *Id.*

228. *Id.*

229. *Id.*

230. *Id.* at 483.

facts to show a strong inference of scienter by the corporation.[231] There was no strong inference because the plaintiff did not allege enough facts "that a reasonable jury could find a divergence between internal reports (the audits) and external statements (the Form 10-K statements)."[232] There was a large time gap between the alleged misstatement and disclosures to the market by the corporation; the disclosures were not made in the shadow of litigation; and the plaintiff did not plead enough facts to show motive of why the defendant would mislead the public.[233] The Sixth Circuit dismissed the suit for lack of a strong inference, despite the finding of imputed knowledge via collective scienter.[234] Essentially, the importance of the strong inference language superseded any utility of collective scienter.

2. *Bondali*

Bondali v. Yum! Brands, Inc.[235] demonstrates further the picayune utility of collective scienter. *Bondali* demonstrates both the complexity and difficulty of pleading a Section 10(b) cause of action, but it also shows the lack of consistency and continuity in the rationale of pleading a survivable Section 10(b) cause of action under collective scienter. In the end, collective scienter proves little help, and a respondeat superior type analysis could have reached the same conclusion.

Between 2010 and 2011, Yum! Brands Inc. ("Yum"), the owner of Taco Bell and Kentucky Fried Chicken ("KFC"), learned through a series of tests performed by the Shanghai Institute for Food and Drug Control ("SIFDC") that three of its Chinese KFC chicken suppliers[236] had "tested positive for drug and antibiotic residues" prohibited under Chinese law.[237] Yum then disqualified the two suppliers, Shandong Luihe Group ("Luihe") and its subsidiary, the Linyi Factor ("Linyi"), in August 2012 and 2011 respectively.[238] Yum did not "immediately disclose the SIFDC results or disqualifications of Liuhe and Linyi to regulators or the public." In late

---

231. *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d at 483 (quoting Abril & Olazábal, *supra* note 18, at 135).

232. *Id.* at 484.

233. *Id.*

234. *Id.*

235. *Bondali*, 620 F. App'x at 483.

236. The suppliers were Shandong Luihe Grp. ("Luihe"), its subsidiary, the Linyi Factor ("Linyi"), and the Yingtai Grp..

Id. at 485.

237. *Id.* SIFDC is "an independent laboratory Yum retained to conduct bimonthly spot testing on the chickens it accepted for distribution to its Chinese KFCs." *Id.*

238. *Id.*

2012, a media firestorm brought the food contamination issues to the public, and Chinese regulators raided several KFC chicken suppliers the following day.[239] Unsurprisingly, Yum stock took a 17% hit by the end of the Class Period.[240] Yum announced that it would not meet its earnings per share growth for 2013 due to a lack of consumer confidence already waning from previous food contamination problems.[241]

A class action suit against Yum was consolidated on May 1, 2013 and stated three counts[242] in its amended complaint.[243] Accordingly, "Count I alleged that Yum violated Section 10(b) of the 1934 Securities Exchange Act, 15 U.S.C. § 78j(b), and SEC Rule 10b-5, 17 C.F.R. § 240.10b-5; Count II alleged Section 10(b) and Rule 10b-5 liability against the individual defendants;" and Count III alleged control person liability under Section 20(a).[244] The defendants included Yum and three senior officers: the CEO David Novak, Richard Carucci, and Jing-Shyh Su.[245] The district court granted a FRCP 12(b)(6) motion to dismiss on all three counts. All three counts were dismissed with prejudice.[246]

In its analysis, before explaining the standard for securities claims that "sound in fraud,"[247] the Sixth Circuit set out a two level standard for de novo review in securities regulation fraud pleading: first, a fraud claim must comport with the particularity requirements of FRCP 9(b),[248] and second, it must meet the escalated "strong inference" particularity requirement of the PSLRA for Section 10(b) or Rule 10b-5 cause of action.[249] Next, the Sixth

---

239. *Bondali*, 620 F. App'x at 485-86.

240. *Id.* The Class Period ended on February 5, 2013, and Yum stock began to decline on November 29, 2012. *Id.* at 486.

241. *Id.* Previous incidents include the Chinese KFC Sudan Red Dye incident and Taco Bell E.coli incidents. *Id.*

242. *Bondali*, 620 F. App'x at 486.

243. *Id.*

244. *Id.* at 484-85.

245. *Id.* at 484-85.

246. *Id.* at 486.

