No. 16-1541

IN THE

Supreme Court of the United States

MARGARET RICHEK GOLDBERG, AS TRUSTEE UNDER THE RESIDUARY TRUST, UNDER THE SEYMOUR RICHEK REVOCABLE TRUST, ON BEHALF OF THE TRUST AND ALL OTHERS SIMILARLY SITUATED,

Petitioner,

v.

BANK OF AMERICA, N.A. AND LASALLE BANK N.A.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

TERRY ROSE SAUNDERS
THE SAUNDERS LAW FIRM
120 North LaSalle Street,
Suite 2000
Chicago, Illinois 60602

J. STEPHEN WALKER
LAW OFFICES OF
J. STEPHEN WALKER, P.C.
20 North Clark Street,
Suite 1200
Chicago, Illinois 60602

THOMAS A. DOYLE
Counsel of Record
WEXLER WALLACE LLP
55 West Monroe Street,
Suite 3300
Chicago, Illinois 60603
(312) 346-2222
tad@wexlerwallace.com

Counsel for Petitioner

272748

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

QUESTION PRESENTED

Does the Securities Litigation Uniform Standards Act of 1998 (SLUSA), 15 U.S.C. § 78bb(f)(1)(A), require dismissing with prejudice a class action complaint for breach of contract and breach of fiduciary duty under state law, when the plaintiff's claims are not predicated on a misrepresentation or omission of material fact?

PARTIES TO THE PROCEEDINGS BELOW

The petitioner here is Margaret Richek Goldberg, as Trustee under the Residuary Trust under the Seymour Richek Revocable Trust, on behalf of the trust and all others similarly situated. In the district court, the predecessor trustee under that trust, Stephen Richek, was the plaintiff. Stephen Richek initially filed the appeal in the court of appeals, but while that appeal was pending, Margaret Richek Goldberg replaced Stephen Richek as trustee and appellant.

The respondents, defendants appellees below, are Bank of America, N.A. and LaSalle Bank, N.A.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner Margaret Richek Goldberg respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Seventh Circuit is published at 846 F.3d 913. Pet. App. 3a-34a. The district court's memorandum opinion and order is unpublished. Pet. App. 35a-49a.

JURISDICTION

The court of appeals issued its decision and entered judgment on January 23, 2017. On February 6, 2017, petitioner filed a timely petition for rehearing *en banc*. The court of appeals denied rehearing on February 21, 2017. Pet. App. 1a-2a. On May 11, 2017, this Court extended the due date for this petition up to and including June 21, 2017. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

RELEVANT STATUTORY PROVISION

Section 101(b) of the Securities Litigation Uniform Standards Act of 1998 (SLUSA), Pub. L. No. 105-353, 112 Stat. 3227 (1998), codified at 15 U.S.C. § 78bb(f), provides in relevant part:

(f) Limitation on remedies

(1) Class action limitations
No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging --

(A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or

(B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

A "covered class action" is a non-derivative suit seeking damages on behalf of fifty or more persons. 15 U.S.C. §§ 78bb(f)(5)(B), (C).

STATEMENT OF THE CASE

I. Legal Background

For years, the Securities Exchange Act and Rule 10b-5 provided the traditional vehicle for bringing private class action lawsuits alleging securities fraud. 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b-5(b). In 1995, Congress perceived that that traditional vehicle was being abused, and Congress enacted the Private Securities Litigation Reform Act (PSLRA), Pub. L. No. 104-67, 109 Stat. 737 (1995). *Merrill Lynch, Pierce, Fenner & Smith v. Dabit,* 547 U.S. 71, 81 (2006). The PSLRA included strict pleading

requirements for class actions alleging securities fraud. The PSLRA "insists that securities fraud complaints 'specify' each misleading statement; that they set forth the facts 'on which [a] belief' that a statement is misleading was 'formed'; and that they 'state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind.'" *Dabit*, 547 U.S. at 81-82 (*quoting Dura Pharms., Inc. v. Broudo*, 544 U.S. 336, 345 (2005), *and* 15 U.S.C. §§ 78u-4(b)(1), (2)).

To avoid the PSLRA, some investors began filing their securities fraud claims as class actions in state court under state law. Congress responded by enacting SLUSA, "in order to prevent certain state private securities class action lawsuits alleging fraud from being used to frustrate the objectives" of the PSLRA, to establish "national standards" for class actions "involving nationally traded securities," and to ensure that "securities class action lawsuits" were brought in federal court. Pub. L. No. 105-353, 112 Stat. 3227, at § 2 (1998). Tracking the fraud language of the federal securities laws, SLUSA provides for the removal to federal court and dismissal of "covered" class actions brought under state law that allege "a misrepresentation or omission of a material fact," or use of a manipulative device, "in connection with the purchase or sale of a covered security." 15 U.S.C. § 78bb(f)(1). *See also* 15 U.S.C. §§ 78bb(f)(5)(B), (C) ("covered class action" is a non-derivative suit seeking damages on behalf of fifty or more persons).

By its terms, SLUSA leaves state law to provide remedies for class actions that do not allege a misrepresentation or omission or a manipulative device, even when a security is involved in the claim.

II. Factual Background

Petitioner Margaret Richek Goldberg is the successor trustee on the Residuary Trust under the Seymour Richek Revocable Trust. In July of 1985, her predecessor as trustee (Stephen Richek) entered into a written agreement with LaSalle Bank, under which the bank, as agent, was to maintain a custody account for the trust. (This petition includes both Margaret and Stephen Richek when it refers to "petitioner.") The bank's responsibilities were to maintain the monies, securities and other property delivered by the trust; buy, sell, and exchange securities for the account upon the trust's directions; and hold dividends, interest and other income on securities and other property in the account subject to further instructions from the trust. As part of the services provided to the custody account, cash balances from deposits, sales of securities, or earned income were transferred or "swept" into investment vehicles, such as cash management funds, selected by petitioner from a list of eligible funds that the bank provided. These funds then invested the cash balances transferred from custody accounts.

Under the terms of the agreement, in return for its services, the bank was to receive a fee in accordance with its schedule of compensation and reimbursement for out-of-pocket expenses. The agreement provided that the bank would notify the trust of any increase in its fee schedule. During the time the account was maintained at the bank, the trust paid account fees in the form of an annual custody fee, based on the size of the account. This fee was deducted quarterly from the custody account. The agreement did not provide for any other payments to the bank.

Unbeknownst to the trustee, however, the bank was also charging custody accounts additional fees, based on the average daily accumulated balances in investment vehicles that resulted from cash that had been swept from the custody accounts. The bank received these fees out of the funds that had been transferred to the investment vehicles.

