SHAREHOLDER PROTECTION IN TENDER OFFERS: HOW TO RESOLVE PRESSING UNCERTAINTY IN SECTION 14(E) LITIGATION AND WHY IT MATTERS

Matthew S. Seafield

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Abstract

In 2018, the Ninth Circuit issued an unprecedented opinion in Varjabedian v. Emulex Corp. that split from the Second, Third, Fifth, Sixth, and Eleventh circuits to hold that only negligence, as opposed to scienter, is required to prove securities fraud in a Section 14(e) claim. As a result, there is an outstanding circuit split and unresolved question as to which standard applies—a question that has drawn the interest and commentary of many significant players in the financial industry, including the Securities and Financial Markets Association, the Chamber of Commerce of the United States, the Former Commissioners of the Securities and Exchange Commission, and the Business Roundtable. When Varjabedian was granted certiorari in 2019, each of these named groups—in addition to others—filed amicus briefs that warned of the potential negative economic implications from a negligence standard. Despite this, the Supreme Court dismissed the case as improvidently granted shortly after oral argument in a one sentence opinion.

Nevertheless, the Ninth Circuit's textual analysis of Section 14(e) correctly shows errors in prior Section 14(e) jurisprudence and points out that legal precedent does not actually require scienter. Importantly, Section 14(e) may be divided into two separate clauses—the first clause being substantially similar to the language of Rule 10b-5 and the second clause being substantially similar to the language of Section 10(b). Prior courts held Section 14(e) to require scienter, in large part, because Section 10(b) and Rule 10b-5 have been interpreted to require scienter. To rebut this presumption, however, the Ninth Circuit referred to the Supreme Court's decision in Ernst & Ernst v. Hochfelder to show that Rule 10b-5 does not require scienter due to its language but simply because its authorizing statute, Section 10(b), requires scienter. The Ninth Circuit also cites the Supreme Court in Aaron v. SEC to argue that language substantially similar to Section 14(e) requires only negligence. Moreover, the Ninth Circuit makes a persuasive argument for the negligence standard that considers legislative history and intent. Considering the importance of economic efficiency, however, a negligence standard may very well not be sustainable in the long run as it is likely to increase frivolous litigation and forced settlements that increase transaction costs.

Moving forward, the SEC should clarify its interpretation of Section 14(e) to explicitly state whether negligence or scienter is required. In doing so, the agency would

[*] J.D./M.B.A. Candidate, Michigan State University College of Law and Eli Broad College of Business, 2022; B.A. in History and Political Science, Calvin University, 2018. The author would like to thank James Chen, Geeyoung Min, Elliot Spoon, and Christian Schultz for insightful feedback and commentary throughout the drafting process.

provide administrative guidance to markets that mitigates uncertainty in a more expedient manner than the traditional legislative process. This clarification would likely take the form of an additional rule—proposed rule 14e-9—within Regulation 14E. At this point, SEC Commentary seems to imply that the agency interprets scienter to be required—an interpretation that would likely be granted Chevron deference under the SEC's broad rulemaking authority. Because Chevron deference sets a high standard, any SEC rule clarification is unlikely to be overturned. However, in the event that it was, the question would almost certainly be back before the Supreme Court on appeal to resolve the issue. The importance of resolving this split should not be taken lightly—after all, uncertainty must be mitigated to provide investors with the confidence needed to spur economic activity—and SEC rule clarification appears to be the most viable path forward.

INTRODUCTION

In 2018, in a drastic turn of events, the Ninth Circuit split from the Second, Third, Fifth, Sixth, and Eleventh Circuits to hold that negligence is the requisite standard of culpability regarding alleged material misstatements or factual omissions in a claim brought forth under § 14(e) in connection with a securities tender offer.[1] In doing so, the Ninth Circuit overturned the U.S. District Court for the Central District of California—which followed legal precedent from the other circuits to hold that § 14(e) instead requires scienter.[2] Notably, the court's analysis diverged from the traditional path of interpreting § 14(e) to require scienter, the same standard of culpability as required for a securities fraud action under § 10(b).[3] Suddenly, the Ninth Circuit created significant unanswered questions with uncertain implications as to whether mere negligence should be the standard for culpability in a private action under § 14(e).[4]

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[1] *See* Varjabedian v. Emulex Corp. (*Varjabedian II*), 888 F.3d 399, 401 (9th Cir. 2018) (holding that section 14(e) of the Exchange Act requires negligence rather than scienter); *see also* John Stigi & John Landry, *Ninth Circuit Split From Other Circuits, Holding That a Negligence Standard Applies to a Claim Challenging Tender Offer Disclosures Under Section 14(e)*, SHEPPARD MULLIN: CORP. & SEC. L. BLOG (Apr. 26, 2018), https://www.corporatesecuritieslawblog.com/2018/04/negligence-standard-scienter/. Section 14(e) allows plaintiffs to bring suit for fraud if any untrue statement or omission of material fact is made with respect to a securities tender offer. *See* 15 U.S.C. § 78n(e) (1968).

[2] *See* Varjabedian v. Emulex Corp. (*Varjabedian I*), 152 F.3d 1226, 1232 (C.D. Cal. 2016) ("[E]ven though the Ninth Circuit has not decided the issue regarding scienter required under section 14(e), the majority of other circuits and districts to address the issue have held that . . . scienter [is] required under section 14(e)[.]").

[3] *Id.*; *see also* Mark J. Loewenstein, *Section 14(e) of the Williams Act and the Rule 10b-5 comparisons*, 71 GEO. L.J. 1311, 1312 (1983).

[4] *See* Stigi & Landry, *supra* note 1.

Unsurprisingly, the Ninth Circuit's decision has proved polarizing.[5] According to some, adopting a negligence standard under § 14(e) will encourage frivolous merger objection lawsuits within the Ninth Circuit, taking advantage of the lower standard.[6] Due to the Securities Exchange Act's liberal provision regarding jurisdiction, for all practical purposes, a de facto negligence standard may then also result from the circuit split as plaintiffs seek to forum-shop.[7]

Specifically, the resulting negligence standard would supposedly encourage the sort of frivolous securities litigation that Congress previously sought to prevent through the Private Securities Litigation Reform Act (PSLRA) in 1995, which elevated the pleadings standard necessary to sufficiently state a claim for securities fraud.[8] In the aftermath of PSLRA, some scholars have noted that enhanced congressional attention on mental state has resulted in substantial and significant changes to heighten the state of mind requirements in a number of private securities fraud actions.[9] With increased emphasis on requisite state of mind for securities fraud, the question addressed by the Ninth Circuit is critical for guiding both

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[5] *See* Stigi & Landry, *supra* note 1; *see also* Reply Brief for the Petitioners at 11, Emulex Corp. v. Varjabedian 888 F.3d at 409–10 (9th Cir. 2018) (No. 18-459) (describing the monumental impact of implementing a negligence standard for securities fraud under Section 14(e)). According to those in opposition of the negligence standard, there are concerns that *Varjabedian I* "will fundamentally alter the civil liability regime that courts have applied under Section 14(e)." *Id.*

[6] *See* Brief for the Securities Industry and Financial Markets Association as Amicus Curiae at 13–14, Emulex Corp. v. Varjabedian (*Varjabedian III*), 139 S. Ct. 1407 (2019) (No. 18-459).

[7] *See* Stigi & Landry, *supra* note 1. According to some, the outstanding circuit split may result in "virtually every suit arising from a tender offer under the more lenient [negligence] standard in the Ninth Circuit" due to the broad venue provisions of the Exchange Act, exacerbating the importance of resolving the issue. *See* Aaron F. Miner, *Supreme Court Has Opportunity to Reexamine Implied Private Right of Action Under Section 14(e) of the Exchange Act*, ARNOLD & PORTER (Oct. 22, 2018), https://www.arnoldporter.com/en/perspectives/publications/2018/10/scotus-has-opportunity-to-reexamine.

[8] In 1995, Congress passed the Private Securities Litigation Reform Act to heighten the pleading standard for the requisite state of mind necessary to carry the case forward. *See* William H. Kuehnle, *On Scienter, Knowledge, and Recklessness under Federal Securities Laws*, 34 HOUS. L. REV. 121, 123 (1997). Kuehnle also notes that Congressional attention on the state of mind for securities fraud "has resulted in several significant changes that heighten the state of mind requirements for some situations in private actions as part of limitations imposed on such suits [such as PSLRA]." *Id.*

[9] *See id.* (stating that increased congressional attention to scienter in light of PSLRA "has resulted in several significant changes that heighten the state of mind requirements for some situations in private actions" due to limitations imposed on those suits in PSLRA).

investors and tender offerors going forward.[10]

As perhaps expected of such an important case, *Varjabedian* was appealed to the Supreme Court and subsequently granted certiorari.[11] There were eleven different amicus briefs filed, including those from several prominent groups such as the Securities Industry and Financial Markets Association, the Chamber of Commerce of the United States of America, the Former Commissioners of the Securities and Exchange Commission, and the Business Roundtable.[12] However, the Court shockingly dismissed the case shortly thereafter as improvidently granted on April 23, 2019 in a one-sentence opinion.[13]

On remand, the U.S. District Court for the Central District of California noted that the Supreme Court oral arguments focused substantially on the issue of whether § 14(e) created any private right of action whatsoever.[14] As Justice Ginsburg pointed out, this issue was not raised before either the district court or the Ninth Circuit.[15] Although the Supreme Court did not elaborate on its reason for dismissal, the Court most likely dismissed the writ of certiorari so that the lower courts could determine: first whether § 14(e) required a private right of action, and second whether the alleged facts of *Varjabedian* sufficiently plead materiality.[16] Nevertheless, the Supreme Court's decision to dismiss the case creates significant confusion within the M&A industry.[17]

Considering the defendant's motion to dismiss, the district court found that materiality did not exist and thus determined the defendant cannot be culpable for securities fraud regardless of mental state.[18] Therefore, the court dismissed the plaintiff's claim with prejudice because the plaintiff had not alleged materially misleading conduct.[19] After being dismissed with prejudice on factual grounds, *Varjabedian* will likely not be the case that ultimately decides the circuit split

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[10] *See* Brief for the Securities Industry and Financial Markets Association as Amicus Curiae at 13–14, *Varjabedian III*, 139 S. Ct. 1407 (2019) (No. 18-459).

[11] *See* Varjabedian v. Emulex Corp. (*Varjabedian IV*), No. SACV 15-00554-CJC (JCDx), 2020 U.S. Dist. LEXIS 40037, *9 (C.D. Cal. 2020) (citing *Varjabedian III*, 139 S. Ct. 1407, 1407 (2019)).

[12] *See Emulex Corp. v. Varjabedian,* SCOTUSBLOG, https://www.scotusblog.com/casefiles/cases/emulex-corp-v-varjabedian/.

[13] *See Varjabedian III*, 139 S. Ct. at 1407.

[14] *See Varjabedian IV*, 2020 U.S. Dist. LEXIS 40037, at *9.

[15] *See id.*

[16] *See id.*

[17] *See* Melissa Sevier, *But in the End, It Doesn't Even Matter: How the Ninth Circuit's Split from Five Other Circuits and the Subsequent Supreme Court Case Changed Nothing for Section 14(e) Claims*, 11 GEO. MASON J. INT'L COM. L. 105, 125 (2020).

[18] *See Varjabedian IV*, 2020 U.S. Dist. LEXIS 40037, at *27.

[19] *See id.* at *30–*31.

regarding whether a negligence or scienter standard applies to a § 14(e) claim.[20]

Putting the issue of materiality aside, this Note addresses competing positions for whether negligence or scienter is the proper standard for § 14(e) claims and proposes a viable and practical solution for resolving the circuit split.[21] To do so, Part I discusses the necessary background on securities regulation in the United States, considering the evolving nature of the regulatory landscape over the past several decades to place *Varjabedian* in its proper context.[22] Next, Part II helps frame the issue of whether negligence or scienter should apply to § 14(e) claims through assessing legal precedent and relevant policy factors.[23] Lastly, Part III critically analyzes the *Varjabedian* case to show how the Ninth Circuit applied major canons of statutory interpretation to correctly identify existing errors in § 14(e) jurisprudence.[24] Moreover, Part III provides a conceptual framework to analyze the debate going forward and applies this framework in order to provide guidance for regulators.[25]

I. THE HISTORICAL DEVELOPMENT OF FEDERAL SECURITIES REGULATION

In 1934, Congress passed the Exchange Act to regulate and control securities transactions on the secondary market.[26] The Exchange Act was necessary, as part of a larger effort to stimulate the economy, to restore public confidence in investment securities after the Wall Street Crash of 1929 triggered the Great Depression.[27] Importantly, the Exchange Act created the Securities and Exchange Commission (the SEC) to implement and enforce the regulations transcribed therein.[28]

As an integral part of the regulatory framework, the Securities Act of 1933

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[20] *See id.* at *33. In dismissing the claim with prejudice, the District Court wrote that "Plaintiff's counsel has not identified any additional facts that Plaintiff could allege beyond those in the [First Amended Complaint] and the judicially noticed materials. In the FAC, Plaintiff put his best foot forward regarding the materiality and misleading nature of the omitted information but failed to state a claim." *Id.*

[21] *See infra* text accompanying notes 200–60.

[22] *See infra* Part I.

[23] *See infra* Part II.

[24] *See infra* Part III.