247. *Bondali*, 620 F. App'x at 488. FRCP 9(b) particularity requires "identifying the statements or omissions alleged to be false or misleading and detailing the "who, what, when, where, and how" of the alleged fraud." *Id.* (citing Sanderson v. HCA-The Healthcare Co., 447 F.3d 873, 877 (6th Cir. 2006)).

248. Bondali, 620 F. App'x at 488.

249. *Id.* at 489.

Circuit laid out the elements of a Section 10(b) and Rule 10b-5 cause of action by citing *Stoneridge*.[250]

The court began its analysis with the first *Stoneridge* element, material misrepresentation or omission,[251] and held that the amended complaint was properly dismissed because it did not "assert facts showing Yum's statements were 'objectively false or misleading in light of the information now known.'"[252] First, the court found that the plaintiffs did not allege facts that "Yum *did not* require its suppliers to adhere to corporate food standards and safety protocols,"[253] but rather, the evidence presented showed that "Yum *did* impose" such standards.[254] In short, the court held that just because a few suppliers were breaking the rules does not mean that Yum did not have standards in place, and furthermore, Yum did not guarantee that no supplier would break the rules.[255] Second, Yum did not mislead investors by callings its standards "strict" because Yum did have multiple protocols, spot checks, and systems to find food contamination problems.[256] The plaintiffs could not succeed in showing that Yum misled investors with the word "strict" by merely creating debate as to whether the protocols Yum designed were really "strict" or not.[257] The court qualified that Yum's statement that it would "immediately" pull contaminated food from distribution may be false or misleading because Yum did not immediately pull some contaminated poultry, but the court categorized this statement from the Code of Conduct as an aspiration rather than a statement of objective fact.[258]

Third, Yum's statements to the public in response to negative publicity were not false or misleading because Yum did take the actions it said it

---

250. *Id.* (quoting Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc., 552 U.S. 148, 157 (2008)).

251. *Id.*

252. *Id.* (quoting In re Omnicare, Inc. Sec. Litig., 769 F.3d 455, 478 (6th Cir. 2014)). The alleged material false or misleading statements included: Earnings Announcements and 10-Qs that made cautionary statements or risk disclosures; Yum's 2011 Form 10-K, Yum's Code of Conduct, and a March 2012 investor conference that touted that Yum had strict food standards and protocols; promises to undertake actions to protect consumers in response to negative publicity; and attributing decreasing same-store sales to softer sales rather than to negative publicity. *Bondali*, 620 F. App'x at 468-88.

253. *Id.* at 489.

254. *Id.*

255. *Id.*

256. *Id.* at 490.

257. *Id.*

258. *Bondali*, 620 F. App'x at 490.

would take in the statements.[259] Fourth, Yum's risk disclosure statements were not false or misleading merely because a statement of risk that should have said certain safety problems *are* happening rather than *may* happen.[260] If the prospective statements were considered false or misleading, it could change the nature of prospective statements, like 10-Qs, that educate investors on elements of possible risk.[261] Furthermore, the plaintiffs did not show that problems with Luihe and Tangtai would cause financial loss to Yum, and without such a showing, there is not demonstration that an investment risk had materialized.[262] Lastly, the court gave "little fanfare" to Yum's statement on softer sales because it did say that the projections would be lower.[263] Ultimately, the court would not allow construing facts in the light most favorable to the plaintiff to mean that it must speculate the existence of facts that would favor the plaintiff.[264]

The court next addressed the scienter element of a Section 10(b) cause of action, and affirmed the district court in holding that the plaintiffs did not allege a strong inference of scienter.[265] The plaintiffs alleged four facts to establish scienter: that "KFC China [was] the 'core' of Yum's business;"[266] that Su made statements in response to negative publicity;[267] that individual officers "paid close attention to food safety;"[268] and that individual officers "had reason not to disclose the SIFDC results because doing so would have harmed Yum's financial bottom line and, in turn, their own performance-based compensation."[269] Although these facts may establish that the individual officers had motive and opportunity to commit fraud, this is not sufficient; the plaintiffs must plead scienter "by alleging facts giving rise to a strong inference of recklessness."[270] The court highlighted the dispute of

259. *Id.*

260. *Id.* at 490-91 (citing In re FBR, Inc. Sec. Litig., 544 F. Supp. 2d 346, 362 (S.D.N.Y. 2008)).

261. *Id.*

262. *Id.* at 490-91.

263. *Id.* at 491.