Petitioner does not know when the bank began collecting sweep fees and did not become aware of them until June 2009, after LaSalle Bank had merged into Bank of America, when the bank notified the trust that it was eliminating the daily cash sweep fees, "resulting in a decrease in the fees charged to the account."

III. Petitioner's Complaint

Based on these facts, petitioner filed this suit in 2010 in Illinois state court alleging a breach of contract and breach of fiduciary duty against the bank and seeking certification of the suit as a class action under Illinois law. The putative class is composed of all persons who maintained custody accounts at the bank between July 18, 1985, and August 1, 2009. Respondents are defendants.

Invoking SLUSA and the diversity jurisdiction under the Class Action Fairness Act (CAFA) provisions of 28 U.S.C. § 1332(d), respondents removed petitioner's suit to federal court. Petitioner did not contest that removal because the federal court had jurisdiction under CAFA. Petitioner filed an amended complaint in federal court alleging the same state law breach of contract and breach of fiduciary duty claims, on behalf of the same putative class and directed at the same respondents. (This petition refers to that amended complaint as the "complaint.")

The complaint details the events described above, and then alleges four class action claims under Illinois law. Count I alleges that the bank, as a fiduciary, was obligated to manage the custody accounts in the best interest of the customers, but that the bank breached its fiduciary duties by taking sweep fees from the custody accounts and breached its duty of candor by failing to disclose that the bank was taking sweep fees. Count II alleges that the bank breached its contract by taking sweep fees in addition to the annual or periodic fees which were provided for in the custody account agreement. Count III alleges that the bank was unjustly enriched because the sweep fees that the bank received were the petitioner's property. Count IV seeks an accounting. The complaint further alleges that the bank had not notified plaintiff of the sweep fees and these fees were not authorized. There is no claim for fraud, and the facts alleged set forth a claim for state law breach of contract and breach of fiduciary duty.

IV. The Prior Proceedings

On respondents' motion, the district court dismissed the complaint. Pet. App. 35a-49a. Focusing on the allegation that the bank never disclosed the sweep fees to petitioner, the district court concluded that the complaint is "predicated upon allegations of misstatements, omissions, deception or manipulation" relating to the transfer of assets to a mutual fund, and that those allegations were "the essence" of the complaint. Pet. App. 42a, 47a. On that basis, the district court held that petitioner's claims were all precluded by SLUSA. Pet. App. 49a.

Petitioner appealed to the Seventh Circuit. Although the case was fully briefed and argued in January 2012,

the court of appeals did not decide the case until January 2017, a five-year period during which one member of the original panel died. Pet. App. 3a. A new panel member was not assigned until December 1, 2016. Pet. App. 3a. On January 23, 2017, the court issued a brief *per curiam* opinion that affirmed the dismissal of the complaint. Pet. App. 3a-8a.

The court of appeals also focused on the allegation that the bank had not disclosed that it was collecting sweep fees, and concluded that the complaint "depends on the omission of a material fact -- that some mutual funds paid, and the [bank] kept fees extracted from the 'swept' balances." Pet. App. 5a. The court of appeals held that SLUSA applied because the omission was in connection with a mutual fund, which is a covered security. Pet. App. 5a-6a. The court of appeals rejected petitioner's argument that the claims rested on state contract law and state fiduciary duty law, reasoning "that if a claim could be pursued under federal securities law, then it is covered by [SLUSA] even if it also could be pursued under state contract or fiduciary law," citing *Holtz v. JPMorgan Chase Bank N.A.*, 846 F.3d 928 (7th Cir. 2017), which was decided that same day. Pet. App. 7a.

One member of the panel dissented. In his dissenting opinion, Judge Hamilton pointed out that petitioner had brought a simple breach of contract claim: the "contract spelled out the fees the bank would charge for its services. The bank breached the contract by charging additional fees." Pet. App. 18a. Proof of that claim did not require proof of any misrepresentation or omission of material fact. Pet. App. 18a. Judge Hamilton criticized the majority for its "reverse alchemy," making the failure to disclose a

breach of contract into an omission of a material fact, and thus turning gold into lead. Pet. App. 18a.

Judge Hamilton set out three grounds for his dissent. First, the majority's opinion distorted the language of SLUSA and the legislature's purpose in enacting it -- namely to prevent plaintiffs and their counsel from avoiding the rigors of the PSLRA by filing securities fraud class actions in state court under a non-federal cause of action. Instead, the majority expanded SLUSA to include non-fraud claims. Pet. App. 20a. This unwarranted expansion "effectively immunize[d]" banks and securities firms "from liability for their breaches of contract and fiduciary duty." Pet. App. 20a-21a. Second, the majority ignored the better approach of the Second, Third and Ninth Circuits, which applies SLUSA only if the plaintiff's claim requires proof of a misrepresentation or omission of a material fact, citing *Freeman Investments, L.P. v. Pacific Life Ins. Co.,* 704 F.3d 1110 (9th Cir. 2013); *In re Kingate Mgt. Ltd. Litig.,* 784 F.3d 128 (2d Cir. 2015); *and LaSala v. Bordier et Cie,* 519 F.3d. 121 (3d Cir. 2008). Pet App. 22a-25a. Third, the majority failed to give effect to the federalism balance that Congress struck in passing SLUSA. Pet. App. 30a-33a.

On February 21, 2017, the court of appeals denied petitioner's request for rehearing. Pet. App. 1a-2a.

REASONS FOR GRANTING THE PETITION

I. This Case Involves An Important And Frequently Recurring Issue Of Federal Law That Has Not Been Decided By This Court.

The Seventh Circuit's interpretation of SLUSA in this case places serious restrictions upon the enforcement of state laws governing contractual relationships, including those of fiduciaries. Those restrictions are inconsistent with the intended scope and purpose of SLUSA.

Petitioner's complaint alleges a straightforward claim for breach of contract and breach of fiduciary duty under Illinois law: the bank charged fees that were greater than the fees that the parties had agreed upon, and took money in its fiduciary capacity from petitioner's trust account that it was not entitled to take. The complaint also alleges that the bank did not disclose that it had taken money to which is was not entitled, but that fact is not alleged to suggest that the bank engaged in fraud. Rather, the complaint pleads that fact to confirm that the parties never mutually modified their contract, and to explain why the bank's conduct could continue for so long. The bank's failure to disclose the sweep fee is not the factual gravamen of petitioner's claims for breach of contract or breach of fiduciary duty.