[25] *See id.*

[26] *See* Securities Exchange Act of 1934, 15 U.S.C. § 78b (1934); *see also* Elisabeth Keller & Gregory A. Gehlmann, *Introductory Comment: A Historical Introduction to the Securities Act of 1933 and the Securities Exchange Act of 1934*, 49 OHIO ST. L.J. 329, 330 (1988).

[27] *See* Keller & Gehlmann, *supra* note 26, at 330.

[28] *See id.*; *see also* 15 U.S.C. § 78d (1934).

requires public companies to disclose pertinent information regarding securities sold through the instrumentalities of interstate commerce by filing quarterly and annual reports with the SEC.[29] Ultimately, the goal of registration is to provide full disclosure of truthful information regarding the character of the securities offerings so that investment decisions may be made with confidence.[30] With full disclosure, the theory goes, securities markets will maintain integrity, operating in a relatively transparent manner, and investors will be protected from unnecessary and unwise speculation.[31]

Although its core has largely remained intact, the Exchange Act has been amended several times.[32] For example, in 1968, Congress added several provisions to § 13 and § 14 of the Exchange Act through the amendment process to specifically govern tender offers, which are traditionally one of the most frequently used methods for acquiring corporate control.[33] Originally titled the Full Disclosure of Corporate Equity Ownership and in Corporate Takeover Bids, the collectively added provisions are now commonly referred to simply as the Williams Act.[34]

In addition, the SEC has exercised its regulatory authority to implement critical administrative rules.[35] Perhaps most famously, in 1942, the SEC promulgated Rule 10b-5 pursuant to its authority granted under § 10(b) of the Exchange Act.[36] Specifically, Rule 10b-5 prohibits untrue material statements,

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[29] *See* Keller & Gehlmann, *supra* note 26, at 330.

[30] *See id.*

[31] See J. Kent Dunlap, *The Role of Scienter and the Need to Limit Damages in Rule 10b-5 Actions—The Texas Gulf Sulphur Litigation*, 59 KY. L.J. 891, 893 (quoting Note, *Negligent Misrepresentations under Rule 10b-5*, 32 U. CHI. L. REV. 824, 829 (1965)).

[32] *See* Keller & Gehlmann, *supra* note 26, at 331; *see also* ROBERTA KARMEL, REGULATION BY PROSECUTION: THE SECURITIES AND EXCHANGE COMMISSION VS. CORPORATE AMERICA 44 (1982).

[33] *See* Jeffery J. Giguere, *Negligence v. Scienter: The Proper Standard of Liability for Violations of the Antifraud Provisions Regulating Tender Offers and Proxy Solicitations Under the Securities Exchange Act of 1934*, 41 WASH. & LEE L. REV. 1045, 1045 (1984). For reference, a tender offer may be defined as a "public offer to buy a minimum number of shares directly from a corporation's shareholders at a fixed price, usually at a substantial premium over the market price, in effort to take control of the corporation." *See Tender Offer*, BLACK'S LAW DICTIONARY (11th ed. 2019).

[34] *See* Loewenstein, *supra* note 3, at 1311 n.1.

[35] *See generally Rulemaking Index*, U.S. SECURITIES AND EXCHANGE COMMISSION: REGULATION, https://www.sec.gov/rules/rulemaking-index.shtml.

[36] *See* Dunlap, *supra* note 31, at 893 (emphasizing the importance of Rule 10b-5 in carrying out § 10(b) as a critical component to protect investors). Section 10(b) of the Exchange Act states:

material omissions of factual information, and manipulative or deceptive devices employed in connection with the purchase or sale of securities.[37] Furthermore, Rule 10b-5 also prohibits engagement in any practice that operates as fraud or deceit in connection with a securities transaction.[38] Initial lower court confusion surrounding Rule 10b-5 resulted, in part, from incomplete records of legislative history regarding § 10(b), causing the judiciary to rely on its own sense of justice and fairness.[39] In many instances, this has led 10b-5 jurisprudence to grow on a case-by-case basis.[40]

A. Interpreting Federal Securities Law

Since the Supreme Court decided *Ernst & Ernst v. Hochfelder* in 1976, Rule 10b-5 has been largely interpreted to cement scienter as the necessary standard to prove culpability in a private damage action under § 10(b).[41] Prior to *Hochfelder*,

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> It shall be unlawful for any person . . . to use or employ in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [SEC] may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78j-2 (1934).

[37] *See Timeline: A History of Insider Trading*, N.Y. TIMES (Dec. 6, 2016), https://www.nytimes.com/interactive/2016/12/06/business/dealbook/insider-trading-timeline.html?searchResultPosition=1. In implementing § 10(b), Rule 10b-5 states:

> It shall be unlawful for any person . . . (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 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.

17 C.F.R. § 240.10b-5 (1948).

[38] *See* 17 C.F.R. § 240.10b-5 (1948).

[39] *See* Dunlap, *supra* note 31, at 893–94 (highlighting that interpretation of Rule 10b-5 became exceedingly important as federal courts were soon tasked with many questions of a "complicated nature," including whether this Rule created a private right of action and whether scienter was required to establish liability).

[40] *See id.* at 894.

[41] *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 (1976) (holding that a private cause of action will not lie under § 10(b) and Rule 10b-5 in absence of any allegation of scienter).

however, the lower negligence standard was widely considered to be sufficient for securities fraud under § 10(b).[42] As it relates to *Varjabedian*, Rule 10b-5 interpretation is particularly important because lower courts have generally relied on this rule to hold that § 14(e) also requires scienter.[43]

Scienter may be defined in the securities law context generally as a mental state consisting in an intent to deceive, manipulate, or defraud.[44] The Court echoed this definition in *Hochfelder*.[45] However, despite ruling that scienter is indeed the proper standard, the Court expressly stated not to decide whether recklessness applies to securities fraud under § 10(b).[46] That being said, in light of *Hochfelder*, the issue of whether recklessness suffices for securities fraud became an intriguing and polarizing question for lower courts.[47]

The question of recklessness was further complicated when Congress passed the Private Securities Litigation Reform Act (PSLRA) in 1995, which heightened the pleading requirements for actions alleging securities fraud.[48] Under § 21D(b)(2) of the Exchange Act, which was added through PSLRA, special attention is paid to whether defendant acted with the particular state of mind required for culpability.[49] After PSLRA, multiple federal courts held that Congress intended to heighten the substantive standards for securities fraud in addition to

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[42] *See* Ezra D. Singer, *SEC Enforcement Actions to Enjoin Violations of Section 10(b) and Rule 10b-5: The Scienter Question*, 5 HOFSTRA L. REV. 831, 831 (1977); *See*, *e.g.*, SEC v. Mgmt. Dynamics, Inc., 515 F.2d 801, 809 (2d Cir. 1975); SEC v. Dolnick, 501 F.2d 1279, 1284 (7th Cir. 1974); SEC v. Pearson, 426 F.2d 1339, 1343 (10th Cir. 1970); SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 854–55 (2d Cir. 1968) (en banc), *cert. denied*, 394 U.S. 976 (1969); SEC v. Van Horn, 371 F.2d 181, 181 (7th Cir. 1966); SEC v. M.A. Lundy Assocs., 362 F. Supp. 226, 234 (D.R.I. 1973).

[43] *See* Loewenstein, *supra* note 3, at 1331.

[44] *See Scienter*, BLACK'S LAW DICTIONARY (11th ed. 2019).

[45] *See Hochfelder*, 425 U.S. at 193 n.12 (stating that "the term 'scienter' refers to a mental state embracing intent to deceive, manipulate, or defraud").

[46] *See* William H. Kuehnle, *On Scienter, Knowledge, and Recklessness Under the Federal Securities Laws*, 34 HOUS. L. Rev. 121, 147–48 (1997); *see also Hochfelder*, 425 U.S. at 193, 194 n.12.

[47] *See* Kuehnle, *supra* note 8, at 180. In the securities law context, a reckless statement made by a defendant "involve[es] not merely simple or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either know to the defendant or is so obvious that the actor must have been aware of it." *See* Institutional Investors Grp. v. Avaya, Inc., 564 F.3d 242, 267 n.42 (3d Cir. 2009).

[48] *See* Kuehnle, *supra* note 8, at 127, 141; *see also* 15 U.S.C. §§ 77z-1, 78u-4.

[49] Under § 21(D)(b)(2), plaintiffs must "state with particularity facts giving rise to a strong inference that the defendant acted *with the required state of mind*." 15 U.S.C. § 78u-4(b)(2) (1995) (emphasis added).

the pleading standards through § 21D(b)(2).[50] Some courts, for example, deemed the statute to eliminate liability for recklessness in Rule 10b-5 actions despite the Supreme Court's silence on the issue.[51] However, while courts naturally placed added emphasis on pleading with the requisite state of mind after PSLRA, there is not much reason to suppose that Congress also intended to heighten the substantive standards.[52]

Legislative history surrounding PSLRA helps shed light on Congress's view of recklessness as a sufficient standard of culpability for securities fraud.[53] Interestingly, records show that Congress went back and forth on this issue, drafting initially for the elimination of recklessness as the standard for all Rule 10b-5 actions.[54] However, the SEC strongly opposed eliminating the recklessness standard at legislative hearings, noting that *Hochfelder* had removed only negligence as a basis for liability in a Rule 10b-5 action.[55] Of particular importance, the SEC considers recklessness as a form of scienter under common law while pointing out that England has explicitly recognized recklessness as satisfactory for fraud.[56] Now, scienter is widely recognized to include recklessness despite some lower courts' early divergence in light of PSLRA.[57]

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[50] *See* Michael B. Dunn, *Pleading Scienter After the Private Securities Litigation Reform Act: Or, a Textualist Revenge*, 84 CORNELL L. REV. 193, 231 (1998).

[51] *See id.*; *see also, e.g., In re* Comshare, Inc. Sec. Litig., No. 96-73711-DT, 1997 U.S. Dist. LEXIS 17262 (E.D. Mich. Sept. 18, 1997); Voit v. Wonderware Corp., 977 F. Supp. 363 (E.D. Pa. 1997); Powers v. Eichen, 977 F. Supp. 1031 (S.D. Cal. 1997); Friedberg v. Discreet Logic Inc., 959 F. Supp. 42 (D. Mass. 1997); Norwood Venture Corp. v. Converse Inc., 959 F. Supp. 205 (S.D.N.Y. 1997); *In re* Silicon Graphics, Inc. Sec. Litig., No. C 96-0393, 1996 WL 664639 (N.D. Cal. Sept. 25, 1996); *see also* Chan v. Orthologic Corp., No. CIV-96-1514-PHX-RCB (D. Ariz. Feb. 5, 1998) (noting that, in the court's opinion, PSLRA removed securities fraud liability for recklessness).

[52] *See* Dunn, *supra* note 50, at 231-32.

[53] *See* Kuehnle, *supra* note 8, at 123–24.

[54] *See* Kuehnle, *supra* note 8, at 123.

[55] *See* Kuehnle, *supra* note 8, at 124.

[56] RESTATEMENT (SECOND) OF TORTS § 526(b) cmt. c (1977); W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 107, at 741–42 (5th ed. 1984). In *Derry v. Peek*, which is often referred to as a seminal case in English law, the House of Lords specifically held recklessness to be a basis for fraud liability in 1889. *See, e.g.,* Mary Garvey Algero, *The Sources of Law and the Value of Precedent: A Comparative and Empirical Study of a Civil Law State in a Common Law Nation*, 65 LA. L. REV. 775, 785 (2005). *See also* Kuehnle, *supra* note 8, at 153. Because the American judicial system is modeled on the common law tradition, common law precedent is particularly persuasive for an American court when considering requisite state of mind for tort liability.

[57]*See* Hanon v. Dataproducts Corp., 976 F.2d 497, 507 (9th Cir. 1992) (citing Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1568–69 (9th Cir. 1990)) (stating that

B. Section 14(e)

When Congress passed the Williams Act, § 14(e) was critically added as a broad provision to protect shareholders from fraudulent conduct in tender offers.[58] The Supreme Court later affirmed the breadth of § 14(e), stating that it serves as a broad antifraud provision.[59] This view was echoed by the Ninth Circuit in *Varjabedian*.[60]

To fully understand the breadth of § 14(e), however, it is important to parse the language of the statute to assess which types of conduct are being prohibited. The full text of § 14(e) is as follows:

> It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading, *or* to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation. The Commission shall, for the purposes of this subsection, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative.[61]

Importantly, proper statutory interpretation of the text shows that the statute prohibits at least two forms of conduct.[62] This is because the Conjunctive/Disjunctive Canon states that *or* specifies a disjunctive list, while the

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"[s]cienter may be satisfied by either proof or actual knowledge of recklessness"); Gebhart v. SEC, 595 F.3d 1034, 1041 (9th Cir. 2010) ("Scienter may be established, therefore, by showing that defendants were reckless as to the truth or falsity of their statements."). *See also* William S. Lerach & Eric Alan Isaacson, *Pleading Scienter Under Section 21D(b)(2) of the Securities Exchange Act of 1934: Motive, Opportunity, Recklessness, and the Private Securities Litigation Reform Act of 1995*, 33 SAN DIEGO L. REV. 893, 913 (1996).

[58] *See* Loewenstein, *supra* note 3, at 1311 n.1.