264. *Bondali*, 620 F. App'x at 491. The Court also rejected the idea many statements that are not actionable on their own can become actionable when they create an "overall impression" of falsity. *Id.*

265. *Id.* at 492.

266. *Id.*

267. *Id.*

268. *Id.*

269. *Id.*

270. *Bondali*, 620 F. App'x at 492 (quoting In re Comshare, Inc. Sec. Litig., 183 F.3d 542, 549 (6th Cir. 2009)).

pleading a strong inference of scienter by saying that the individual officers must have "received the test results and, thus, knew or should have known that Yum's statements discussing investment risks or touting its safety protocols were false or misleading."[271] The amended complaint failed to plead facts that tied the individual officers to the SIFDC results.[272] The complaint may have survived if the plaintiffs had made a showing that the "senior officers were regularly notified of test results or that Yingtai and Liuhe supplied such a substantial proportion of KFC China's chickens that senior officers would have had to be aware of any issues with such major suppliers."[273]

Finally, the court reached the theory of collective scienter and applied this case to the rule adopted in *Omnicare*.[274] According to the court, a corporation's state of mind as to a false statement can be determined with reference to one of three *Omnicare* categories.[275] Although the plaintiffs showed that some Yum employees knew of the food issues at Liuhe and Yingtai, the plaintiffs did not show that the individual defendants who made the alleged false statements were these employees.[276] Accordingly, the Court held that the plaintiffs did not sufficiently allege scienter as to the corporation or the individual defendants and affirmed the district court's dismissal.[277]

D. Analysis of Collective Scienter

The collective scienter is suboptimal and contrary to congressional intent. The purpose of the PSLRA is to clarify the pleading requirements of Section 10(b) lawsuits and to make it harder for a plaintiff to meet those pleading requirements.[278] As the Supreme Court noted in *Makor Issues & Rights, Ltd.*,[279] "[t]he 'strong inference' standard 'unequivocally raise[d] the bar for pleading scienter.'"[280] Furthermore, collective scienter runs contrary to the congressional purpose of promoting uniformity among the circuits

---

271. *Id.*

272. *Id.*

273. *Id.* 492-93.

274. *Id.* at 493.

275. *Id.* (quoting Omnicare, 769 F.3d at 476).

276. *Bondali*, 620 F. App'x at 493.

277. *Id.*

278. O'Riordan, *supra* note 20, at 1623 (2007); 4 HAZEN, *supra* note 25, at 27-31, 37-40; *see* Private Securities Litigation Reform Act, 109 Stat. 737, 746-47 (1995).

279. Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308 (2007).

280. *Id.* at 321 (citing Makor Issues & Rights, Ltd. v. Tellabs, Inc., 437 F.3d 588 (2006)).

because the other circuits look to respondeat superior over collective scienter, or completely reject collective scienter.[281] Collective scienter is inherently about making the threshold for pleading lower[282] while Congress intended the "strong inference" threshold of the PSLRA to be difficult to satisfy.[283] When collective scienter inquires into lowering the congressional standard, it proceeds down the wrong path entirely by usurping congressional intent. Unless Congress provides for collective scienter, it appears the Supreme Court will continue to adhere to the strict pleading standards of the PSLRA, [284] and this is the sound function of the judicial branch.[285]

The PSLRA does not provide specific statutory guidelines as to scienter, and as such, the courts must determine whether the pleading standards have been met on a case-by-case basis.[286] As the Supreme Court stated in *Makor*, "In sum, the reviewing court must ask: When the allegations are accepted as true and taken collectively, would a reasonable person deem the inference of scienter at least as strong as any opposing inference?"[287] If the plaintiff in the case makes a showing that the strong inference of scienter is "at least as compelling as any opposing inference of nonfraudulent intent,"[288] then the plaintiff may survive pleading. The standard for pleading

---

281. *Tellabs, Inc.,* 551 U.S. at 321-22; *see* 4 HAZEN, *supra* note 25, at 27; *see supra* Section IV.A.

282. Abril & Olazábal, *supra* note 18, 115-16; O'Riordan, *supra* note 20, at 1605.

283. O'Riordan, *supra* note 20, at 1623.

284. *See supra* Section II.E.