Nonetheless, the Seventh Circuit held that petitioner's claims depended on an omission of material fact and that petitioner could have brought her claim under the federal securities laws. Pet. App. 5a, 7a. That holding is wrong because the complaint actually alleges that the bank's wrongful taking of money was a breach of contract and a

breach of fiduciary duty, and those claims did not depend on the bank's failure to disclose that it was taking the money. All of the facts necessary to prove both the breach of contract claim and the breach of fiduciary duty claim occurred when the bank took money from petitioner's account. That conduct constituted a breach of contract and a breach of fiduciary duty. (As pled in the complaint, the bank's fiduciary duty included both obligations of loyalty and candor.)

The court compounded that error by going on to rule that "if a claim could be pursued under federal securities law, then it is covered by [SLUSA] even if it also could be pursued under state contract or fiduciary law." Pet. App. 7a. The cumulative effect of these two rulings was to nullify Illinois contract law in any situation in which a claim of fraud under federal securities law could be imagined -- even if that claim could not be pled in good faith -- if the amounts involved are too small to justify individual actions. Overcharges on account fees are, by their nature, small amounts for each account. When there is so little at stake for each injured person, a claim cannot be litigated economically on an individual basis. *See Hughes v. Kore of Indiana Enterprise, Inc.*, 731 F.3d 672, 675 (7th Cir. 2013). In the real world, once a state law breach of contract class action is barred, no realistic remedy exists for people who each suffer an injury of this scale, and very few (if any) of them will litigate on an individual basis. *Butler v. Sears, Roebuck & Co.*, 727 F.3d 796, 801 (7th Cir. 2013).

Nothing in SLUSA or its legislative history indicates that SLUSA was intended to diminish the states' responsibility over contract law. States have a legitimate interest in protecting their citizens' contract rights. *See,*

e.g., AT&T Mobility LLC v. Concepcion, 563 U.S. 333, 364 (2011)(Breyer, J., dissenting). State law has always had an active role in protecting individual investors from misconduct in connection with their accounts. *See Chadbourne & Parke, LLP v. Troice*, 134 S. Ct. 1058, 1068-69 (2014); Pet. App. 30a-31a. By reading SLUSA to bar class-wide recovery for breaches involving amounts too small to justify individual actions, the majority opinion jeopardizes the ability of states to protect their citizens' contract rights and gives unwarranted protection to any entity that processes securities. Pet. App. 31a. As this Court pointed out in *Dabit,* 547 U.S. at 87-88, SLUSA was drafted to preserve certain specific roles for state securities law and securities regulators. Inclusion of these explicit "carve-outs" for state law "both evinces congressional sensitivity to state prerogatives in this field and makes it inappropriate for courts to create additional, implied exceptions." *Id.*; *Accord, Chadbourne & Parke,* 134 S. Ct. at 1068-69 (interpreting SLUSA to preserve roles for state law and state courts). The Seventh Circuit's holding disregards those prerogatives. Pet. App. 29a-31a.

Moreover, the Seventh Circuit's holding cannot be reconciled with the purpose of SLUSA. In enacting SLUSA, Congress was acting to protect the supremacy of the federal laws relating to securities fraud class actions. *Dabit*, 547 U.S. at 87-88. Dismissing petitioner's state law claims does not further that purpose. Instead, the Seventh Circuit's holding merely disrupts the federalism balance that Congress struck in SLUSA. Pet. App. 30a.

To be sure, this Court has not yet ruled on the precise question involved in this case. While this Court has liberally construed the implied right of action under

Rule 10b-5 to combat schemes to defraud (*see, e.g., S.E.C. v. Zandford*, 535 U.S. 813, 819 (2002)), this Court has also held that the implied right of action does not extend beyond settings involving fraud. In *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976), this Court held that merely negligent conduct is not actionable under Rule 10b-5. In *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 473-74 (1977), this Court held that conduct that oppressed a minority shareholder was not actionable under Rule 10b-5 if it did not involve manipulation or deception. In *Chiarella v. United States*, 445 U.S. 222, 232 (1980), this Court declined to expand the Rule 10b-5 right of action to cover insider trading claims, noting that "not every instance of financial unfairness constitutes fraudulent activity under § 10b." And in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 191 (1994), this Court ruled that a private plaintiff may not bring an action for aiding and abetting a violation of Rule 10b-5. In these cases, this Court has resisted attempts to stretch Rule 10b-5 to cover facts that will not support a fraud claim.

The Seventh Circuit's opinion ignores the guidance implicit in these decisions, turning SLUSA into a law that requires trial courts to treat a breach of contract claim as if it were a securities fraud claim whenever a misrepresentation or omission appears in the pleading, even if the plaintiff would not need to allege or prove a misrepresentation or omission to prevail. Indeed, the majority's opinion would expand SLUSA by turning meritorious claims for breach of contract into non-meritorious claims for fraudulent misrepresentations or omissions.

This Court should review the decision here, in order to preserve the right of the states to govern contractual and fiduciary relationships in situations where claims do not depend on federal securities laws.

II. The Seventh Circuit's Decision -- That SLUSA Bars Class Actions Based On State Law Claims That Are Not Predicated On Misrepresentations Or Omissions -- Conflicts With Decisions Of The Second, Third And Ninth Circuits.

Even though Congress intended to create a nationwide standard, the circuits have split on what is necessary to allege a misrepresentation or omission under SLUSA. The Seventh Circuit interprets SLUSA to preclude any state law class action for breach of contract, so long as the plaintiff could have tried to plead the case as a federal securities law claim, even if the case does not turn on an omission or misstatement of a material fact. Pet. App. 7a.

That interpretation is in conflict with the interpretation adopted by the Ninth Circuit. In that circuit, courts interpret SLUSA to require an examination of the facts alleged in the complaint to determine if "deceptive statements or conduct form the gravamen or essence of the claim." *Freeman Investments, L.P. v. Pacific Life Ins. Co.*, 704 F.3d 1110, 1115 (9th Cir. 2013). In *Freeman Investments*, the plaintiff alleged that a seller of a variable insurance policy (which was a covered security, because it was tied to an investment account) had breached the contract by charging excessive fees. 704 F.3d at 1115. The Ninth Circuit held that SLUSA did not bar the claim because plaintiff would not be required to prove a misrepresentation in order to prove his breach of

contract claim. The plaintiff's claim was not barred by SLUSA merely because the complaint also alleged that the defendant had used misrepresentations to conceal its own breach of contract. 704 F.3d at 1115-16.

The Second and Third Circuits follow the same approach, focusing on whether the plaintiff's claim is predicated on a misrepresentation or omission. *See LaSala v. Bordier et Cie,* 519 F.3d 121, 141 (3d Cir. 2008); *Rowinski v. Salomon Smith Barney Inc.,* 398 F.3d 294, 300 (3d Cir. 2005); *and In re Kingate Mgt. Ltd. Litig.,* 784 F.3d 128, 152 (2d Cir. 2015).