[59] According to the Court, "[b]esides requiring disclosure and providing specific benefits for tendering shareholders, the Williams Act also contains a broad antifraud prohibition [§ 14(e)]." *See* Piper v. Chris-Craft Indus., 430 U.S. 1, 24 (1977).

[60] The Ninth Circuit stated that the "purpose of § 14(e) is to regulate the conduct of a broad range of persons, including those engaged in making or opposing tender offers or otherwise seeking to influence the decision of investors or the outcome of the tender offer." *See Varjabedian II*, 888 F.3d 399, 404 (9th Cir. 2018).

[61] 15 U.S.C. § 78n(e) (1976) (emphasis added).

[62] *See Varjabedian II*, 888 F.3d at 404 (stating that a "plain reading of Section 14(e) readily divides the section into two clauses"); *See also* ANTONIN SCALIA & BRYAN A. GARNER, READING LAW: THE INTERPRETATION OF LEGAL TEXTS 116, 174 (2012).

Surplusage Canon states that no words should be ignored.[63] Specifically, the two forms of conduct prohibited by § 14(e) include: 1) "to make any untrue statement or to omit any material fact necessary in order to make the statements . . . not misleading" and 2) "to engage in any fraudulent, deceptive, or manipulative acts or practices" in connection with a securities tender offer.[64]

The Williams Act does not expressly create a private right of action to enforce its provisions; however, lower federal courts have interpreted § 14(e) to imply such a private right of action.[65] Critically, federal circuit courts have often looked to Rule 10b-5 for guidance in interpreting the Williams Act and enforcing its implied right of action.[66] That being said, considering that the Supreme Court held scienter to be the correct standard for § 10(b) and Rule 10b-5 claims in *Hochfelder*,[67] lower courts have largely determined that scienter should also apply to § 14(e) claims.[68] In many ways, this is because Rule 10b-5 and § 14(e) have strikingly similar language and courts have therefore held that these provisions should be interpreted in the same manner.[69] Application of the reenactment rule, which dictates that provisions with the same language should be interpreted in the same manner, has largely guided the lower courts' reasoning.[70]

In *Chris-Craft Industries, Inc. v. Piper Aircraft Corp.*, for example, the first time that a lower court determined that scienter should apply to a securities fraud action under § 14(e), the Second Circuit held in 1973 that § 14(e) required scienter

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[63] *See* SCALIA & GARNER, *supra* note 62, at 174; *see also Varjabedian II*, 888 F.3d at 404.

[64] § 78n(e); s*ee also Varjabedian II*, 888 F.3d at 404.

[65] *See* Loewenstein, *supra* note 3, at 1311–12.

[66] *Id.*

[67] *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 214 (1976).

[68] *See* Bell v. Cameron Meadows Land Co., 669 F.2d 1278, 1281 n.7 (9th Cir. 1982); H.K. Porter Co. v. Nicholson File Co., 482 F.2d 421, 425–26 (1st Cir. 1973); Elec. Specialty Co. v. Int'l Controls Corp., 409 F.2d 937, 940–41 (2d Cir. 1969); *Dyer v. E. Tr. & Banking Co.*, 336 F. Supp. 890, 913–14 (D. Me. 1971) (stating that a "sensible and coherent interpretation" of Section 10(b) and Section 14(e) requires interpretation that implicates a corresponding damage remedy under the two statutes). The court further wrote in *Dyer* that "[t]here is every reason to believe that Congress intended the remedies to be similar." 336 F. Supp. at 914; *see also, e.g.,* Loewenstein, *supra* note 3, at 1311-1312 (noting that the other circuits deem scienter to apply to both Rule 10b-5 and Section 14(e) claims).

[69] *See*, *e.g.*, Smallwood v. Pearl Brewing Co., 489 F.2d 579, 605 (5th Cir. 1974) (quoting Chris-Craft Indus. v. Piper Aircraft Corp., 480 F.2d 341, 362 (2d. Cir. 1973)) (stating that the court is in accord with the Second Circuit and that "the same elements must be proved to establish a violation of either [Section 14(e)] or [Rule 10b-5]").

[70] *See, e.g.*, Lorillard v. Pons, 434 U.S. 575, 581 (1978).

because its language is virtually identical to that of Rule 10b-5.[71] Just before stating this, however, the court also acknowledged that § 14(e) was relatively new and that it had not yet been the subject of extensive judicial construction.[72] By comparison, in 1974, only one year after *Chris-Craft*, the Fifth Circuit issued its own opinion in *Smallwood v. Pearl Brewing Co.* that was aligned with the Second Circuit.[73] In *Smallwood*, the Fifth Circuit reasoned that Congress, presumably knowingly, accepted "the precedential baggage" of Rule 10b-5 when it adopted the rule's substantive language.[74]

C. § 10(b) and Rule 10b-5

The language of § 14(e), § 10(b), and Rule 10(b)(5) are so similar that the interpretation of one impacts the interpretation of the other.[75] However, at the same time, the language is subtly different that there remains ambiguity in how each provision should be enforced.[76] For example, as the enforcing statute, the text of § 10(b) is as follows:

> 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—[t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.[77]

Evidently, only part of § 10(b)—specifically the part about "manipulative or

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[71] *See Chris-Craft*, 480 F.2d at 362.

[72] *See id.*

[73] *See Smallwood*, 489 F.2d at 605.

[74] *See id.* After all, as the Supreme Court has stated, when adopting a new law, "Congress normally can be presumed to have had knowledge of the interpretation given to the incorporated law, at least insofar as it affects the new statute." *See also Lorillard*, 434 U.S. at 581.

[75] *See*, *e.g.*, *Smallwood*, 489 F.2d at 605 (5th Cir. 1974) (quoting *Chris-Craft*, 480 F.2d at 362) (stating that the court is in accord with the Second Circuit and that "the same elements must be proved to establish a violation of either [Section 14(e)] or [Rule 10b-5]").

[76] *See infra* text accompanying notes 77–83 (highlighting the differences in statutory language); *see also infra* text accompanying notes 186–99 (explaining how the differences in statutory language, coupled with legal precedent, show that the text of § 14(e) does not require scienter).

[77] 15 U.S.C. § 78j(b) (1934).

deceptive devices"—is *in pari materia* with, or possesses similar language to, the language of § 14(e).[78] Moreover, this part is only similar to the second of the two forms of conduct that § 14(e) prohibits.[79] By comparison, the text of Rule 10b-5 is as follows:

> 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 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.[80]

Based on the text, it is evident that only subsection (b) of Rule 10b-5 is *in pari materia* with the language of § 14(e).[81] Specifically, this similarity relates to the first of the two forms of conduct that is prohibited by § 14(e).[82] In sum, the text of § 14(e) clearly prohibits two distinguishable forms of conduct. The text of Rule 10b-5 is similar only to the first form of conduct—which involves making any untrue statement or omission regarding a material fact—while the text of § 10(b) is similar only to the second form of conduct—which involves employing fraudulent, deceptive, or manipulative devices.[83]

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[78] *Compare* § 78j(b), *with* 15 U.S.C. § 78n(e) (1976) (noting that the main similarity between these statutes is language around prohibiting "manipulative or deceptive devices").

[79] There are two forms of conduct prohibited by Section 14(e), as illustrated by application of the Surplusage Canon, and employing any "manipulative or deceptive devices" is only one form of conduct prohibited by Section 14(e). *See id.*

[80] 17 C.F.R. § 240.10b-5.

[81] *Compare* § 240.10b-5, *with* § 78n(e) (noting that the main similarity between Section 14(e) and Rule 10b-5 is language around making "any untrue statement of a material fact" or omissions of material facts).

[82] There are two forms of conduct prohibited by Section 14(e), as illustrated by application of the Surplusage Canon, and making any untrue statement or omission of a material fact is only one form of conduct prohibited by Section 14(e). *See id.*

[83] *See id.*

II. THE NEGLIGENCE V. SCIENTER DEBATE

Because *Varjabedian* is so recent, only dismissed by the district court in February 2020, the issue of negligence or scienter as it relates to a § 14(e) claim has not been resolved.[84] Now, significant ambiguity is almost unanimously recognized throughout the M&A industry as to which standard applies.[85] Specifically, there is substantial uncertainty in the M&A industry regarding the requisite mental state for § 14(e) claims and whether the lower negligence standard will result in higher transaction costs.[86] Moving forward, in light of the Ninth Circuit's decision in *Varjabedian*, the issue of whether scienter is required in a claim under § 14(e) remains open—or, at least, in question.[87]

The Ninth Circuit ruled that § 14(e) prohibits more forms of conduct than § 10(b) alone.[88] Therefore, according to the court, § 14(e) does not necessarily require scienter simply because § 10(b) does.[89] However, the court also proceeded to determine that § 14(e) actually compels a negligence standard.[90] In part, the Ninth Circuit did so because it determined that the legislative history and apparent intent of the Williams Act points toward negligence.[91] As the court noted, the Williams Act was created with the primary intention of ensuring informed shareholder voting during tender offers.[92] Considering § 14(e)'s specific purpose

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[84] *See* Sevier, *supra* note 17, at 125.

[85] In the Respondent's Brief in Opposition filed with the Supreme Court in *Varjabedian*, the plaintiff argued that two circuits were overruled by *Hochfelder* and *Aaron* and that no other circuits have actually addressed the issue. *See* Sevier, *supra* note 17, at 125; *see also*, Brief for Respondent in Opposition to Petition for Writ of Certiorari at 1, *Varjabedian III*. Therefore, according to the plaintiff, there is no outstanding issue for the Supreme Court to resolve. *See* Sevier, *supra* note 17, at 125. Nevertheless, "the issue of the circuit split is widely accepted by the circuits, M&A companies, attorneys, etc." *See* Sevier, *supra* note 17, at 125.

[86] *See* Matthew A. Powell, *The Vital Need to Eliminate a De Facto Negligence Standard Under Section 14(e) of the Exchange Act*, 15 HASTINGS BUS. L.J. 253, 255 (2019) (stating that M&A lawsuits have become so common that "businesses view merger objection suits simply as a transaction or merger tax on the tender offer" and proposing that this economically adverse reality will only increase after *Varjabedian*).

[87] *See Varjabedian II*, 888 F.3d 399, 404 (9th Cir. 2018) (stating that a "plain reading of Section 14(e) readily divides the section into two clauses"); *see also* SCALIA & GARNER, *supra* note 62, at 174 (highlighting the Surplusage Canon).

[88] *See Varjabedian II*, 888 F.3d at 408-09. Specifically, the court wrote that the text of the first clause in Section 14(e) "is devoid of any suggestion that scienter is required" and that such language in the first clause only requires negligence. *Id.* at 408.

[89] *See id.*

[90] *See id.*

[91] *See id.* at 407–08.

[92] *See id.* at 408; *see also* Giguere, *supra* note 33, at 1050.

as a broad antifraud provision and that negligence is sufficient for fraud under common law, the Ninth Circuit makes a sound and reasonable argument that the negligence standard is more closely aligned with legislative intent.[93]

Based on Supreme Court precedent, legislative intent should be seriously considered in determining the proper standard.[94] However, a staunch textualist might disagree with this proposition.[95] Opposing the relevance of legislative intent from a textualist perspective, Justice Scalia opined that such considerations are "nothing but an invitation to judicial lawmaking."[96] Nevertheless, the Supreme Court has directly stated that legislative intent is an important factor when interpreting securities law.[97] If the Supreme Court wanted to affirm or reverse the Ninth Circuit's decision based on legislative history and perceived legislative intent, or even based on economic policy concerns, then it could have.[98] Because the Court chose not to act, therefore, one might reasonably infer that the Court declined to rule—at least in part—because it preferred to defer the specific question of negligence or scienter to the legislative process.[99]

Regardless, the Court's decision to refrain has left the issue open to be clarified by regulators.[100] Looking forward, interpreting prior securities fraud

[93] *See Varjabedian*, 888 F.3d at 408 (describing various pieces of legislative history from the Williams Act that point towards shareholder protection as being of utmost importance); *see also* McNollgast, *The Use of Positive Political Theory in Statutory Interpretation*, 57 LAW & CONTEMP. PROBS. 3, 5 (Winter 1994) (highlighting the third step of statutory interpretation that go beyond the text to assess legislative history and guidance).

[94] In the seminal case, *Church of the Holy Trinity v. United States,* the Supreme Court first established that it is a "familiar rule, that a thing may be within the letter of the statute and yet not within the statute, because not within its spirit, nor within the intention of its makers." 143 U.S. 457, 459 (1892). For example, the importance of legislative intent in American jurisprudence was relied on in *United Steelworkers of America v. Weber* for the Supreme Court to interpret the intent of the Civil Rights Act of 1964. 443 U.S. 193, 195 (1979).

[95] According to a strict textualist, for example, the doctrine of legislative intent that flows from the Court's reasoning in *Holy Trinity* allows judges to substitute their personal preferences for the will of Congress. *See* Public Citizen v. Dep't of Just., 491 U.S. 440, 457 (1989).

[96] ANTONIN SCALIA, A MATTER OF INTERPRETATION: FEDERAL COURTS AND THE LAW 21 (Amy Gutmann et al. eds., 1998).

[97] As stated in *Hochfelder*, legislative intent is important to consider when interpreting statutes. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212–14 (1976).