285. King v. Burwell, 135 S. Ct. 2480, 2506 (2015) (Scalia, J., dissenting).)

> It is not our place to judge the quality of the care and deliberation that went into this or any other law. A law enacted by voice vote with no deliberation whatever is fully as binding upon us as one enacted after years of study, months of committee hearings, and weeks of debate. Much less is it our place to make everything come out right when Congress does not do its job properly. It is up to Congress to design its laws with care, and it is up to the people to hold them to account if they fail to carry out that responsibility.
>
> Rather than rewriting the law under the pretense of interpreting it, the Court should have left it to Congress to decide what to do about the [Act] . . . .

Id. The author enjoyed reading the opinions of Justice Scalia, whether he agreed with them or not, and admired his example of civic virtue, bold legal reasoning, and uncommon character. Justice Scalia passed away during the course of writing this note. As such, this quote serves as an apropos salute to Justice Scalia's legacy, and it is fitting critique of judicial activism.

286. *Tellabs, Inc.,* 551 U.S. at 321-22 (citations omitted); *see* 4 THOMAS LEE HAZEN, TREATISE ON THE LAW OF SECURITIES REGULATION 27 (West Practitioner's Ed. 6th ed. 2009).

287. *Tellabs, Inc.,* 551 U.S. at 326.

288. *Id.* at 314, 326; 4 HAZEN, *supra* note 25, at 29.

then is "at least as likely as" an opposing inference and the standard for trial is "more likely than not."[289] Therefore, if there is a strong inference, a cogent one, not just a plausible one, [290] the plaintiff survives pleading and there is no need for a showing of collective scienter.

When the plaintiff can identify specific individuals within a corporation who possess scienter, then pleading a strong inference is easy because it can be pled against the individual. Respondeat superior imputes the individual's scienter to the defendant corporation for purposes pleading Section 10(b) and Rule 10b-5 liability against the corporation.[291] But when the plaintiff cannot identify specific individuals, then the plaintiff must meet the strong inference standard by other means.[292]

The plaintiff should plead in accordance with the strong inference language of the PSLRA clarified in Supreme Court's decision in *Makor*[293] and the Seventh Circuit's General Motors analogy.[294] In this manner, the pleading standard is coherent and high in accordance with congressional intent, and it avoids the potential for broadening liability[295] by focusing on the strong inference language.[296] The Sixth Circuit need not create a separate collective scienter analysis during pleading because the strong inference standard is already sufficient.[297] In *Omnicare*, the imputation of scienter to the corporation through collective scienter did not matter because the court still dismissed the plaintiff's suit for lack of a strong inference.[298] Essentially, while in the pleading stage, the Second Circuit need not traverse the realm of collective scienter for the corporate defendant to possess scienter. Eliminating collective scienter will avoid potential confusion and broadening of liability beyond the scope of congressional intent.[299] As the Second Circuit noted in *Dynex*,[300] a specially named individual defendant within the corporation is not needed when the

---

289. *Tellabs, Inc.*, 551 U.S. at 328-29.

290. *Id.* at 314; 4 HAZEN, *supra* note 25, at 28.

291. Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital, Inc., 531 F.3d 190, 195-96 (2008).

292. The author finds it helpful to think of this in terms of control. S*ee supra* notes 114, 116, 131, 132, 156 and accompanying text; s*ee supra* Sections II.E.1, II.E.3, III.A.

293. *Tellabs, Inc.*, 551 U.S. at 308, 314, 323-24, 326, 328-29; 4 HAZEN, *supra* note 25, at 29.

294. *Makor*, 513 F.3d at 710.

295. *Stoneridge*, 552 U.S. at 164-65.

296. *Tellabs, Inc.*, 551 U.S. at 321 (quoting *Makor*, 437 F.3d 588 (2006)).

297. 4 HAZEN, *supra* note 25, at 28.

298. KBC Asset Mgmt. N.V. v. Omnicare, Inc., 769 F.3d 455, 484 (6th Cir. 2014).

299. *See supra* Section II.D.

300. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 195-96.

plaintiff can satisfy the strong inference standard.[301] Once the strong inference standard is met, the plaintiff survives pleading; there is no need for further complication.[302] The Second Circuit does this well and comports with the other respondeat superior circuits.[303]

In *Bondali*, one may note how little written attention was given to the collective scienter argument and the rule prescribed by the Sixth Circuit in *Omnicare*.[304] In completing this pattern of abandonment in future cases, the Sixth Circuit should strike the collective scienter analysis and focus on the strong inference language provided to it in the PSLRA.[305] The Sixth Circuit could have achieved the dismissal of the case via the strong inference standard without the collective scienter gloss. The corporation's state of mind can be determined without the collective scienter *Omnicare*[306] categories.[307]