Because of the conflicts in the circuit courts' rulings, the district courts have been all over the map in deciding when SLUSA bars state law claims. Some jurisdictions permit state law class actions so long as the plaintiff need not prove a misrepresentation or omission in order to prevail on its claim. *See, e.g., Lee v. Pincus,* No. 13-cv-834-SLR, 2013 U.S. Dist. LEXIS 179619, at *4-*6 (D. Del. Dec. 23, 2013); *Normand v. The Bank of New York Mellon,* No. 16-cv-212 (JPO), 2016 U.S. Dist. LEXIS 134881 at *16 (S.D.N.Y. Sept. 29, 2016); *and Stephens v. Gentilello,* 853 F. Supp. 2d 462, 468 (D. N.J. 2012). Other courts cite SLUSA to bar state law class actions simply because the complaint refers to a misrepresentation or omission. *See, e.g., Broadhead L.P. v. Goldman, Sachs & Co.,* No. 2:06-cv-009, 2007 U.S. Dist. LEXIS 21302, at *12-*13 (E.D. Tex. March 26, 2007); *Kutten v. Bank of America, N.A.,* No. 06-cv-937 (PAM), 2007 U.S. Dist. LEXIS 63897, at *20-*21 (E.D. Mo. Aug. 29, 2007); *and Luis v. RBC Capital Markets, LLC,* No. 16-cv-175 (SRN/JSM), 2016 U.S. Dist. LEXIS 142057, at *12-*14 (D. Minn. Oct. 13, 2016). Such a situation is unfair both to the litigants involved and to

the district court judges, because it inhibits the efficient administration of justice in an important area of the law.

This case provides this Court with an ideal opportunity to decide the proper scope of SLUSA. Petitioner's claims for breaches of contract and fiduciary duty are not fraud claims; petitioner's claims do not depend on an omission or a misrepresentation. Nor does the complaint suggest that the petitioner has shoe-horned these facts into state-law causes of action in order to circumvent the PSLRA's heightened pleading requirements. Rather, petitioner's complaint is nothing more than what it purports to be: a class action lawsuit arising from a bank's breach of contract and breach of its fiduciary duty. With this case, the Court can make it clear that SLUSA only reaches claims that are predicated on misrepresentations or omissions of material fact.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully Submitted,

TERRY ROSE SAUNDERS
THE SAUNDERS LAW FIRM
120 North LaSalle Street,
Suite 2000
Chicago, Illinois 60602

J. STEPHEN WALKER
LAW OFFICES OF
J. STEPHEN WALKER, P.C.
20 North Clark Street,
Suite 1200
Chicago, Illinois 60602

THOMAS A. DOYLE
Counsel of Record
WEXLER WALLACE LLP
55 West Monroe Street,
Suite 3300
Chicago, Illinois 60603
(312) 346-2222
tad@wexlerwallace.com

Counsel for Petitioner

APPENDIX

APPENDIX A — DENIAL OF REHEARING OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT, FILED FEBRUARY 21, 2017

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT
Chicago, Illinois 60604

No. 11-2989

MARGARET RICHEK GOLDBERG, AS TRUSTEE UNDER THE SEYMOUR RICHEK REVOCABLE TRUST, ON BEHALF OF A CLASS,

Plaintiff-Appellant,

v.

BANK OF AMERICA, N.A.
AND LASALLE BANK, N.A.,

Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 10 C 6779
Robert M. Dow, Jr., *Judge*

February 21, 2017

Appendix A

Before

JOEL M. FLAUM, *Circuit Judge*
FRANK H. EASTERBROOK, *Circuit Judge*
DAVID F. HAMILTON, *Circuit Judge*

ORDER

Plaintiff-appellant filed a petition for rehearing and rehearing *en banc* on February 6, 2017. No judge in regular active service has requested a vote on the petition for rehearing *en banc*,* and all of the judges on the panel have voted to deny rehearing. The petition for rehearing is therefore DENIED.

* Judge Rovner and Judge Williams did not participate in the consideration of this petition.

APPENDIX B — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT, FILED JANUARY 23, 2017

IN THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

No. 11-2989

MARGARET RICHEK GOLDBERG, AS TRUSTEE UNDER THE SEYMOUR RICHEK REVOCABLE TRUST, ON BEHALF OF A CLASS,

Plaintiff-Appellant,

v.

BANK OF AMERICA, N.A., and LASALLE BANK, N.A.,

Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division. No. 10 C 6779. Robert M. Dow, Jr., Judge.

ARGUED JANUARY 17, 2012 – DECIDED JANUARY 23, 2017

Before FLAUM, EASTERBROOK, and HAMILTON, *Circuit Judges.**

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* Circuit Judge Cudahy was a member of the panel that heard oralargument but died before the decision was issued. On December 1, 2016, Circuit Judge Flaum was selected by a random procedure to replace him. He has read the briefs and listened to the recording of oral argument.

PER CURIAM. LaSalle Bank offered custodial accounts that clients used to invest in securities. If an account had a cash balance at the end of a day, the cash would be invested in ("swept" into) a mutual fund from a list that the client chose. LaSalle Bank would sell the mutual fund shares automatically when the customer needed the money to make other investments or wanted to withdraw cash. Stephen Richek, as trustee under the Seymour Richek Revocable Trust, opened a custodial account with a sweeps feature. (The current trustee is Margaret Richek Goldberg; for the sake of continuity we continue to refer to the investor and plaintiff as Richek.) Richek was satisfied with LaSalle's services until it was acquired by Bank of America. After the acquisition, Bank of America notified the clients that a particular fee was being eliminated. Richek, who had not known about the fee, then sued in state court, contending that LaSalle had broken its contract (which had a schedule that did not mention this fee) and violated its fiduciary duties. Richek proposed to represent a class of all customers who had custodial accounts at LaSalle. (Because LaSalle became a subsidiary of Bank of America, and now operates under its name, we refer from now on to "the Bank," which covers both institutions.)

The Bank removed the suit to federal court, relying on the Securities Litigation Uniform Standards Act of 1998 (SLUSA or the Litigation Act), 15 U.S.C. § 78bb(f). (Section 78bb is part of the Securities Exchange Act of 1934. The Litigation Act added similar language to the Securities Act of 1933. See 15 U.S.C. § 77p(b). The Bank is not an issuer or underwriter covered by the 1933 Act,

so we refer to § 78bb(f).) SLUSA authorizes removal of any "covered class action" in which the plaintiff alleges "a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security" (§ 78bb(f)(1)(A)). The statute also requires such state-law claims to be dismissed. The district court held that Richek's suit fits the standards for both removal and dismissal and entered judgment in the Bank's favor. 2011 U.S. Dist. LEXIS 86105 (N.D. Ill. Aug. 4, 2011).