[98] *See* David S. Law & David Zaring, *Law Versus Ideology: The Supreme Court and the Use of Legislative History*, 51 WM. & MARY L. REV. 1653, 1654 (2010).

[99] *See* Sevier, *supra* note 17, at 125.

[100] *See* Adrian Vermeule, *Deference and Due Process*, 129 HARV. L. REV. 1890, 1890–91 (2016) (discussing procedural due process).

precedent is crucial to determining whether negligence or scienter standard should apply to § 14(e) claims.[101] In addition, one's view of the historical and practical interconnectedness between a § 14(e) claim and a Rule 10b-5 action, for example, plays a critical role in determining the proper outcome.[102] Further, competing policy positions about the economic implications of a more lenient standard on transaction costs are important to assessing the best standard.[103]

A. Assessing Legal Precedent

The Ninth Circuit critically noted that § 14(e) stands alone as an enforceable federal statute while enforcement of Rule 10b-5 is limited to the power granted in § 10(b).[104] Thus, in staunch contrast to the opposing circuits, the Ninth Circuit reasoned in *Varjabedian* that legal precedent regarding Rule 10b-5 adjudication does not actually require § 14(e) claims to allege scienter.[105] Rather, the Ninth Circuit held that § 14(e) should require only negligence.[106]

The Ninth Circuit emphasized that the Supreme Court in *Hochfelder* previously acknowledged the possibility of the language of Rule 10b-5 requiring only a negligence standard.[107] Specifically, the Court stated in *Hochfelder* that Rule 10b-5(b) "could be read [in isolation] as proscribing, respectively, *any type* of material misstatement or omission . . . *whether the wrongdoing was intentional*

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[101] *See id.*

[102] *See* Loewenstein, *supra* note 3, at 1312 (arguing that Section 14(e) and Rule 10b-5 differ in both language and legislative history, which thus requires different interpretation and application).

[103] *See* Powell, *supra* note 86, at 255-66.

[104] The Ninth Circuit wrote:

> Put simply [the Supreme Court held in *Ernst & Ernst v. Hochfelder* that] Rule 10(b)-5 requires a showing of scienter because it is a regulation promulgated under Section 10(b) of the Exchange Act, which allows the SEC to regulate *only* "manipulative or deceptive device[s]." This rationale regarding Rule 10b-5 does not apply to Section 14(e), which is a statute, not an SEC rule.

See Varjabedian II, 888 F.3d 399, 406 (9th Cir. 2018) (internal citations omitted) (emphasis added).

[105] *See id.* at 405–06.

[106] *See id.* at 408 (holding that "the first clause of Section 14(e) requires a showing of only negligence, not scienter").

[107] *See Varjabedian II*, 888 F.3d at 406. The Supreme Court noted that "the wording of Rule 10b-5(b) could reasonably be read as imposing a scienter standard *or a negligence standard*." *See id.* (quoting Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212 (1976)) (emphasis added).

or not."[108]

In fact, the Supreme Court specifically wrote that the language of § 10(b), rather than the language of Rule 10b-5, compelled a scienter standard, highlighting the fact that § 10(b) is quite specific in its use of the words "manipulation and deception," as well as "of implementing devices and contrivances—the commonly understood terminology of intentional wrongdoing."[109] Because Rule 10b-5 was adopted under authority granted to the SEC under § 10(b), the Court determined that the scope of Rule 10b-5 cannot exceed the power granted under § 10(b)—the controlling statute.[110] Therefore, the Court did not determine that Rule 10b-5 required scienter because of its own specific language but rather held that Rule 10b-5 necessarily required scienter because the specific language of § 10(b) required scienter.[111] The Ninth Circuit emphasized this fact in *Varjabedian*.[112]

To further support its position, the Ninth Circuit referenced *Aaron v. SEC* as requiring a negligence standard for actions under § 17(a)(2) of the Securities Act of 1933 (Securities Act).[113] Instead of looking to *Hochfelder* and its interpretation of § 10(b) and Rule 10b-5, the Ninth Circuit found that the Supreme Court's decision in *Aaron* offered critical guidance regarding the requisite mental state for a statute similarly worded to § 14(e).[114] In *Aaron*, the Court held that § 17(a)(2) of the Securities Act, which has nearly identical wording to § 14(e) of the Exchange Act, is devoid of the scienter requirement.[115] Therefore, because § 17(a)(2) and § 14(e) have nearly identical wording, the Ninth Circuit determined that § 14(e) claims are also devoid of the scienter requirement.[116]

In its ruling, the Ninth Circuit used a similar line of reasoning as other lower courts have to guide its interpretation of § 14(e)—determining that interpretation of one statute with similar language provides guidance as to how another statute

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[108] *Hochfelder,* 425 U.S. at 212 (emphasis added).

[109] *See id.* at 214 (stating that "the original interpretation of Rule 10b-5 was compelled by the language and history of § 10(b)" and that "[w]hen a statute [Section 10(b)] speaks so specifically in terms of manipulation and deception . . . we are quite unwilling to extend the scope of the statute to negligent conduct").

[110] *See id.* at 212–14.

[111] *See id.*

[112] *See Varjabedian II*, 888 F.3d at 405–06.

[113] *See id.* (citing Aaron v. SEC, 445 U.S. 680, 696–97 (1980)).

[114] *See id.* (noting that the provision at issue in *Aaron*, Section 17(a)(2) of the Securities Act of 1933, and Section 14(e) have nearly identical wording).

[115] *See Aaron*, 446 U.S. at 696 (quoting Securities Act of 1933, § 17(a)(2), 15 U.S.C.A. § 77q(a)(2)) (stating that language "which prohibits any person from obtaining money or property 'by means of any untrue statement of a material fact or any omission to state a material fact,' is devoid of any suggestion whatsoever of a scienter requirement").

[116] *See Varjabedian II*, 888 F.3d at 406.

should be interpreted.[117] To rebut any presumption that these claims are not comparable because they are from different statutes, the Ninth Circuit stated that "statutes dealing with similar subjects should be interpreted harmoniously."[118] Furthermore, in support of its prior decision in *Jonah R. vs. Carmona*, which also ruled that § 14(e) and § 17(a) should be construed similarly, the court added that "[b]eyond their nearly identical text, § 14(e) and § 17(a) serve similar purposes. Both provisions govern disclosures and statements made in connection with an offer of securities, albeit in different contexts."[119]

Regardless of persuasion from this comparison, however, courts have disagreed on whether any similarity between § 14(e) and Rule 10b-5 should compel scienter.[120] The Supreme Court was clearly compelled to hold that Rule 10b-5 requires scienter in *Hochfelder* because it determined that § 10(b)—the authorizing statute—requires scienter.[121] Therefore, the pivotal question is whether § 14(e) and § 10(b)—both of which are federal statutes—are similarly worded to the point that they should be interpreted the same.[122] Importantly, the language of § 10(b) and § 14(e) are not the same as it relates to the implied requisite mental state.[123] While § 10(b) specifically states that the use of "any manipulative or

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[117] *See id.* at 405 (stating that "the decisions from these five circuits rest on the shared text found in both Rule 10b-5 and Section 14(e)"); *see also id.* at 406 (citing *Aaron*, 446 U.S. at 696-97) (stating that "*Aaron* took a further step by holding that the plain language of Section 17(a)(2), which is largely identical to the first clause of Section 14(e), requires a showing of negligence, not scienter").

[118] Prior to *Varjabedian*, the Ninth Circuit wrote in *Jonah R. v. Carmona* that "[a]lthough Section 17(a)(2) appears in the Securities Act of 1933, while Section 14(e) appears in the Exchange Act, 'statutes dealing with similar subjects should be interpreted harmoniously.'" *See* Jonah R. v. Carmona, 446 F.3d 1000, 1007 (9th Cir. 2006) (quoting Jett v. Dallas Indep. Sch. Dist., 491 U.S. 701, 738–39 (1989) (Scalia, J., concurring)).

[119] *Varjabedian II*, 888 F.3d at 406.

[120] *Id.* (citing Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212-214 (1976)) (stating that "the scienter requirement is not rooted in the text of Rule 10b-5, but rather in the relationship between Rule 10b-5 and its authorizing legislation").

[121] *See id.* (stating that the rationale used in *Hochfelder* to determine that Rule 10b-5 requires scienter "does not apply to Section 14(e), which is a statute, not an SEC rule").

[122] *See id.*

[123] 15 U.S.C. § 78j(b) (1934) and 15 U.S.C. § 78n(e) (1976). Rather than speak specifically and exclusively in terms of manipulation or deceptiveness, which seem to imply more than mere negligence, section 14(e) states that it is "unlawful for any person to make any untrue statement of a material fact or omit to state any material fact . . . *or* to engage in any fraudulent, deceptive, or manipulative acts or practices . . . ." § 78n(e) (emphasis added). Contrasted with section 10(b), section 14(e) evidently provides a disjunctive test with the use of the word "or," prohibiting either untrue statements or omissions of material fact in addition to "fraudulent, deceptive, or manipulative" conduct. *See* § 78j(b); *see also* § 78n(e).

deceptive device or contrivance" is prohibited, § 14(e) does not use such precise language.[124]

The Ninth Circuit also argues that § 10(b) is not similar to the first form of conduct prohibited by § 14(e)—namely, the prohibition of untrue statements or omissions of a material fact—and thus should be construed to prohibit more types of conduct than § 10(b) merely does.[125] Thus, according to the Ninth Circuit, the question of whether negligence applies to the first form of conduct prohibited by § 14(e)—making any untrue statement or omission of a material fact—should remain open despite the Supreme Court's decision in *Hochfelder*.[126] In fact, in *Hochfelder*, the Supreme Court itself also acknowledged *in dicta* that the language of Rule 10b-5 might plausibly be construed to require negligence alone.[127] Nevertheless, in highlighting statutory inconsistencies between § 14(e) and § 10(b) in *Varjabedian*, the Ninth Circuit exposed an important and unresolved issue in the existing securities regulatory framework.[128] Specifically, the Ninth Circuit illustrated—through textualist doctrine and application of well-founded canons of statutory interpretation—that existing § 14(e) jurisprudence was flawed in wrongly assuming the language *in pari materia* with Rule 10b-5 mandated § 14(e) to require scienter.[129]

The Ninth Circuit's opinion in *Varjabedian* highlights the stark contrast in

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[124] *Compare* §78j(b), *with* § 78n(e) (noting that the quoted language of the statutes, although similar, is noticeably distinct in construction). For example, one might argue that "to use or employ any manipulative or deceptive device"—as used in section 10(b)—is clearly distinguishable, in terms of the requisite mental state—from engaging "in any fraudulent, deceptive, or manipulative acts or practices"—as used in section 14(e). *See* § 78n(e).

[125] *See Varjabedian II*, 888 F.3d at 407.

[126] The Supreme Court has not specifically ruled on whether this form of conduct requires negligence or scienter because it only ruled that Rule 10b-5 requires scienterbecause section 14(e) does. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212–14 (1976).

[127] *See id.*

[128] *See Varjabedian II*, 888 F.3d at 405-06 (explaining that the Supreme Court determined Rule 10b-5 to require scienter because its authorizing statute, Section 10(b), requires scienter, rather than due to its specific language).

[129] *See id.* at 405 (noting that the other five circuits' decisions rest on the flawed rationale that shared text between Rule 10b-5 and Section 14(e) mandates importation of the scienter requirement to Section 14(e) claims). To reiterate, Section 14(e) undoubtedly prohibits more forms of conduct than Section 10(b) alone does. *See id.* at 404 (emphasizing that the word "or" separates the two clauses of Section 14(e) and thus creates a disjunctive test).

legal reasoning among splitting circuits on the issue.[130] Specifically, the outstanding question of whether a negligence or scienter standard should apply to § 14(e) claims has resulted, at least in part, from differing interpretations of Supreme Court precedent.[131]

B. Relevant Policy Factors

In addition to legal precedent, competing policy factors help to define both sides of the negligence or scienter question.[132] Many of these concerns were summarily outlined in the several amicus briefs submitted to the Court in the *Varjabedian* case.[133] For example, one might claim that a negligence standard would only increase frivolous class-action securities litigation, sometimes called merger objection suits, because the lower standard would be more enticing and likely increase settlement value.[134] By contrast, another might point out that the purpose of the Exchange Act was largely to protect investors.[135] Because a negligence standard conceivably does more to protect investors in a wider variety of situations, one might argue that it is better aligned with the intent of the

[130] In *Varjabedian*, the Ninth Circuit opined that the other circuits erroneously interpreted certain cases, such as Chris-Craft Indus. Inc. v. Piper Aircraft Corp., 480 F.2d 341 (2d Cir. 1973), and Smallwood v. Pearl Brewing Co., 489 F.2d 579, 605 (5th Cir. 1974), to hold that Section 14(e) requires scienter because Rule 10b-5 does. *See Varjabedian II*, 888 F.3d at 405–06.

[131] While acknowledging that the Supreme Court held that Rule 10b-5(b) requires scienter in *Hochfelder*, the Ninth Circuit emphasized that "the Court's conclusion that scienter is an element of Rule 10b-5(b) had nothing to do with the text of Rule 10b-5." *See Varjabedian II*, 888 F.3d at 405-06. Rather, according to the Ninth Circuit, Rule 10b-5 requires scienter because Section 10(b), with distinguishable and more clear language, requires scienter. *See id.* Because Rule 10b-5 is an SEC regulation rather than a statute, its enforcement relies entirely on the authority granted under Section 10(b), the statute it was promulgated under. *See id.* (quoting 15 U.S.C. §78j(b) (1934)) (stating that "Rule 10b-5 requires a showing of scienter because it is a regulation promulgated under Section 10(b) of the Exchange Act, which allows the SEC to regulate *only* 'manipulative or deceptive device[s]'").