The Sixth Circuit should perform its analysis like the Second Circuit by focusing on the strong inference standard to the exclusion of the collective scienter.[308] In *Bondali*, the Sixth Circuit tagged on a collective scienter addendum that showed that the plaintiff did not even plead collectively that the individual defendants possessed the requisite scienter.[309] It performed this analysis immediately after concluding that there was no strong inference of scienter.[310] This is unnecessary because if the plaintiff did not properly plead fraud against the individual defendants[311] and the strong inference standard was not met against the corporation,[312] then there is no need to inquire into the whether the individual defendant's scienter could be imputed to the corporation. There is no scienter to be imputed because the individuals did not possess it, and, regardless, there was no strong inference of scienter.

---

301. *Id.*

302. *Id.*

303. *Id.; Makor*, 513 F.3d at 710.

304. *Omnicare*, 769 F.3d at 476-77; Abril & Olazábal, *supra* note 18, at 135.

305. *Bondali*, 620 F. App'x at 489. The Sixth Circuit discussed the strong inference language, but the focus shifted at the end of the *Bondali* decision from strong inference to collective scienter. *Id.* at 492-93.

306. *Id.* at 493 (quoting *Omnicare*, 769 F.3d at 476).

307. Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital, Inc., 531 F.3d 190, 195-96 (2008).

308. *Id.* at 196.

309. *Bondali,* 620 F. App'x at 493.

310. *Id.* at 492-93.

311. *Id.* at 492.

312. *Id.*

The plaintiff in *Bondali* only pled four facts to support a strong inference of scienter.[313] These facts boil down to the plaintiff alleging that the individual officers made statements and that they were in a position because of their job title to know that the statements were false.[314] The competing inference of scienter would be that the officers were merely negligent in performing their duties. Negligence is not a strong inference of scienter,[315] and the inference of scienter was not strong enough to oppose the competing inference of negligence.[316] Motive and opportunity to commit fraud is not sufficient; there must be strong inference of recklessness or intentionality.[317]

In *Bondali*, the defendant made several statements that did not give rise to the level of inferring that the corporation possessed the scienter to commit fraud pursuant to the PSLRA. The plaintiff did not allege facts that Yum lacked corporate food standards and safety protocols in contradiction to its statements that it did.[318] The failure of the corporation to meet aspirational standards does not rise to the level of a strong inference of scienter.[319] It is also not a fraudulent misstatement to state in prospective investment publications that there may be safety problems when there were safety problems.[320] This makes sense given that there was no showing by the plaintiff of investment risk.[321] The plaintiff must plead facts that give rise to the strong inference, not rely on the court to speculate about the existence of possible facts.[322] Essentially, in *Bondali*, the plaintiff did not reached the level of a strong inference of scienter laid out in the Seventh Circuit's General Motors analogy.[323]

---

313. *Id.*

314. *Bondali,* 620 Fed. App'x at 492 ; *see supra* note 119 and accompanying text.

315. *See supra* note 50 and accompanying text. Negligence is definitely not a strong inference of scienter rather it is the opposite. Negligence steps in where scienter cannot be proven, not when it can.

316. *Bondali,* 620 F. App'x at 492 (quoting In re Comshare, Inc. Sec. Litig., 183 F.3d 542, 549 (6th Cir. 2009)); *see Ernst*, 425 U.S. at 198-200. *See supra* Section II.E.2.

317. *Bondali,* 620 F. App'x at 492 (quoting In re Comshare, Inc. Sec. Litig., 183 F.3d 542, 549 (6th Cir. 2009)); *see supra* note 50 and accompanying text.

318. *Bondali*, 620 Fed. App'x at 489.

319. *Id.* at 490.

320. *Id.* at 490-91 (citing In re FBR, Inc. Sec. Litig., 544 F. Supp. 2d 346, 362 (S.D.N.Y. 2008)).

321. *Id.* at 491.

322. *Bondali,* 620 F. App'x at 491; *see* Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital, Inc., 531 F.3d 190, 196 (2d Cir. 2008).

323. *Makor,* 513 F.3d at 710; *see supra* Section IV.A.2.