According to the complaint, some mutual funds paid the Bank a fee based on the balances it transferred, and the Bank did not deposit these fees in the custodial accounts or notify customers that it was retaining them. The Bank's retention of these payments is economically equivalent to a secret fee collected from the accounts, because they contained less money than they would have had the Bank credited them with the fees paid by the mutual funds—fees derived from the custodial accounts themselves. Richek contends that the Bank thus kept for its own benefit fees exceeding those in the contractual schedule, without disclosure to its customers.

Richek's claim depends on the omission of a material fact—that some mutual funds paid, and the Bank kept, fees extracted from the "swept" balances. He concedes that his suit is a "covered class action" (the class has more than 50 members; see § 78bb(f)(5)(B)(i)(I)) and that each of the mutual funds is a "covered security" (see § 78bb(f)(5)(E)). The Bank's omission was in connection with a purchase or sale of a "covered security". See *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S.

71, 126 S. Ct. 1503, 164 L. Ed. 2d 179 (2006). *Chadbourne & Parke LLP v. Troice*, 134 S. Ct. 1058, 188 L. Ed. 2d 88 (2014), does not affect this conclusion, because customers were dealing directly with covered investment vehicles. (*Troice* holds that the Litigation Act does not apply when the customer invests in an asset that does not consist of, or contain, covered securities.) Because "[n]o covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party" (§ 78bb(f)(1)) when these conditions have been met, the district court's decision is unexceptionable.

According to Richek, the Bank's omission is outside the scope of the Litigation Act because it does not involve the price, quality, or suitability of any security. But the Litigation Act does not say what kind of connection must exist between the false statement or omission and the purchase or sale of a security; the statute asks only whether the complaint alleges "a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security". Richek's complaint alleged a material omission in connection with sweeps to mutual funds that are covered securities; no more is needed.

Apparently Richek believes that only statements (or omissions) about price, quality, or suitability are covered by the federal securities laws, and that only state-law claims that overlap winning securities claims are affected by the Litigation Act. This is doubly wrong. First, *Dabit* holds that claims that arise from securities transactions are covered whether or not the private party could recover

damages under federal law. (In *Dabit* itself no private right of action for damages was possible, yet the Court held the claim covered and preempted.) Second, the Securities Exchange Act of 1934 forbids material misrepresentations and omissions in connection with securities transactions whether or not the misrepresentation or omission concerns the price, quality, or suitability of the security. See, e.g., *SEC v. Zandford*, 535 U.S. 813, 122 S. Ct. 1899, 153 L. Ed. 2d 1 (2002); *United States v. Naftalin*, 441 U.S. 768, 99 S. Ct. 2077, 60 L. Ed. 2d 624 (1979). Thus Richek may have had a good claim under federal securities law. But he chose not to pursue it, and SLUSA prevents him from using a state-law theory instead.

We said earlier that Richek concedes that his claim rests on a material omission and that the mutual funds are covered securities. He does not concede that the omission was "in connection with" the purchase or sale of a covered security. This branch of his argument rests on *Gavin v. AT&T Corp.*, 464 F.3d 634 (7th Cir. 2006). We reject Richek's contention for the reasons given in *Holtz v. JPMorgan Chase Bank, N.A.*, No. 13-2609, 846 F.3d 928, 2017 U.S. App. LEXIS 1112 (7th Cir. Jan. 23, 2017), [slip op.] at 9-11.

Richek also maintains that his action rests on state contract law and state fiduciary law, not securities law. This line of argument, too, is addressed and rejected in *Holtz*, which holds that if a claim could be pursued under federal securities law, then it is covered by the Litigation Act even if it also could be pursued under state contract or fiduciary law. A claim that a fiduciary that trades in

securities for a customer's account has taken secret side payments is well inside the bounds of securities law. See *Holtz*, 2017 U.S. App. LEXIS 1112, [slip op.] at 4-9.

AFFIRMED

FLAUM, *Circuit Judge*, concurring. I agree that the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), 15 U.S.C. § 78bb(f), warranted removal and dismissal of Stephen Richek's lawsuit. The challenge presented by this appeal requires addressing the scope of SLUSA's "misrepresentation or omission of a material fact" prohibition.

Stephen Richek, as trustee under the Seymour Richek Revocable Trust, entered into an agreement with LaSalle National Bank, under which LaSalle would open a custodian account for the Trust to invest in securities.[1] The parties agreed to a fee schedule that required LaSalle to notify Richek of any increases. As part of maintaining Richek's custodian account, LaSalle would invest ("sweep") any cash balances at the end of the day into a mutual fund Richek had selected from a list provided by LaSalle. Eventually, Richek learned that LaSalle, unbeknownst to him, had been accepting reinvestment ("sweep") fees from the mutual funds based on the average daily invested balance LaSalle had swept from his custodian account. Each fee was unique to the particular mutual fund.

Richek sued the Bank[2] in Illinois state court on behalf of all customers with custodian accounts, alleging that the

1. Margaret Richek Goldberg is the current trustee; I will refer to the investor and plaintiff as "Richek."

2. Prior to the lawsuit, Bank of America acquired LaSalle, and LaSalle became a subsidiary of Bank of America; I will refer to both institutions and defendants as "the Bank."

Bank had (1) violated its fiduciary duties and (2) breached the underlying contract. The Bank removed the lawsuit to federal court pursuant to SLUSA and 28 U.S.C § 1332(d)(2). Richek subsequently amended his complaint, and the district court dismissed that amended complaint under SLUSA, entering judgment for the Bank. This appeal followed.

SLUSA provides, in relevant part:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging—
>
> (A) A misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security.

15 U.S.C. § 78bb(f)(1). There is no dispute that Richek's class action qualified as a "covered class action" under the statute. Instead, the issue is whether Richek alleged "a misrepresentation or omission of a material fact."[3]

Brown v. Calamos, 664 F.3d 123 (7th Cir. 2011), is instructive. There, a plaintiff shareholder sued a closed-end investment fund alleging that the fund had breached

3. Richek also disputes that his allegations were "in connection with the purchase or sale of a covered security." I agree with Judge Easterbrook and reject these arguments under *Holtz v. JPMorgan Chase Bank, N.A.*, No. 13-2609, 846 F.3d 928, 2017 U.S. App. LEXIS 1112, *15 (7th Cir. Jan. 23, 2017).

its fiduciary duty by redeeming a particular stock, at terms unfavorable to the common shareholders, in an effort to remain in the good graces of the investment banks and brokerage firms facing lawsuits stemming from the stock's value after the 2008 financial crisis. *Id.* at 126. We concluded, despite the complaint's language to the contrary,[4] that the complaint "implicitly" alleged a material misrepresentation or omission: The fund had failed to disclose the conflict of interest created by its broader concerns for the fund family's[5] long-term wellbeing. *Id.* at 127. Without addressing the complaint's unjust enrichment claim, we affirmed the district court's dismissal of the complaint under SLUSA. *Id.* at 131.