[132] *See* Powell, *supra* note 86, at 255.

[133] *See* Sevier, *supra* note 17, at 106 (arguing that "[t]he decision of the Ninth Circuit and the Brief in Opposition filed by the respondent provide the strongest legal arguments based on the plain language of the statute and well-reasoned precedent, while the Petition for Writ of Certiorari and Amicus Briefs make strong policy arguments and somewhat tenuous legal arguments").

[134] *See* Powell, *supra* note 86, at 253–56.

[135] *See* Keller & Gehlmann, *supra* note 26, at 329–30 (describing the purpose of the Exchange Act and the goal of registration to protect the truthfulness surrounding investment decisions).

Exchange Act.[136] Further, the negligence standard finds support under English common law, which has traditionally deemed negligence alone to be sufficient for liability in tort claims.[137]

Some of these policy factors were certainly at issue in *Varjabedian*; for example, the defendant argued that the negligence standard encourages frivolous litigation and increases transaction costs.[138] Moreover, according to the defendant, the Exchange Act's liberal jurisdictional provision would encourage forum-shopping in the Ninth Circuit for § 14(e) claims.[139] According to those in favor of the defendant, the Ninth Circuit's decision in *Varjabedian* now effectively creates a de facto negligence standard across the country for § 14(e) claims.[140]

However, in contrast to economic concerns about frivolous litigation and in line with those who emphasize investor protection, the Second Circuit held in *Gerstle v. Gamble-Skogmo, Inc.* that a negligence standard should apply for an action under § 14(a), which is also part of the Williams Act.[141] In *Gerstle*, important policy considerations such as the duty of care owed by one party to another affected the court's legal interpretation of the Williams Act through case law.[142] In addition, the court reasoned, requiring truthfulness and accuracy in disclosure statements helps ensure that objectives of the Exchange Act are met.[143]

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[136] *See* Patricia S. Abril & Ann Morales Olazabal, *The Locus of Corporate Scienter*, 2006 COLUM. BUS. L. REV. 81, 89–90 n.24 (2006) (noting that the Private Securities Litigation Reform Act requires plaintiffs to "plead particular facts that give rise to a strong inference of scienter"). Pleading facts that give rise to a strong inference of scienter is a considerably high standard, and plaintiffs' claims are often unable to proceed in cases due to failure to meet this high standard. *See, e.g.*, Pension Tr. Fund v. Apple Comput., Inc., No. 03-16614, 2005 U.S. App. LEXIS 5511 (9th Cir. 2005) (holding that, while the allegations might permit a reasonable inference of negligence, the pleadings "did not reach the level of scienter required for liability under the Private Securities Litigation Reform Act"). In securities transactions, "purchasers or sellers are less able to protect themselves against misrepresentations" due to requirements of pleading scienter because investors "cannot realistically inspect a corporation's books, assets, or business practices, but must rely upon the representations of others" and thus a standard of reasonable care should arguably apply. *See* David Strout, *Unlawful Securities Transactions and Scienter: An Emasculating Requirement*, 1 U. PUGET SOUND L. REV. 366, 373 (1978).

[137] Kuehnle, *supra* note 8, at 153.

[138] *See* Brief for the Securities and Financial Markets Association, *supra* note 6, at 13–14.

[139] *See id.*

[140] *See id.*

[141] *See* Gerstle v. Gamble-Skogmo, Inc., 478 F.2d 1281, 1300 (2d Cir. 1973) (writing that "[a] broad standard of culpability . . . will serve to reinforce the high duty of care owed by a controlling corporation to minority shareholders").

[142] *See id.*

[143] Keller & Gehlmann, *supra* note 26, at 329–31.

As shown in *Gerstle*, the Second Circuit implied that the lower negligence standard does more to protect investors.[144]

The Second Circuit also noted in *Gerstle* that investors are owed a duty of care regarding the truthfulness of disclosure statements and that privity is established because of this relationship.[145] Specifically, the Second Circuit reasoned in *Gerstle* that parties involved in suits under § 14 of the Williams Act maintain privity because the defendant corporation owes the plaintiff shareholder a fiduciary duty.[146] This reasoning is built on the objective to protect shareholders and the fiduciary relationship they have established.[147]

Expanding this position, the Second Circuit wrote that the question of whether a relationship between parties enjoys "privity" bears heavily on determining the appropriate standard of culpability.[148] Privity has traditionally been protected through legal recourse.[149] Interestingly, privity—which includes, for example, pecuniary interest in a particular transaction—has traditionally required negligence rather than scienter in an action for fraud.[150]

In addition, although § 14(a) deals with securities fraud specifically regarding minority shareholder proxy statements rather than securities fraud related to tender offers, the court noted in *Gerstle* that both provisions—§ 14(a) and § 14(e)—are part of the Williams Act and thus have similar legislative history, implying similar legislative intent.[151] As such, the Second Circuit's interpretation of § 14(a) cuts toward § 14(e) potentially also permitting negligence as sufficient.[152] If a negligence standard for § 14(a) claims operates to better protect investors, as the Second Circuit says it does, then logic might follow that a negligence standard for § 14(e) claims would also do more to protect investors.[153] If so, then there is a persuasive argument that the negligence standard would be more aligned with the

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[144] *See Gerstle*, 478 F.2d at 1300 (1973).

[145] *See id.*

[146] *See id.* at 1300–02.

[147] *See id.*

[148] *See id.* at 1300.

[149] *See id.* For reference, "privity" may be defined as the "connection or relationship between two parties, each having a legal recognized interest in the same subject matter (such as a transaction)." *Privity*, BLACK'S LAW DICTIONARY (11th ed. 2019).

[150] *See* Gerstle v. Gamble-Skogmo, Inc., 478 F.2d 1281, 1300 (2d Cir. 1973). The Second Circuit also noted that "the common law itself finds negligence sufficient for tort liability where a person supplies false information to another with the intent to influence a transaction in which he has a pecuniary interest."

[151] Loewenstein, *supra* note 3, at 1339.

[152] *See Gerstle*, 478 F.2d at 1300–02.

[153] *See id.* at 1300-01.

intent of the Exchange Act in general.[154] More specifically, one might argue that a negligence standard aligns with the intent of § 14(e) of the Williams Act as a "broad antifraud provision" to protect investors.[155]

However, while there is plausible legal reasoning to contend that negligence is sufficient for § 14(e) claims, the economic policy considerations surrounding implementation of a negligence standard must be addressed as these concerns are significant—as evidenced by the plethora of large financial players who rushed to file amicus briefs in *Varjabedian*.[156] According to Petitioners in *Varjabedian*, and most of the organizations that filed amicus briefs, the Ninth Circuit's decision to implement a negligence standard for § 14(e) claims will substantially raise transaction costs as frivolous litigation and forced settlement will likely become even more commonplace.[157]

III. ANALYZING THE CIRCUIT SPLIT

When *Varjabedian* was argued in the Supreme Court, the parties largely argued, and the Court presumably considered, competing positions about legal precedent in addition to substantial focus on economic policy factors.[158] As shown through the briefs filed with the Supreme Court, the Ninth Circuit's decision in

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[154] Keller & Gehlmann, *supra* note 26, at 329–30 (describing the purpose of the Exchange Act and the goal of registration to protect the truthfulness surrounding investment decisions).

[155] Section 14(e) of the Williams Act—positioned within the context of the larger Securities Exchange Act of 1934—serves a strong purpose to help protect investors by providing broad ranges of conduct that is prohibited in tender offers. *See* Piper v. Chris-Craft Indus., 430 U.S. 1, 24 (1977) (noting that the Williams Act also contains a broad antifraud prohibition [Section 14(e)]).

[156] *See* Sevier, *supra* note 17, at 116 (stating that *Varjabedian* might plausibly deter foreign direct investment in the United States because of increased risk and cost of litigation); *see also* Powell, *supra* note 86, at 253, 255 (citing Brief for the Securities and Financial Markets Association, *supra* note 6, at 9, 12) (describing how between 85-90% of public M&A deals were challenged in 2015 and that experts expect this trend to continue while also noting that the "problem has grown so routine that businesses view merger objection suits simply as a transaction or merger tax on the tender offer").

[157] *See* Petition for Certiorari at 25 (citing In re Trulia, Inc. Stockholder Litig., 129 A.3d 884, 891 (Del. Ch. 2016)) (arguing that nearly all transactions involving acquisition of a public corporation provoke class-action lawsuits and that the vast majority of those suits, roughly 78%, are dismissed). Due to large risks associated with class action lawsuits and the time-consuming and expensive nature of discovery in these suits, Petitioners argue that defendants will often be forced to settle frivolous suits regardless of merit. *See id.* at 891.

[158] *See*, *e.g.*, Brief of the Securities Industry and Financial Markets Association, *supra* note 6, at 19.

Varjabedian has significant implications on the regulatory framework surrounding securities tender offers, creating uncertainty among offerors, offerees, and those that represent and advise the deal-making parties.[159] Further, the adoption of a negligence standard under § 14(e) has fostered substantial concern among several prominent players in the M&A industry.[160] Various organizations and individuals have cogently advanced their own theories regarding economic implications and other policy factors resulting from a negligence standard.[161] That being said, because the Ninth Circuit's decision in *Varjabedian* creates uncertainty of great magnitude, familiarity with competing ideologies is important to properly analyze the case's impact on the securities regulatory landscape and assess the most plausible path going forward—including the potential viability of the negligence standard for § 14(e) claims.[162]

From a policy standpoint, rejecting the negligence standard is worth consideration based on the sheer volume of M&A lawsuits and increased transaction costs that result from excessive litigation.[163] There is a strong policy argument that the negligence standard might not be economically viable going forward.[164] Because economic policy concerns—and other politically legitimate values—may arguably be better resolved by the legislature, however, perhaps the

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[159] *See* Sevier, *supra* note 17, at 125.

[160] *See e.g.,* Brief for the Securities Industry and Financial Markets Association, *supra* note 6, at 9, 12, 13–14 (noting potential problems stemming from drastic increase in number of "merger objection" suits filed and that *Varjabedian* will create a de facto national negligence standard that encourages frivolous suits).

[161] *See, e.g.,* Brief for the Chamber of Commerce of the United States of America as Amicus Curiae at 1, 22, *Varjabedian III*, 139 S. Ct. 1407 (2019) (No. 18-459) (arguing that vast majority of merger objection lawsuits typically settle within three months and do not provide much value to shareholders but rather hefty fees for plaintiff attorneys); *see also* Brief for the Securities and Financial Markets Association, *supra* note 6, at 9, 10 (arguing that defendants frequently settle merger objection cases that are frivolous in an effort to avoid the potential death of their deal).

[162] Because *Varjabedian* was dismissed on grounds other than the issue of whether negligence or scienter is the proper standard for Section 14(e) claims, that question is still outstanding and undecided by the Supreme Court, resulting in a circuit split. *See Varjabedian IV*, No. SACV 15-00554-CJC (JCDx), 2020 U.S. Dist. LEXIS 40037, *33 (C.D. Cal. 2020). There are several key players who have expressed competing ideologies and policy concerns in this case, yet, there is no clear path forward. *See id.*; *see also, e.g.*, Brief for the Securities and Financial Markets Association, *supra* note 6, at 9.

[163] *See* Powell, *supra* note 86, at 253 (providing statistics that 85-90% of public M&A deals were challenged in 2015 and that this trend is expected to continue upward).

[164] *See, e.g., id.* at 253–56. *But see, e.g.*, Loewenstein, *supra* note 3, at 1313 (arguing that Section 14(e) claims, as opposed to Rule 10b-5 actions, should not require proof of scienter).

Supreme Court correctly dismissed *Varjabedian* to place the issue at the feet of the legislative branch.[165] Nevertheless, due to the brevity of the Court's dismissal as improvidently granted, the Court's full rationale remains unclear.[166] That being said, the legal profession must move forward to advise on M&A transactions and other tender offers despite uncertainty and potential litigation chaos.[167]

The Ninth Circuit certainly deserves credit for correctly pointing out that proper application of the canons of statutory interpretation illustrate that § 14(e) prohibits more types of conduct than § 10(b) alone does.[168] Moreover, the court correctly showed that Rule 10b-5 jurisprudence does not compel § 14(e) to necessarily require scienter.[169] Now, given that the Supreme Court dismissed *Varjabedian*, the onus falls on regulators—either Congress or the SEC—to help resolve outstanding ambiguity.[170]

A. Why the Ninth Circuit Was Correct to Identify Erroneous § 14(e) Jurisprudence

The Supreme Court has endorsed the well-known textualist doctrine known as the plain-meaning rule, which enjoys rich legal tradition in American

[165] *See* Sevier, *supra* note 17, at 125.

[166] *See id.* at 105.

[167] *See id.* at 125 (describing how the circuit split is widely accepted by M&A companies, attorneys, and circuits courts and that there is no clear conclusion on the issue); *see also Varjabedian III*, 139 S. Ct. 1407, 1407 (2019).