The General Motors analogy involved a misstatement that millions of cars were sold when none were sold.[324] The conclusion is that the officers must know that such a statement is false, and imputing the officers' scienter makes sense even though specific individuals that knew of the falsity cannot be identified.[325] *Bondali* involved hardly such a blatant misstatement, but involved only two rogue chicken factories in China[326] and statements involving aspirational information.[327] The pleadings point out no dramatic announcement[328] and don't argue that the officials knew or would have known that the statements were false because of certain circumstances.[329] The pleadings only make general allegations that the officers would look into food safety, and were motivated by their performance based compensation.[330] This is not a sufficient allegation for a strong inference of scienter to arise.[331] The Sixth Circuit would have done well to stop here in its dismissal analysis, and dismiss the complaint as the Second Circuit would have done in *Dynex*.[332] There was no need to progress into a collective scienter analysis as to the individual defendants because the strong inference standard already would dismiss the suit.[333]

The reason for collective scienter is to avoid the potential difficulty of identifying a specific culpable defendant whose scienter can be imputed to the corporation under a Section 10(b) cause of action.[334] Collective scienter looks to several individual defendants whose combined scienter can be aggregated and then imputed to the corporation for the required state of mind under the PSLRA.[335] The PSLRA requires specifically that the plaintiff

---

324. *Makor,* 513 F.3d at 710; *see supra* Section IV.B.

325. *Makor,* 513 F.3d at 710.

326. *Bondali,* 620 F. App'x at 485.

327. *Id.* at 489-90.

328. Southland Sec. Corp. v. Inspire Ins. Sols., Inc., 365 F.3d 353, 366 (5th Cir. 2004) (citing Nordstrom, Inc. v. Chubb & Son, Inc., 54 F.3d 1424, 1435 (9th Cir. 1995); In Re Apple Computer, Inc. Sec. Litig., 243 F. Supp. 2d 1012, 1023 (N.D. Cal. 2002)).

329. *Bondali,* 620 F. App'x at 492-93.

330. *Id.* at 492 (citations omitted).

331. *Teamsters Local 445 Freight Div. Pension Fund*, 531 F.3d at 196; *see* KBC Asset Mgmt. N.V. v. Omnicare, Inc., 769 F.3d 455, 484 (6th Cir. 2014); *see Bondali*, 620 F. App'x at 492.

332. *Teamsters Local 445 Freight Div. Pension Fund,* 531 F.3d at 197. The same can be said for the Sixth Circuit's decision in *Omnicare. Omnicare,* 769 F.3d at 483.

333. *Bondali,* 620 F. App'x at 493.

334. *See supra* Sections, II.A, II.D.; Abril & Olazábal, *supra* note 18, at 121-22; Kircher, *supra* note 19, at 159.

335. O'Riordan, *supra* note 20, at 1605.

allege the state of mind of the "defendant."[336] This singular defendant language comports with respondeat superior precedent that requires the plaintiff to point to a single individual within the corporation.[337] The collective scienter language offends this language by making it plural, and furthermore, collective scienter shifts the focus from the corporation, the main defendant to be held liable, to the individuals within the corporation. The language in the PSLRA is in context of a singular individual.[338] It is confusing and complicated for the plaintiff to plead the untrue misstatements[339] made by the individual defendants and then the different scienters possessed by certain differing levels of officers and employees of the corporation—especially when it is already difficult to identify the individuals.[340] Essentially, collective scienter's bane is the very same problem it sought to solve—the difficulty of finding specific individuals[341] within the corporation with the requisite scienter.[342] After extensive groundwork, only then can the aggregate scienter be imputed to the corporation under collective scienter. It would have been far simpler to maintain a strong inference focus to the exclusion of any collective scienter rule.

When specific individual officers cannot be named for the imputation of scienter to the corporation, it is much simpler just to argue that the singular defendant, the corporation, made misstatements—which, in the end, it did through its employees.[343] The plaintiff would then plead the required state of mind of the corporation itself in accordance with the strong inference language, much like the Second Circuit in *Dynex*[344] and Seventh Circuit in *Makor*.[345] The Second, Seventh, and Ninth Circuits' precedent already affirms that the corporation can be held liable even though specific individual officers cannot be named,[346] and that the focus in these cases is properly placed on the defendant corporation, rather than on finding the

---

336. Private Securities Litigation Reform Act, 109 Stat. 737, 747 (1995).

337. Abril & Olazábal, *supra* note 18, at 113.

338. Private Securities Litigation Reform Act, 109 Stat. 737, 747 (1995).

339. *Id.*

340. *Id.* For example of this, see *Bondali*, 620 F. App'x at 493.

341. *See supra* note 234 and accompanying text.