In doing so, we considered three approaches to dismissing complaints under SLUSA: (1) the Sixth Circuit's "literalist" approach, where the court asks simply whether the complaint can reasonably be interpreted as alleging a material misrepresentation or omission, *see Atkinson v. Morgan Asset Mgmt., Inc.*, 658 F.3d 549, 554-55 (6th Cir. 2011); (2) the Third Circuit's "looser" approach, where the court asks whether proof of a material misrepresentation or omission is inessential (an "extraneous detail" that does

4. The complaint explicitly stated, "Plaintiff does not assert by this action any claim arising from a misstatement or omission in connection with the purchase or sale of a security, nor does plaintiff allege that Defendants engaged in fraud in connection with the purchase or sale of a security." Such a statement, however, was not a well-pleaded allegation but rather a legal conclusion entitled to no deference on review.

5. The fund at issue was one of at least twenty in a family of mutual funds.

not require dismissal) or essential (either a necessary element of the cause of action or otherwise critical to a plaintiff's success in the case, warranting dismissal), *see LaSala v. Bordier et Cie*, 519 F.3d 121, 141 (3d Cir. 2008) (citing *Rowinski v. Salomon Smith Barney Inc.*, 398 F.3d 294 (3d Cir. 2005)); and (3) the Ninth Circuit's "intermediate" approach, where the court dismisses preempted suits without prejudice, permitting plaintiffs to file complaints devoid of any prohibited allegations, *see Stoody-Broser v. Bank of America*, 442 F. App'x 247, 248 (9th Cir. 2011).

We have expressed concern with the Ninth Circuit's approach, cautioning, "No longer in American law do complaints strictly control the scope of litigation." *Brown*, 664 F.3d at 127. A plaintiff who removes SLUSA-triggering allegations in an attempt to avoid dismissal may simply "reinsert" them later upon returning to state court. *Id.* It is an open question in this Circuit whether this risk of reinsertion warrants a court's looking beyond the amended complaint to the original pleading.[6] Doing so may leave the court's analysis vulnerable to hindsight bias, but may also aid in guarding against artful amendments.

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6. Actually, as suggested by *Brown*, it may be that the district court may consider *only* the original complaint in assessing a defendant's SLUSA filing; and if so, Richek's amendment was inappropriate. *See* 664 F.3d at 131 (discussing amendments to a complaint after a defendant has moved to dismiss under SLUSA); *see also id.* (disagreeing with *Behlen v. Merrill Lynch*, 311 F.3d 1087, 1095-96 (11th Cir. 2002)). In any event, as will be explained, SLUSA warranted dismissal of both the original and amended complaints in this case.

Richek's complaint history illustrates this tension. In his original complaint in state court, Richek's fiduciary duty claim alleged,

> Defendants breached their fiduciary duties of loyalty, care and candor when they *steered* plaintiff and members of the Class to investment vehicles that had agreed to pay a percentage fee to defendants from, and based on, reinvestments made by Custodian Accounts.

(emphasis added). This claim is nearly identical to the fiduciary duty claim dismissed pursuant to SLUSA in *Holtz v. JPMorgan Chase Bank, N.A.*, No. 13-2609, 846 F.3d 928, 2017 U.S. App. LEXIS 1112 (7th Cir. Jan. 23, 2017), [slip. op.] at 1-2, where the plaintiff alleged that J.P. Morgan Chase had steered its employees to invest client money in the bank's own mutual funds, despite higher fees or lower returns. As we noted, claims alleging that "one party to a contract conceal[ed] the fact it planned all along to favor its own interests ... is a staple of federal securities law." 2017 U.S. App. LEXIS 1112 at *8. Here, upon removal to federal court, Richek amended his complaint to among, other things, omit the "steered" language. This amendment, however, does not alleviate the concerns under SLUSA: "[O]nce the case shorn of its fraud allegations resumes in the state court, the plaintiff—who must have thought the allegations added *something* to his case, as why else had he made them?—may be sorely tempted to reintroduce them, and maybe the state court will allow him to do so. And then SLUSA's goal of preventing state-court end runs around limitations that

the Private Securities Litigation Reform Act had placed on federal suits for securities fraud would be thwarted." *Brown*, 664 F.3d at 128. One must then turn to Richek's amended complaint, and to the two remaining approaches to dismissals under SLUSA, with this "reinsertion" risk in mind.

As in *Brown*, Richek's fiduciary duty claim triggered SLUSA preemption under both the Sixth Circuit's "literalist" approach and the Third Circuit's "looser" approach. In his amended complaint, he claims,

> Defendants breached their duty of candor to plaintiff and members of the Class when they *failed to disclose* that they were receiving daily cash re-investment (sweep) fees from investment vehicles into which cash balances from Custody Accounts were transferred.

(emphasis added). Following the "literalist" approach, the claim's language speaks for itself. One can reasonably read it to allege a material misrepresentation or omission: The Bank failed to disclose a particular fee that, if disclosed, may have "given pause to potential investors." *Brown*, 664 F.3d at 127. Likewise, under the "looser" approach, the Bank's failure to disclose was far from an inessential "extraneous detail." Rather, Richek's claim rested on it: To have succeeded on his fiduciary "duty of candor" claim, Richek needed to show that the Bank failed to disclose, or omitted, the fact that it collected "swipe fees" while investing its clients' custody-account cash balances. The inherent misrepresentation becomes

especially clear after considering the claim as it originally appeared to the state court—if, in fact, we may consider the original complaint—which alleged that the Bank secretly "steered" the clients' money to those mutual funds that had agreed to pay the Bank "sweep fees." The risk that Richek may "reinsert" these original allegations in a future state-court proceeding is amplified by the fact that his amended claim is inseparably intertwined with a material misrepresentation or omission. *See generally Brown*, 664 F.3d at 128-31. As such, Richek's fiduciary duty claim triggered SLUSA preemption.