[168] The use of the word "or" to create a disjunctive test shows that Section 14(e) prohibits more conduct than is simply prohibited by Section 10(b) alone. *See* SCALIA & GARNER, *supra* note 62, at 174; *see also Varjabedian II*, 888 F.3d 399, 404 (9th Cir. 2018) (stating that a "plain reading of Section 14(e) readily divides the section into two clauses").

[169] As discussed, the Supreme Court determined in *Hochfelder* that Rule 10b-5 requires scienter because Section 10(b) does. *Compare* 15 U.S.C. § 78j(b) (1934) *with* 15 U.S.C. § 78n(e) (1976) (noting that the main similarity between these statutes is language around prohibiting "manipulative or deceptive devices"). Ernst & Ernst v. Hochfelder, 425 U.S. 185, 214 (1976).

[170] When the Court dismissed *Varjabedian* as improvidently granted, it effectively chose to leave the question of whether negligence or scienter should apply to Section 14(e) claims outstanding—thus placing the issue at the feet of the legislature. *See* Sevier, note 17, at 125. Being the overarching legislative body, Congress certainly has the ability to pass legislation that clarifies the proper standard for Section 14(e) claims. *See* U.S. CONST. art. I, § 1. More likely and practical, however, the SEC might use its rulemaking authority to clarify the proper standard. *See* 15 U.S.C. § 78n(a)(1) (1968) (providing the SEC with rulemaking authority "as necessary or appropriate in the public interest or for the protection of investors.").

jurisprudence.[171] Therefore, at least some core elements of textualism have become almost universally adopted in correctly adjudicating statutory language—such as § 14(e) of the Exchange Act.[172] For example, in *Camminetti v. United States*, the Supreme Court specified a two-step process to determine the plain meaning of a statute.[173] According to the two-step textualist approach, the first step in statutory interpretation involves determining the plain meanings of the words in the statute.[174] However, if a statute remains ambiguous despite plain-meaning analysis, then courts often turn toward other factors to determine the intent of the legislature.[175] Many renowned jurisprudential figures hold that legislative-intent analysis may include legislative history; however, other scholars and jurists argue

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[171] *See, e.g.,* Camminetti v. United States, which applied the "plain-meaning" approach to statutory interpretation:

> It is elementary that the meaning of a statute must, in the first instance, be sought in the language in which the act is framed, and if that is plain, and if the law is within the constitutional authority of the lawmaking body which passed it, the sole function of the courts is to enforce it according to its terms . . . Where the language is plain and admits of no more than one meaning, the duty of interpretation does not arise, and the rules which are to aid doubtful meanings need no discussion.

Camminetti v. United States, 242 U.S. 470, 485 (1917).

[172] Because this principle is recognized at the highest level of U.S. legal precedent, it serves as an important guide to statutory interpretation. *See* Algero, *supra* note 56, at 785–86 (noting that, in common law jurisdictions, "judicial decisions have the force of law—judge-made law or common law").

[173] In *Camminetti*, the Court determined that the first step of the process should be to assess whether the meaning of the statute is plain. *See* 242 U.S. at 485. The Court also expressed its view that, if the language of a statute is plain, then courts do not have the duty of interpretation. *Id.* Thus, because the Court's logic in *Camminetti* presents a counterfactual statement, and applying principles of formal logic for counterfactual statements, then it is also true that a court *may have a duty of interpretation*. *See* Roderick M. Chisholm, *Law Statements and Counterfactual Inference*, 15 OXFORD UNIV. PRESS 97, 98 (1955).

[174] *See Camminetti*, 242 U.S. at 485; *see also* United States v. Johnson, 680 F.3d 1140, 1144 (9th Cir. 2012) (stating that "statutory interpretation begins with the plain language of the statute").

[175] For example, in *Varjabedian*, the Ninth Circuit assessed the plain meaning of the statute, § 14(e) of the Exchange Act, before also considering that meaning within the context of legal precedent and legislative intent. *See Varjabedian II*, 888 F.3d 399, 405–06 (9th Cir. 2018) (disagreeing with the rationale the other circuits used to uphold scienter as the only sufficient mental standard in Section 14(e) claims and characterizing those decisions as being predicated on misinterpretations of legal precedent).

that it is never permissible to consult legislative history.[176] Although commentators and, more importantly, members of the judiciary may differ from time to time on whether a statute is ambiguous—and whether judges should even consult legislative history at all—there is little doubt that the plain meaning of text is a fair place to start in interpretation.[177]

According to Matthew McCubbins, Roger Noll, and Barry Weingast—known collectively as McNollgast—prevailing literature recommends five steps for statutory interpretation.[178] To summarize, one must first read the text in step one before proceeding to step two to consider the structure and purpose of the statute.[179] Where relevant, legal precedent regarding other related statutes may prove helpful in resolving ambiguities at step two.[180] If the statute remains ambiguous after these first two steps, then legislative history may be consulted in step three before assessing policy concerns—or politically legitimate values—to resolve the

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[176] Although Justice Scalia and some other strict textualists believe that legislative history should never be consulted in statutory interpretation, the majority of judges do not follow Scalia's approach to never rely on legislative history to decipher legislative intent. *See* Note, *Why Learned Hand Would Never Consult Legislative History Today*, 105 HARV. L. REV. 1005, 1006 (1992). In particular, Scalia's method is not followed by those who use the "congressional agent" mode of interpretation developed by Justice Hand and followed by Justice Posner. *See id.*

[177] *See* A. Raymond Randolph, *Dictionaries, Plain Meaning, and Context in Statutory Interpretation*, 17 HARV. J. L. & PUB. POL'Y 71, 71–72 (1994).

[178] The five steps for statutory interpretation are as follows:

> 1. Read the text; if it is not clear, then proceed to step two.
> 2. Consider the overall structure and purpose of the statute as written and, where relevant, other related statutes; if it is still not clear, then proceed to step three.
> 3. Consult the legislative history to see if, in the course of the legislative process, elected political officials left a record about how ambiguities should be resolved, and proceed to step four.
> 4. Based on the information collected in the previous steps, ascertain whether the statutory provision in question reflects politically legitimate values or the pathologies of representative democracy; if the statute remains ambiguous, or if it reflects a democratic pathology, then proceed to step five.
> 5. Invoke normative principles (varying among the authors) to determine whether the statute should be applied, and if so, how to resolve the ambiguities and compensate for the pathologies.

See McNollgast, *supra* note 93, at 5.

[179] *See id.*

[180] *See id.*

ambiguity in step four.[181] Lastly, if all else fails, then McNollgast argues that normative principles may be invoked to determine how the statute should be applied.[182]

While the first two steps are essentially undisputed, the latter two steps—those that depart from the text and recommend reflection on politically legitimate values and normative principles to resolve ambiguities—arguably extend beyond the scope of the judiciary's authority.[183] These steps often may be negatively referred to as judicial activism.[184] Nevertheless, analyzing legislative history, the third step, and even policy factors are recognized as legitimate practice among several federal courts.[185]

Still, the validity of the Ninth Circuit's argument that § 14(e) is not bound to scienter due to Rule 10b-5 jurisprudence need not rely on these latter steps.[186] Rather, the Ninth Circuit showed the errant nature of the other circuits' reasoning through the sole application of the first two steps.[187] In *Varjabedian*, the Ninth Circuit assessed the plain meaning of § 14(e) and determined, using the Surplusage

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[181] *See id.*

[182] *See id.*

[183] *See* Melanie E. Walker, Comment, *Congressional Intent and Deference to Agency Interpretations of Regulations*, 66 U. CHI. L. REV. 1341, 1354 (1999) (arguing that Congress intended factors related to political interests that "fill the gaps left in statutes" to be handled by agencies rather than the courts).

[184] *See* Corey Rayburn Yung, *Flexing Judicial Muscle: An Empirical Study of Judicial Activism in the Federal Courts*, 105 NW. U. L. REV. 1, 2 (2011) ("When a federal judge elevated his or her judgment above that of another constitutionally significant actor . . . then he or she was engaging in activity indicative of judicial activism."); *See also id.* at 7 (stating that "the term [judicial activism] normally has been overwhelmingly loaded with negative connotations").

[185] "Ultimately, many contemporary American courts view the judicial role of statutory interpretation as an opportunity to support the democratic process by applying statutes in accordance with the legislative intent and purpose." *See* Matthew B. Todd, Note, *Avoiding Judicial in-Activism: The Use of Legislative History to Determine Legislative Intent in Statutory Interpretation*, 46 WASHBURN L.J. 189, 194 (2006).

[186] *See Varjabedian II*, 888 F.3d 399, 405–06 (9th Cir. 2018) (making the argument that Section 14(e) prohibits more conduct than Section 10(b) does and based on the text, that Section 14(e) does not necessarily require scienter).

[187] *See* McNollgast, *supra* note 93, at 5 (describing how the first step involves reading the text and the second step involves consideration of the overall structure and purpose of the statute as written). The Ninth Circuit applies textual analysis in *Varjabedian* to compare Section 14(e) with Section 10(b), concluding that the Surplusage Canon and use of the disjunctive word "or" illustrates that Section 14(e) prohibits more types of conduct than Section 10(b) does. *See* 888 F.3d at 405–06. This point is established before the court then goes on to assess legislative history and intent to hold that only negligence is required. *See id.* at 406-08.

Canon, that there are two offenses for which a defendant might be held liable under the statute.[188] From there, the Ninth Circuit proceeded to assess the relevant legal precedent and case law in other circuits.[189] Essentially, the Ninth Circuit determined that the decisions from the other five circuits upholding the scienter standard rely on the faulty legal reasoning that certain shared text between Rule 10b-5 and § 14(e) equates the substantive standards required to recover under these provisions.[190]

Applying the reenactment rule, one might reasonably argue that Rule 10b-5 and § 10(b) together are similar enough to § 14(e) to be construed similarly.[191] However, the Supreme Court specifically noted that "despite the broad view of the Rule [10b-5] advanced by the Commission in this case, its scope cannot exceed the power granted the Commission by Congress under § 10(b)."[192] Thus, noting that the decision in *Ernst & Ernst v. Hochfelder* was not based on the language of Rule 10b-5 itself, the Ninth Circuit showed that the Supreme Court has really only ruled on how the language of one of the two forms of conduct prohibited by § 14(e) should be interpreted.[193]

As the Ninth Circuit identified, therefore, statutory interpretation—coupled with legal precedent—shows that § 14(e) claims should not necessarily require scienter simply because scienter has been determined to be the proper standard for § 10(b) and Rule 10b-5 claims.[194] If the other circuits had correctly compared the

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[188] *See Varjabedian II*, 888 F.3d at 404 (quoting Hart v. McLucas, 535 F.2d 516, 519 (9th Cir. 1976)); *see also* SCALIA & GARNER, *supra* note 62, at 174.

[189] *See Varjabedian II*, 888 F.3d at 404–05 (noting that the court was "persuaded that the rationale underpinning those decisions [of the other circuits] does not apply to Section 14(e) of the Exchange Act").

[190] *See id.*

[191] *See, e.g.*, Chris-Craft Indus., Inc. v. Piper Aircraft Corp., 480 F.2d 341, 362 (2d Cir. 1973).

[192] *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 214 (1976).

[193] Section 14(e) clearly prohibits two forms of conduct—making untrue statements or omissions regarding material facts *or* engaging in fraudulent, deceptive, or manipulative acts or practices. *See Varjabedian II*, 888 F.3d at 404. Otherwise, the statute would be rendered "hopelessly redundant." *See* Hart v. McLucas, 535 F.2d 516, 519 (9th Cir. 1976). Section 10(b), which the Supreme Court determined possesses language that requires scienter in *Hochfelder*, bears similar wording to only one of these two forms of conduct prohibited by Section 14(e). *Compare* 15 U.S.C. § 78j(b) (1934), *with* 15 U.S.C. § 78n(e) (1976) (noting that the main similarity between these statutes is only language around prohibiting "manipulative or deceptive devices" and not around making "any untrue statement of a material fact" or omissions of material facts).

[194] Rule 10b-5 and Section 14(e) differ in both language and purpose. *See* Loewenstein, *supra* note 3, at 1312. *Compare* § 78j(b), *with* § 78n(e) (noting that the main

language of § 14(e) with only that of § 10(b) to assess similarity, instead of Rule 10b-5 as well, those courts would have realized that the statutes significantly differ because § 14(e) distinctly prohibits conduct that is manipulative or deceptive in addition to conduct that omits or misstates materially factual information.[195] However, those courts incorrectly equated the language of § 14(e) with Rule 10b-5, holding that such similar language mandates scienter—perhaps failing to recognize that Rule 10b-5 was only bound to require scienter because the rule draws its authority entirely from § 10(b), as pointed out by the Supreme Court in *Hochfelder* and reiterated by the Ninth Circuit in *Varjabedian*.[196]

Rather than speaking specifically and exclusively in terms of manipulation or deceptiveness, which seem to imply more than mere negligence, § 14(e) states that it is "unlawful for any person to make any untrue statement of a material fact or omit to state any material fact . . . *or* to engage in any fraudulent, deceptive, or manipulative acts or practices . . . ."[197] Contrasted with § 10(b), § 14(e) evidently provides a disjunctive test with the use of the word "or," prohibiting both untrue statements or omissions of material fact in addition to "fraudulent, deceptive, or manipulative" conduct.[198] Now, in the wake of the Ninth Circuit's decision, the textualist argument for understanding that the Supreme Court has not bound § 14(e) to require scienter, but that it has not actually addressed the issue, has been

similarity between these statutes is language around prohibiting "manipulative or deceptive devices"). In addition, Rule 10b-5 is a regulation rather than a statute, so it does not carry the force of law alone and must gain its legal authority through Section 10(b), which has differing language. *See Varjabedian II*, 888 F.3d at 406.