342. *See supra* Section II.D.

343. Private Securities Litigation Reform Act, 109 Stat. 737, 747 (1995).

344. Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital, Inc., 531 F.3d 190, 195-97 (2008).

345. Private Securities Litigation Reform Act, 109 Stat. 737, 747 (1995); *Makor*, 513 F.3d at 710.

346. *See supra* Sections IV.A.2 and IV.A.3.

individual defendants who already could not be found.[347] Collective scienter looks for individuals in precisely the moment when individuals cannot be named. The strong inference language is not made clear by this reverse logic. If a strong inference cannot be pled because individuals cannot be named, it does not make sense just to keep looking for individuals at different levels of the corporation. It is simpler to look to whether the plaintiff pled a strong inference of scienter against the corporation without naming the individuals.

Furthermore, the strong inference standard, excluding a collective scienter analysis, avoids the pitfall of a changing judicial standard. It is "Business Law 101" that the law should "provide stability, predictability, and continuity so that people [and corporations] can know how to order their affairs."[348] When corporations do not have a stable standard to orientate their affairs, they cannot effectively manage their risk exposure to liability, but a stable standard, whatever it may be, allows corporations to react effectively in ordering their behavior. The goal of the PSRLA was to create uniformity among the circuits as the Section 10(b) cause of action,[349] and in this manner, the PSLRA meant to give some stability to corporations.[350]

Collective scienter attacks this stability on multiple fronts. Since the Sixth Circuit embarked on its collective scienter journey, it has used slightly different standards or focuses as to pleading the scienter of the corporation. Collective scienter has proved an unstable standard. In *Monroe,* the Sixth Circuit took a pure collective scienter stand and allowed the plaintiff's claim to survive.[351] In *Omnicare*, the court adopted a middle ground collective

---

347. Glazer Capital Mgmt., LP v. Magistri, 549 F.3d 736, 744-45 (9th Cir. 2008); *Teamsters Local 445 Freight Div. Pension Fund,* 531 F.3d at 195; *Makor,* 513 F.3d at 710;.

348. Roger LeRoy Miller & Frank B. Cross, BUSINESS LAW 2 (Cengage Learning, Alternate Edition: Text and Summarized Cases. 12th ed. 2013).

349. *Tellabs, Inc.*, 551 U.S. at 321-22 (citations omitted); *see* 4 HAZEN, *supra* note 25, at 27 (West Practitioner's Ed. 6th ed. 2009). The PSLRA does not provide specific statutory guidelines as to scienter, and as such, the courts must determine whether the pleading standards have been met on a case-by-case basis. *Tellabs, Inc.*, 551 U.S. at 321-22.

350. Some may argue that a safe harbor rule would be giving stability to corporations in terms of knowing how to manage their behavior. This is precisely the problem. The author believes that a safe harbor in a fraud liability rule is inadvisable. A corporation will simply organize itself to avoid liability, and in this manner, turn a blind eye to what is going on at controllable levels of the corporation structure.

351. City of Monroe Emps. Ret. Sys. v. Bridgestone Corp., 399 F.3d 651, 688-91 (6th Cir. 2005).

scienter approach using a three level standard,[352] and then dismissed the suit for lack of pleading a strong inference of corporate scienter.[353] In *Bondali*, the focus primarily was pleading a strong inference of corporate scienter, and then collective scienter was tagged on the end of the opinion to support its decision of dismissal.[354] Since adopting collective scienter, the Sixth Circuit has left varying and unstable precedent for corporations in its jurisdiction to orientate their risk exposure. Like building a physically sound house from a singular measuring point, the strong inference standard is superior to one that is unstable, changing, or a compromise.[355]

The collective scienter standard is further confused and unstable because of a simple confusion of terms in the language of collective scienter and the PSLRA. The strong inference of scienter language applies to a singular defendant, namely the corporation.[356] Collective scienter muddles this standard by creating two iterations of the same issue: a strong inference of scienter. It becomes unclear whether a strong inference of scienter must be pled against the individual defendants whose collective knowledge is sought to be aggregated and then imputed to the corporation.[357] This makes more sense if one sticks to the language of the PSLRA but less sense if one is trying to lower the pleading standard because a single culpable officer cannot be located.[358] The plaintiff would now be faced with pleading a strong inference against many defendants, rather than one. Or, on the other hand, is the standard that a strong inference must be pled against the defendant corporation through the many aggregated and less than strong inferences of the individual officers? This makes more sense if one sticks to the language of collective scienter, but it offends the PSLRA's singular defendant language.[359] While the second phrasing of the issue is the

352. KBC Asset Mgmt. N.V. v. Omnicare, Inc., 769 F.3d 455, 476-77 (6th Cir. 2014); Abril & Olazábal, *supra* note 18, at 135.