All of this raises the question: Did SLUSA preempt Richek's entire *complaint* or just the individual *claim*? We have not decided this issue.[7] Some circuits, on one hand, have endorsed a claim-by-claim approach. *See In re Kingate Mgmt. Ltd. Lit.*, 784 F.3d 128, 153 (2d Cir. 2015); *In re Lord Abbett Mut. Funds Fee Lit.*, 553 F.3d 248, 254-58 (3d Cir. 2009); *Proctor v. Vishay Intertech. Inc.*, 584 F.3d 1208, 1228-29 (9th Cir. 2009). The Third Circuit, for example, has explained that "SLUSA does not mandate dismissal of an action in its entirety where the action includes only some preempted claims." *In re Lord Abbett*, 553 F.3d at 255-56. Instead, the court concluded: "Allowing those claims that do not fall within SLUSA's preemptive scope to proceed, while dismissing those that do, is consistent with the goals of preventing abusive securities litigation while promoting national legal

7. Although we discussed the plaintiff's claims in *Brown* collectively, and thus referred to a single "suit," we did not address the issue of whether individual claims may be preempted under SLUSA.

standards for nationally traded securities." *Id.* at 257. On the other hand, some courts have interpreted SLUSA to preempt actions, not individual claims. *See Behlen v. Merrill Lynch*, 311 F.3d 1087, 1095 n.6 (11th Cir. 2002); *Hidalgo-Velez v. San Juan Asset Mgmt., Inc.*, Civil No. 11-2175CCC, 2012 U.S. Dist. LEXIS 136714, 2012 WL 4427077, at *3 (D.P.R. Sept. 24, 2012), *rev'd on other grounds*, 758 F.3d 98 (1st Cir. 2014) ("Removal of the entire action was proper because SLUSA precludes actions; not just claims. Based on [SLUSA's] statutory language, many courts have rejected the claim-by-claim analysis advanced by Plaintiffs.") (citation omitted) (collecting cases).

This appeal, however, does not require us to resolve the issue. Richek's second claim, alleging breach of contract, also triggered SLUSA preemption. Specifically, Richek's amended complaint alleged,

> Despite full performance by plaintiff and the other members of the Class, defendants breached their contract with plaintiff and the other members of the Class by receiving daily cash re-investment (sweep) fees on cash balances in Custody Accounts that were transferred into money market or other investment vehicles from the recipients of the transferred funds, *without authorization, or disclosure to*, Custody Account holders.

(emphasis added). We have previously explained that "a plaintiff [should not be able to] evade SLUSA by making a claim that did not *require* a misrepresentation

[or omission] in every case, such as a claim of breach of contract, but did in the particular case." *Brown*, 664 F.3d at 127. The same is true here. Richek alleged the Bank breached the contract by receiving the "sweep fees" without "authorization, or disclosure to," Richek. The disclosure claim inherently alleges a material misrepresentation or omission for the same reasons that the "disclosure" language in Richek's fiduciary duty claim does. And for Richek to have "authorized" the fees, the Bank would have had to have disclosed them to him; so the "authorization" claim was still fundamentally tied to a material misrepresentation or omission.

As noted in *Holtz*, SLUSA does not preempt all contract claims—just those that allege misrepresentations or omissions. Claims involving negligent breach or post-agreement decisions to breach, for example, may avoid SLUSA's scope. *Holtz*, 2017 U.S. App. LEXIS 1112, [slip. op.] at 7. I do not, however, read the examples identified in *Holtz* as exhaustive. Richek's breach of contract claim may have avoided SLUSA preemption had he pleaded, for instance, that the Bank effectively reduced the "returns" the parties had agreed Richek would receive. Although such an allegation would not necessarily have involved negligence on the Bank's part, or a post-agreement decision to breach, it still may have successfully supported a breach of contract claim that did not include a material misrepresentation or omission. But Richek did not take this approach.

Thus, SLUSA preempted Richek's complaint, and the district court properly dismissed it.

HAMILTON, *Circuit Judge*, dissenting. "Just as plaintiffs cannot avoid SLUSA through crafty pleading, defendants may not recast contract claims as fraud claims by arguing that they 'really' involve deception or misrepresentation." *Freeman Investments, L.P. v. Pacific Life Ins. Co.*, 704 F.3d 1110, 1116 (9th Cir. 2013) (reversing dismissal of similar breach of contract case). That's why we should reverse the dismissal of this complaint, which alleges only breach of contract and breach of fiduciary duty, not any form of fraud or negligent misrepresentation.

Plaintiff's breach of contract claim is simple: my contract with the bank spelled out the fees the bank would charge for its services. The bank breached the contract by charging additional fees. Plaintiff can prove that claim without proving any misrepresentation or omission of material fact.

To affirm dismissal, however, my colleagues transform this simple claim for breach of contract into one of "omission of a material fact." The "omitted fact" was that the bank was breaching the contract by charging the unauthorized fees. By this sort of reverse alchemy, my colleagues turn gold into lead. They use logic that other circuits have rejected and transform an ordinary state-law claim for breach of contract into a leaden and doomed claim under federal securities law. I respectfully dissent.

The opinions in this case and *Holtz v. JPMorgan Chase Bank, N.A.*, No. 13-2609, widen an already existing circuit split under SLUSA. They also head in the wrong direction. They take our circuit to a position that: (a) departs from the statutory text; (b) loses sight of Congress's efforts

in SLUSA to protect federalism interests; (c) selects a standard for SLUSA preemption that is difficult to administer and will produce arbitrary results; and (d) takes special-interest legislation to extraordinary lengths. The opinions shelter the wrongful conduct of powerful financial institutions from the only viable means to enforce contractual and fiduciary duties.

We should instead apply the standard adopted in the Second, Third, and Ninth Circuits, which allows class actions under state contract and fiduciary law where the plaintiffs can prevail on their claims without proving the defendants engaged in deceptive misrepresentations or omissions. *In re Kingate Management Ltd. Litig.*, 784 F.3d 128, 149, 152 (2d Cir. 2015); *Freeman Investments*, 704 F.3d at 1115-16; *LaSala v. Bordier et Cie*, 519 F.3d 121, 141 (3d Cir. 2008).

I. SLUSA: The Securities Fraud Core and the Issue of Expansion to Contract Claims

The general story of "SLUSA," the acronym for the Securities Litigation Uniform Standards Act of 1998, is well known. In 1995, Congress enacted stringent new pleading standards for private federal securities fraud litigation in the Private Securities Litigation Reform Act. Securities plaintiffs and their lawyers responded to the 1995 Act by bringing securities fraud claims involving securities traded on national markets in state courts under state law.