[195] Typically, judges begin statutory interpretation by referring to prior decisions. *See* McNollgast, *supra* note 93, at 4 n.5 (citing Richard A. Posner, *Statutory Interpretation—in the Classroom and in the Courtroom*, U. CHI. L. REV. 220 (1988)). Therefore, since other courts were applying the language of Rule 10b-5 to require scienter in the context of Section 14(e), it is not entirely surprising that errant precedent that assumed that similar language to Rule 10b-5 required scienter continued to grow. *See, e.g.*, Smallwood v. Pearl Brewing Co., 489 F.2d 579, 605 (5th Cir. 1974) (citing *Chris-Craft*, 480 F.2d at 362). Nevertheless, the Conjunctive/Disjunctive Canon states that *or* specifies a disjunctive list, while the Surplusage Canon states that no words should be ignored. *See* SCALIA & GARNER, *supra* note 62, at 116, 174. As a result, considering the Supreme Court's explicit statement in *Hochfelder* that the language of Rule 10b-5 does not mandate scienter, the text of § 14(e) cannot be said to necessarily require scienter for each of the two forms of prohibited conduct.

[196] *See Hochfelder*, 425 U.S. at 212–14; *see also Varjabedian II*, 888 F.3d at 405–06.

[197] *See* § 78n(e) (emphasis added).

[198] § 78j(b); *see also* § 78n(e).

brought to the forefront of debate.[199]

B. How to Resolve the Circuit Split and Clarify Ambiguity

To help determine what the proper standard for liability under § 14(e) should be, regulatory bodies should not only consider legal precedent but also legislative history, politically legitimate values, and normative principles while balancing economic policy factors.[200] In addition, as is common practice in the United States, common law tradition should be considered.[201] This framework incorporates the fundamental factors of legal precedent, policy implications, and common law tradition to support a balanced approach to implementing or clarifying any new rule.[202]

Following McNollgast's recitation of the five steps to statutory interpretation, consulting legislative history would follow a plain-meaning textual analysis and comparison to other similar statutes in this case because textual interpretation still renders the requisite state of mind ambiguous, or at least unanswered.[203] On one hand, legislative history shows that the overarching goal of the Exchange Act is to protect investors.[204] Moreover, the fact that § 14(e) operates as a broad antifraud

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[199] While the language of Section 10(b)—which relates to fraudulent, deceptive, or manipulative acts or practices—was used by the Supreme Court to support its decision in *Hochfelder*, the language of Rule 10b-5—which relates to making untrue statements or omissions regarding material facts—has not yet been determined to require scienter. *See Hochfelder*, 425 U.S. at 212–14.

[200] Analyzing legislative history, politically legitimate values, and normative standards represent steps three through five of the McNollgast approach. *See* McNollgast, *supra* note 93, at 5. Economic policy factors, while certainly falling under politically legitimate values, standalone as a particularly important concern given the compelling intricacy and interconnectedness of the ramifications of the *Varjabedian* decision and potential adverse economic effects—as highlighted by several major players in the financial industry. *See* Powell, *supra* note 86, at 253–55; *see also* Brief for the Securities and Financial Markets Association, *supra* note 6, at 13–14.

[201] A. Raymond Randolph writes that three counter-arguments are always available against parties that urge creation of a new constitutional right: 1) "We've always done it [a different] way," 2) "Look what would happen if we did it that way," and 3) "They don't do it that way in England." *See* Randolph, *supra* note 177, at 71 (1994). The first available argument invokes legal precedent, the second refers to the policy concern that a new rule would start a slippery slope of negative events, and the third illustrates the persuasive authority of English common law on the American jurisprudential system. *Id.*

[202] *See* Randolph, *supra* note 177, at 71.

[203] *See* McNollgast, *supra* note 93, at 5.

[204] *See* Keller & Gehlmann, *supra* note 26, at 329–30 (describing the purpose of the Exchange Act and the goal of registration to protect the truthfulness surrounding investment decisions).

provision further underscores the importance of protecting investors through its enforcement.[205] As shown by the Second Circuit's analysis in *Gerstle* and expanded upon by the Ninth Circuit in *Varjabedian*, legislative history of the Williams Act in particular seems to cut toward a negligence standard.[206] To cap it all off, negligence itself has been deemed sufficient for liability in common law tort claims.[207]

On the other hand, however, there are legitimate economic concerns with excessive litigation surrounding mergers and acquisitions and subsequent increased transaction costs.[208] Furthermore, the SEC has issued relevant commentary on the subject of mini-tender offers—defined as tender offers for less than 5% of total available shares—that points toward an interpretation of scienter as the proper standard when dealing with § 14(e).[209] In the Commission Guidance on Mini-Tender Offers and Limited Partnership Tender Offers, the SEC clarifies that § 14(e)'s purpose is to prohibit "fraudulent, deceptive, and manipulative acts in connection with a tender offer," which is the language used in § 10(b) to imply scienter.[210]

In addition, throughout Regulation 14E, the SEC repeatedly uses specific language that is similar to language used in § 10(b).[211] In fact, the SEC further states its position that the antifraud provisions of § 10(b) and Rule 10b-5 should also apply to tender offers.[212] The SEC's use of such strikingly similar language to § 10(b) throughout Regulation 14E indicates the agency's presumed intent to

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[205] *See* Loewenstein, *supra* note 3, at 1311–12; *see also* Piper v. Chris-Craft Indus., 430 U.S. 1, 24 (1977).

[206] *See* Gerstle v. Gamble-Skogmo, Inc., 478 F.2d 1281, 1300-02 (2d Cir. 1973); *see also Varjabedian II*, 888 F.3d 399, 408 (9th Cir. 2018).

[207] In *Derry v. Peek*, which is often referred to as a seminal case in English law, the House of Lords specifically held recklessness to be a basis for fraud liability in 1889. *See* Kuehnle, *supra* note 8, at 153.

[208] *See* Powell, *supra* note 86, at 253–55.

[209] *See* U.S. SECURITIES AND EXCHANGE COMMISSION, SEC INTERPRETATION: COMMISSION GUIDANCE ON MINI-TENDER OFFERS AND LIMITED PARTNERSHIP TENDER OFFERS (2000) [hereinafter *SEC Commentary*].

[210] *See id.; see also* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 214 (1976) (stating that "the original interpretation of Rule 10b-5 was compelled by the language and history of § 10(b)" and that "[w]hen a statute [Section 10(b)] speaks so specifically in terms of manipulation and deception . . . we are quite unwilling to extend the scope of the statute to negligent conduct").

[211] *See, e.g.*, 17 C.F.R. 240.14e-1 ("As a means reasonably designed to prevent fraudulent, deceptive or manipulative acts or practices within the meaning of section 14(e) of the Act, no person who makes a tender offer shall: . . . .").

[212] *See* SEC Commentary, *supra* note 209, at n.19.

treat enforcement of these provisions similarly under the scienter standard.[213] While the SEC perhaps appears to have impliedly interpreted scienter to apply to § 14(e) claims, it should be noted that the SEC has yet to explicitly state this interpretation.[214]

Nevertheless, now that *Varjabedian* has been dismissed with prejudice, the substantial ambiguity that exists is arguably best resolved through the legislature or administrative process.[215] Since the Court has declined to adjudicate the issue, regulatory authorities should act to help clarify ambiguities and provide certainty to the markets to mitigate some of the forewarned potential negative economic effects of a "de facto negligence standard."[216] Presently, if the SEC does in fact interpret § 14(e) to require scienter, then the agency has a compelling opportunity to clarify Regulation 14E to help resolve outstanding ambiguities through its rulemaking authority.[217]

Assuming that the SEC does in fact interpret § 14(e) to require scienter, then the best path would probably be to add a rule to Regulation 14E that explicitly states its interpretation of the requisite mental state for § 14(e) claims.[218] In the event that such a rule is challenged, courts would refer to the *Chevron* test to determine whether the SEC's interpretation falls within its delegated authority.[219] Agency interpretation is not necessarily dispositive for the judiciary.[220] However,

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[213] *See* SCALIA & GARNER, *supra* note 62, at 252 (describing how language used *in pari materia* implies that shared text is to be interpreted together as though it had the same meaning).

[214] *See* 17 C.F.R. 240.14e-1 to 14e-8. There is no instance where the SEC clarifies its belief that scienter should apply to Section 14(e) claims, despite this arguably being implied. *See id.*

[215] *See* Sevier, *supra* note 17, at 125; *see also* Vermeule, *supra* note 101, at 1890.

[216] *See* Powell, *supra* note 86, at 255; *see also* Brief for the Securities and Financial Markets Association, *supra* note 6, at 13–14.

[217] *See* Keller & Gehlmann, *supra* note 26, at 330 (describing the role of the SEC to restore public confidence in the securities markets).

[218] This new rule would likely become Rule 14e-9 and would state—for example—with explicit certainty that SEC interprets Section 14(e) to require scienter for securities fraud. *See generally* 17 C.F.R. 240.14e-1 to 14e-8 (noting that this sort of statement is nowhere to be found in the current rules).

[219] *See* Chevron USA, Inc. v. Natural Resources Defense Council, 467 U.S. 837, 843–44 (1984) (ruling that Congress delegates certain areas of expertise to administrative agencies when it leaves a gap in the legislation, or a statute is otherwise silent or ambiguous).

[220] In the words of Justice Scalia, "deferring to agency interpretation solely because of the agency's relative expertise, that is, because the court thinks the agency is more likely to reach the correct result, is constitutionally indefensible." *See* Walker, *supra* note 183, at 1354 (quoting Justice Scalia); *see also* Vermeule, *supra* note 100, at 1891.

under the *Chevron* test, a court must ask two questions.[221] First, the court must determine whether Congress has spoken on the issue—in which case, if it has spoken, Congress's statement controls.[222] Second, if Congress has not spoken on the issue, then the court must assess whether the agency's interpretation is reasonable.[223] Critically, courts are bound to accept agency interpretation, so long as that interpretation is found to be reasonable, regardless of whether the court itself might have chosen a different interpretation.[224]

In this case, Congress has not directly spoken on the issue of whether scienter or negligence is required for § 14(e) claims.[225] Therefore, the question likely becomes whether the SEC's presumed interpretation of § 14(e) to require scienter is reasonable.[226] As the Court stated in *Chevron*, considerable weight is given to an agency's interpretation of a statute that falls within its area of expertise.[227] For example, unless there is reason to believe that Congress would not have sanctioned a particular interpretation, then agency interpretations should be followed.[228] That being said, in this context, it seems unlikely that an SEC interpretation requiring scienter for § 14(e) claims would be held unreasonable.[229]

In *Varjabedian*, the Ninth Circuit impliedly acknowledged that the second clause of § 14(e), which mirrors § 10(b), requires scienter due to its explicit

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[221] *See* Walker, *supra* note 183, at 1346.

[222] *See Chevron*, 467 U.S. at 842.

[223] *See id.* at 843.

[224] *See id.* at 843–44 (stating that agency interpretation controls unless it is "arbitrary, capricious, or manifestly contrary to the statute"); *see also* Walker, *supra* note 183, at 1346 ("If the agency's interpretation is reasonable, it is controlling, even if the court itself would have chosen a different interpretation.").

[225] *See,* e.g., *Varjabedian II*, 888 F.3d 399, 404–05 (9th Cir. 2018) (describing how scienter requirements have grown entirely out of case law).

[226] *See Chevron*, 467 U.S. at 843–44.

[227] *See id.* at 844 ("We have long recognized that considerable weight should be accorded to an executive department's construction of a statutory scheme it is entrusted to administer."). After all, "expertness in matters of substance [is] relevant to the exercise of procedural discretion." LOUIS L. JAFFE, JUDICIAL CONTROL OF ADMINISTRATIVE ACTION 567 (1965).

[228] *See Chevron*, 467 U.S. at 843–44 (quoting United States v. Shimer, 367 U.S. 374, 382–83 (1961)) ("If this choice represents a reasonable accommodation of conflicting policies that were committed to the agency's care by the statute, we should not disturb it unless it appears from the statute or its legislative history that the accommodation is not one that Congress would have sanctioned.").

[229] *See* Walker, *supra* note 183, at 1347 (reiterating the high bar that exists for agency interpretation to be held unreasonable, especially in areas that are "technical and complex").

language to regulate "manipulative or deceptive devices."[230] The Ninth Circuit also pointed out, however, that the language of the first clause of § 14(e) conversely does not necessarily require scienter according to the Supreme Court.[231] With this in mind—considering the Ninth Circuit's conclusion that a negligence standard is more aligned with the legislative intent of the Williams Act—the court might disagree with an SEC rule that interprets scienter as the proper standard for § 14(e).[232] However, the court would be hard-pressed to make a compelling argument that such interpretation is unreasonable.[233] Normative principles and politically legitimate values, such as economic policy, within the SEC's area of expertise further support the reasonability of a scienter requirement.[234]

CONCLUSION

When the Supreme Court dismissed the defendant's writ of certiorari as improvidently granted in *Varjabedian*, it dramatically bolstered the significance of the Ninth Circuit's polarizing opinion by creating industry-wide confusion in mergers and acquisitions.[235] The Court's rationale for dismissal surely extends beyond its one-sentence opinion.[236] However, stakeholders in M&A transactions are now faced with ambiguity and uncertain economic implications that could negatively impact the market through increased transaction costs that account for anticipated litigation and settlement.[237] Undoubtedly, considering the substantive input on this case from major financial industry players, industry-wide stakeholder

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[230] *See Varjabedian II*, 888 F.3d at 405–06.