353. *Omnicare,* 769 F.3d at 483-84 (quoting Abril & Olazábal, *supra* note 18, at 135).

354. *Bondali*, 620 F. App'x at 492-43.

355. *See contra*, Michael T. Jones, Note, *Where to Point the Finder: Omnicare's Attempt to Rectify the Collective Scienter Debate*, 57 B.C. L. REV. 695, 695-97, 729 (2016). *Ephesians* 2:18-22 (English Standard Version). Christ is the chief cornerstone upon which the whole building of the church is built and measured. *Id.*

356. Private Securities Litigation Reform Act, 109 Stat. 737, 747 (1995).

357. *See Omnicare,* 769 F.3d at 483 (quoting Abril & Olazábal, *supra* note 18, at 135).

358. *See id.* at 476-77.

359. *See id.* at 476-77; Abril & Olazábal, *supra* note 18, at 135.

approach the Sixth Circuit takes,[360] the PSLRA's strong inference language literally applies to a singular defendant.[361] If collective scienter were adopted, a literal interpretation of the PSLRA would mandate following the first iteration of the issue, not the second. A strong inference must be pled for each defendant. This renders negligible collective scienter's purposed utility in lowering the pleading standard, which is already a wrong aim to begin with.

The Supreme Court limited the scope of the private cause of action it created under Section 10(b) and Rule 10b-5.[362] The scope should be limited because the private cause of action is a judicial construct underneath Section 10(b),[363] and Congress purposefully limited the cause of action with the PSLRA.[364] Congress could potentially solve any confusion by codifying the cause of action and specifying its scope. Until new congressional direction, the Supreme Court mandates adherence to the higher pleading standard of the PSLRA,[365] and collective scienter goes against this grain. The Sixth Circuit would do well to abandon its collective scienter analysis and adopt the strong inference focus of the Second and Seventh Circuit it already appears to be moving towards.[366]

V. CONCLUSION

Collective scienter should be abandoned as an unhelpful addendum to an already complicated pleading analysis under the PSLRA, and the Sixth Circuit should move to a standard like the Second or Seventh Circuit.[367] When the plaintiff can identify specific individuals within a corporation who possess scienter, their scienter can simply be imputed to the defendant corporation for purposes of pleading Section 10(b) and Rule 10b-5 liability against the corporation,[368] but when the plaintiff cannot identify specific individuals, the plaintiff must meet the strong inference standard by other

360. *See generally Bondali*, 620 F. App'x at 492-93; *Omnicare*, 769 F.3d at 483-84 (quoting Abril & Olazábal, *supra* note 18, at 135); City of Monroe Emps. Ret. Sys. v. Bridgestone Corp., 399 F.3d 651, 688-89 (6th Cir. 2005).

361. Private Securities Litigation Reform Act, 109 Stat. 737, 747 (1995).

362. 3 HAZEN, *supra* note 25, at 522-23, 525-26.

363. *See supra* Sections II.B, II.C.

364. O'Riordan, *supra* note 20, at 1623.

365. *Tellabs, Inc.*, 551 U.S. at 321 (quoting *Makor*, 437 F.3d at 601).

366. *Bondali*, 620 Fed. App'x at 492-93.

367. *See supra* Sections IV.A.2., IV.A.3.

368. Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital, Inc., 531 F.3d 190, 195-96 (2d Cir. 2008).

means. The plaintiff should plead in accordance with strong inference language of the PSLRA clarified in Supreme Court's decision in *Makor*[369] and the Seventh Circuit's General Motors analogy.[370] In this manner, the pleading standard is coherent and high in accordance with congressional intent, and it avoids the potential for broadening liability[371] under collective scienter by focusing on the strong inference language.[372]

369. *Tellabs, Inc.*, 551 U.S. at 314, 323-24, 326, 328-29; 4 HAZEN, *supra* note 25, at 29.

370. *Makor*, 513 F.3d at 710.

371. *Stoneridge Inv. Partners, LLC.*, 552 U.S. at 164-65.

372. *Tellabs, Inc.*, 551 U.S. at 321 (quoting *Makor*, 437 F.3d at 601).