[231] *See id.* at 405 (citing Ernst & Ernst v. Hochfelde*r*, 425 U.S. 185, 212-14 (1976)) (showing that the Supreme Court has explicitly stated that the text of Rule 10b-5 could be read as proscribing "any type of material misstatement or omission . . . whether the wrongdoing was intentional or not").

[232] *See id.* at 408 (stating that "the text of the first clause of Section 14(e) is devoid of any suggestion that scienter is required"); *see also Varjabedian II*, 888 F.3d at 407–08 (describing the court's reasoning for why negligence is the proper standard as opposed to scienter).

[233] See *Chevron*, 467 U.S. at 844 (stating that "a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency").

[234] *See* McNollgast, *supra* note 93, at 5; *see also* Powell, *supra* note 86, at 253–55.

[235] *See* Powell, *supra* note 86, at 253–55.

[236] The District Court speculated that the Supreme Court dismissed the writ of certiorari as improvidently granted because factual issues related to materiality were left unsettled. *See Varjabedian IV*, 2020 U.S. Dist. LEXIS 40037, at *9.

[237] *See* Powell, *supra* note 86, at 253–56.

interest in the issue is high.[238]

Nevertheless, while the Ninth Circuit's result in holding for negligence was certainly polarizing, the methodology for determining that scienter is not necessarily required in § 14(e) claims is rather straightforward.[239] In many ways, *Varjabedian* is a textbook example of classic, sound statutory interpretation.[240] It starts with the text and proceeds to correctly apply the canons of statutory interpretation.[241] Following this approach, the court reminds readers that even case law established for decades is not immune from textual scrutiny.[242]

For the Ninth Circuit, legislative history and other normative factors pushed negligence over scienter in terms of capturing the spirit of the law and furthering legislative intent.[243] Understandably, however, given competing views on the use of legislative history, this latter part of the opinion raises questions.[244] After all, there are a myriad of policy arguments to be made in favor of scienter, including the importance of limiting transaction costs to spur economic activity.[245]

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[238] *See* Powell, *supra* note 86, at 255; *see also* Brief for the Securities and Financial Markets Association, *supra* note 6, at 13-14.

[239] In pointing out that the language of Section 14(e) does not require scienter, the Ninth Circuit relied on well-established means of statutory interpretation. *See* McNollgast, *supra* note 93, at 5; *see also* Sevier, *supra* note 17, at 124 ("The Ninth Circuit's holding is supported by the plain language of the statute and by viewing the Code as a whole. Additionally, the Ninth Circuit's interpretation of the Supreme Court cases are well reasoned and supported and the Court correctly identified flaws in the reasoning of other Circuits. While the [Petitioner and Amicus Briefs] address serious social, economic, and political concerns surrounding M&A litigation, the issues they present are appropriate problems for the legislature and not the judiciary.").

[240] *See* McNollgast, *supra* note 93, at 5. In conducting its analysis, the Ninth referred directly to and expanded upon the Supreme Court's textual analysis of Section 10(b) and Rule 10b-5 to ensure consistency with binding precedent. *See also Varjabedian II*, 888 F.3d 399, 405–06 (9th Cir. 2018) (citing Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212–14 (1976)).

[241] *See* Richard A. Posner, *Statutory Interpretation: In the Classroom and in the Courtroom*, 50 U. CHI. L. REV. 800, 805 (1983).

[242] Unlike statutes, the text of judge-made common law decisions is not controlling, but rather the concepts espoused therein are controlling. *See* Richard A. Posner, *Legal Formalism, Legal Realism, and the Interpretation of Statutes and the Constitution*, 37 CASE W. RES. L. REV. 179, 186-87 (1986) ("The [common law] doctrine is inferred from a judicial opinion, or more commonly a series of judicial opinions, but it is not those opinions, just as Newton's law is learned from a text but is not the text itself."). By contrast, the text of a statute cannot be revised or rewritten based on deduction or policy analysis. *See id.* at 187.

[243] *See Varjabedian II*, 888 F.3d at 407–08.

[244] *See* Posner, *supra* note 242, at 188–89.

[245] *See* Powell, *supra* note 86, at 253–56.

Regardless, despite anticipated debate about negligence or scienter, the Ninth Circuit's textual analysis in *Varjabedian* importantly identified existing errors in § 14(e) jurisprudence.[246]

Unfortunately, without clarity in the immediate term, lower courts will likely be confused regarding how to apply the law and ambiguous, unpredictable outcomes may result.[247] Therefore, if and when the Supreme Court decides the negligence or scienter question, the Court should seek to clarify its position in *Hochfelder* and how Rule 10b-5 adjudication and interpretation applies to § 14(e) claims to provide lower court guidance.[248] That being said, although the Supreme Court chose not to act in this instance, the issue need not remain entirely shrouded in its current state of ambiguity and disarray until another case reaches the Court.[249]

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[246] While economic policy factors may point towards maintaining recognition of scienter as the proper standard under Section 14(e), deduction from the text based on policy factors that is at odds with the plain meaning of the text is inappropriate. *See* Posner, *supra* note 242, at 187 ("But there is no such thing as deduction from a text."). *See also* Sevier, *supra* note 17, at 124.

[247] The Supreme Court has highlighted the importance of predictability in law, and thus, it may be inferred that it is important to rectify existing unpredictability. *See* Hohn v. United States, 524 U.S. 236, 251 (1998) (quoting Payne v. Tennessee, 501 U.S. 808, 827 (1991)) ("Stare decisis is 'the preferred course because it promotes the evenhanded, predictable, and consistent development of legal principles, fosters reliance on judicial decisions, and contributes to the actual and perceived integrity of the judicial process.'"). *See also* Algero, *supra* note 56, at 785.

[248] The Supreme Court has stated that the language of Rule 10b-5 itself does not compel scienter. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212 (1976). Subsequently, however, the Fifth and Second Circuits hold that Section 14(e) claims require scienter because Rule 10b-5 claims require scienter under *Hochfelder*. *See* Smallwood v. Pearl Brewing Co., 489 F.2d 579, 605 (5th Cir. 1974); *see also* Chris-Craft Indus. v. Piper Aircraft Corp., 480 F.2d 341, 362 (2d Cir. 1973). By contrast, the Ninth Circuit interprets the Supreme Court's decision in *Hochfelder* not to conflict with allowing a negligence standard for Section 14(e) claims. *See Varjabedian II*, 888 F.3d at 405–06 (determining that the language of Section 10(b) drove the Supreme Court to deem scienter required for a Rule 10b-5 action rather than the text of Rule 10b-5 itself). At this point, since there is disagreement in how to interpret the language of Rule 10b-5, elaborating on the position taken in *Hochfelder* as it relates to similar language situated within Section 14(e) would be helpful in resolving the circuit split. *Compare Chris-Craft*, 480 F.2d at 362, *with Varjabedian II*, 888 F.3d at 409–10 (highlighting the backbone of the outstanding circuit split).

[249] Without a Supreme Court decision, lower courts have split on how to interpret Section 14(e). *Compare Chris-Craft*, 480 F.2d at 362, *with Varjabedian II*, 888 F.3d at 409–10. However, in such a case, an administrative agency may offer interpretive guidance, which will be upheld if the statute in question is deemed ambiguous and such interpretation is reasonable under *Chevron*. *See* Antonin Scalia, *Judicial Deference to*

In the meantime, agency law enables regulatory bodies like the SEC to leverage rulemaking authority to clarify interpretation and thus mitigate uncertainty.[250]

Moving forward, courts and agencies alike will be challenged to assess § 14(e)—including its language, legislative history, and intent—in ways that were previously overlooked.[251] Undoubtedly, such debate will serve to bolster and further refine interpretation of the law—which benefits the public at large, and specifically the securities industry, through enhanced scrutiny directed at implementing the major antifraud provision of the Williams Act.[252] Assuming that errant § 14(e) jurisprudence is corrected, this enhanced scrutiny will move § 14(e) jurisprudence towards alignment with both Supreme Court precedent and the text of the statute.[253] Furthermore, nuanced interpretation in light of *Varjabedian* will ultimately mitigate the current uncertainty in the markets.[254]

Although an SEC rule would not provide complete certainty—as such a rule could still theoretically be struck down if a court ruled the text of the statute to be unambiguous or found the agency interpretation as unreasonable—the high standard of deference under *Chevron* provides a substantial likelihood that rule

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Administrative Interpretations of Law, 1989 DUKE L.J. 511, 511 (1989). In fact, the practice of deference to "reasonable" agency interpretations is not new law and was commonplace even before *Chevron*. ("[C]ourts have been content to accept 'reasonable' executive interpretations of law for some time."). Antonin Scalia, *Judicial Deference to Administrative Interpretations of Law*, 1989 DUKE L.J. 511, 511 (1989).

[250] An SEC rule will not provide complete certainty as such a rule could still theoretically be struck down as unreasonable under *Chevron*. *See* 467 U.S. at 842–43. However, the high standard of deference under *Chevron* certainly mitigates this uncertainty. *Id.*; *see also* Walker, *supra* note 183, at 1346.

[251] Lack of clarity does not permit courts to refrain from applying the text of a statute until the statute is rewritten or otherwise made clear. *See* Posner, *supra* note 242, at 191-92. Rather, courts must strive to continue to interpret the law—Section 14(e) in this instance—in order to figure out how to best carry out the directive of the statute. Posner, *supra* note 242, at 191-92.

[252] *See* Posner, *supra* note 242, at 191-92 (describing the important role of courts in carrying out the will of the legislature when the legislature does not clearly communicate its enactment).

[253] *See Varjabedian II*, 888 F.3d at 405–06 (making the argument that Section 14(e) prohibits more conduct than Section 10(b) does and based on the text, that Section 14(e) does not necessarily require scienter); *see also id.* at 412 (Christen, J., concurring) ("[T]he decision we issue today is most consistent with the Supreme Court's decisions in [*Hochfelder*] and *Aaron*.").

[254] For there to be certainty in the markets, participants must have an accurate prediction of how the law will be applied. *See, e.g.*, Oliver Wendell Holmes, *The Path of the Law*, 10 HARV. L. REV. 457, 461 (1897) (highlighting the value of law as providing a reliable prediction of how judges will rule in a particular case with a particular set of facts).

clarification would be held legitimate.[255] Even if a court rejected SEC interpretation, however, then the issue would likely be right back before the Supreme Court to offer further guidance on the negligence or scienter question.[256]

At this point, the SEC seems likely to interpret § 14(e) to require scienter.[257] If so, any SEC rule that clarifies this interpretation would likely be held to be reasonable, or at least not unreasonable.[258] Moving forward, therefore, the SEC should seek to clarify its interpretation of whether negligence or scienter should be required for § 14(e) claims through implementation of a new rule.[259] In doing so, the agency would leverage its rulemaking authority to mitigate uncertainty in an efficient manner that is more expedient than the traditional legislative process.[260]

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[255] *See* Walker, *supra* note 183, at 1346–47.

[256] The Department of Justice and the SEC have already stated "substantial interest" in the issue of whether negligence or scienter applies under Section 14(e). *See* Brief for the United States as Amicus Curiae in Support of Neither Party at 1, Emulex Corp. v. Varjabedian, 139 S. Ct. 1407 (2019) (No. 18-459). That being said, if an SEC attempt at rule clarification was struck down, the case would almost certainly be appealed to the Supreme Court and contested. *Id.*

[257] *See generally* SEC Commentary, *supra* note 209.

[258] After all, if five circuits and the SEC interpreted Section 14(e) to require scienter for decades without issue, then it seems unlikely that such a position would be deemed unreasonable. *See, e.g.*, Chris-Craft Indus. v. Piper Aircraft Corp., 480 F.2d 341, 362 (2d Cir. 1973). Additionally, considering the economic and political policy factors in favor of a scienter standard, which includes recklessness, the reasonability of agency interpretation for scienter is seemingly well supported. Walker, *supra* note 183, at 1346-47.

[259] Without clarification, the de facto negligence standard will persist given the Exchange Act's liberal jurisdiction provision. *See* Powell, *supra* note 86, at 290. As such, and considering recent rises in litigation, there are legitimate market efficiency concerns that beckon clarification of the issue. Powell, *supra* note 86, at 255–56. With its vast rulemaking authority to implement "rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors," the SEC is positioned to clarify ambiguity and offer guidance. *See* 15 U.S.C. § 78n(a)(1) (1968).

[260] *See* Walker, *supra* note 183, at 1355 (citing Am. Hosp. Ass'n v. Bowen, 834 F.2d 1037, 1045 (D.C. Cir. 1987)) (describing how administrative interpretive rules allow agencies to explain ambiguous terms in legislation without needing to undertake cumbersome proceedings).