Congress enacted SLUSA to prevent such avoidance of the standards of the 1995 Act. See *Merrill Lynch, Pierce,*

Fenner & Smith Inc. v. Dabit, 547 U.S. 71, 82, 126 S. Ct. 1503, 164 L. Ed. 2d 179 (2006). SLUSA includes provisions in 15 U.S.C. §§ 77p(b) and 78bb(f)(1) to bar plaintiffs from using fraud class actions under state statutes or common law in connection with the purchase or sale of a security traded on a national exchange. In that core application, SLUSA seems to be working. The controversial question is whether SLUSA preemption reaches so far as to bar class actions asserting not fraud but only state-law claims for breach of contract or breach of fiduciary duty. If it does, then defendants can manage some extraordinary feats of legal jiu-jitsu to avoid liability for wrongdoing:

Start with a plaintiff, a customer of a bank or securities firm, who believes that she and other customers are the victims of systematic breaches of contract and fiduciary duty. She knows she does not have a viable claim under federal securities law or for common-law fraud. She files a class action in state court under state contract and fiduciary law. The defendant removes to federal court and argues for dismissal under SLUSA. The jiu-jitsu move is that the defendant then embraces a sweeping approach to federal securities law. It argues that the plaintiff *could* assert a securities fraud claim (though perhaps a fatally flawed one), that that's what she must really be doing, and that only her artful pleading conceals that claim. If this logical flip works, SLUSA requires dismissal of a perfectly good contract claim.

In our prior SLUSA cases, we have taken care to leave room for state-law claims for breach of contract, at least. See *Kurz v. Fidelity Management & Research Co.*, 556 F.3d 639, 640 (7th Cir. 2009). By extending SLUSA

preemption to dismiss the state-law class actions in *Goldberg* and *Holtz*, my colleagues effectively immunize a favored category of defendants—banks and securities businesses—from liability for their breaches of contract and fiduciary duty. That is an erroneous interpretation of SLUSA.

The critical statutory language describes which state-law class actions are not permitted:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging—
>
> (A) *a misrepresentation or omission of a material fact* in connection with the purchase or sale of a covered security; or
>
> (B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

15 U.S.C. § 78bb(f)(1). The key phrase in (A), "alleging a misrepresentation or omission of a material fact," is of course the language of fraud and negligent misrepresentation, and (B) also echoes the prohibitions of federal securities law.

How might one transform a complaint alleging only breach of contract and breach of fiduciary duty into one

"alleging a misrepresentation or omission of a material fact"? The problem is that parties who disagree about the meaning of their contract will often believe and allege that the counter-party has told them something that is not true or has failed to disclose something, such as that party's different interpretation of the contract. Also, a fiduciary owes a beneficiary a duty of candor, see generally Restatement (Third) of Trusts §§ 82 (duty to provide information), 109 (duty to account for principal and income). A breach of that duty can look a lot like an "omission of a material fact."

II. The Circuit Split

How should a court apply SLUSA to such class action complaints alleging state-law claims for breaches of contract and fiduciary duty? This question has produced at least a three- or four-way circuit split.

Since the 2012 oral argument in this case, the Second and Ninth Circuits have adopted the approach that I believe is best: a class action claim is barred by SLUSA only if the plaintiff's claim requires proof of a misrepresentation or omission of material fact. This approach avoids both the risks of artful pleading by plaintiffs and the jiu-jitsu move by defendants. It bars claims that are, in substance, for fraud or negligent misrepresentation yet allows contract and fiduciary claims to go forward. This approach is most consistent with the statute's text and purposes, and it is administrable and fair.[1]

1. The recent Second and Ninth Circuit cases explain why my description of the circuit split differs from that in Judge Flaum's concurrence.

In *Freeman Investments, L.P. v. Pacific Life Ins. Co.*, 704 F.3d 1110 (9th Cir. 2013), the defendant had sold variable universal life insurance policies to the plaintiffs. The plaintiffs alleged that the defendant had breached their contracts and a duty of good faith and fair dealing by charging policyholders an excessive "cost of insurance." The original complaint had included allegations of systematic concealment and deceit involving hidden fees. Those allegations provided fuel for the defendants' argument that these were allegations of misrepresentations and omissions of material facts so that SLUSA should apply. The district court agreed and dismissed.

In an opinion by then-Chief Judge Kozinski, the Ninth Circuit reversed, explaining that SLUSA preemption should depend on what the plaintiffs would be *required* to show to prove their claims:

> *To succeed on this* [*contract*] *claim, plaintiffs need not show that Pacific misrepresented the cost of insurance or omitted critical details.* They need only persuade the court that theirs is the better reading of the contract term. *See Yount v. Acuff Rose-Opryland*, 103 F.3d 830, 836 (9th Cir. 1996). "[W]hile a contract dispute commonly involves a 'disputed truth' about the proper interpretation of the terms of a contract, that does not mean one party omitted a material fact by failing to anticipate, discover and disabuse the other of its contrary interpretation of a term in the contract." *Webster v. N.Y.*

> *Life Ins. and Annuity Corp.*, 386 F. Supp. 2d 438, 441 (S.D.N.Y. 2005). Just as plaintiffs cannot avoid SLUSA through crafty pleading, *defendants may not recast contract claims as fraud claims by arguing that they "really" involve deception or misrepresentation. Id.; see also Walling v. Beverly Enters.*, 476 F.2d 393, 397 (9th Cir. 1973) ("Not every breach of a stock sale agreement adds up to a violation of the securities law.").

704 F.3d at 1115-16 (emphasis added).

In *Kingate Management*, 784 F.3d 128, the Second Circuit adopted essentially the same approach in a complex case against some of the "feeder funds" for Bernie Madoff's Ponzi scheme. The plaintiffs asserted 28 claims, which the Second Circuit organized in five groups. Most relevant for our purposes are the "Group 4" and "Group 5" claims for breaches of contract and fiduciary duty and other non-fraud tort theories, and for recovery of professional fees that were calculated in error or charged for services performed poorly. The district court had dismissed the entire case under SLUSA.

The Second Circuit reversed in a thorough opinion by Judge Leval. SLUSA preempted some claims alleging that the defendants themselves had engaged in fraudulent or negligent misrepresentations. SLUSA did not preempt the claims for breaches of contract or fiduciary duty or for fees. Those claims would not *require* the plaintiffs to prove that the defendants had misrepresented or omitted

material facts, so they were not preempted by SLUSA. 784 F.3d at 151-52. Accord, *LaSala v. Bordier et Cie*, 519 F.3d 121, 141 (3d Cir. 2008) (reversing dismissal; SLUSA preemption would not apply to breach of fiduciary duty claims unless allegation of misrepresentation operates as "factual predicate" for claim; extraneous allegations would not support SLUSA preemption) (Pollak, J.); *Norman v. Salomon Smith Barney, Inc.*, 350 F. Supp. 2d 382, 387-88 (S.D.N.Y. 2004) (Lynch, J.) ("Plaintiffs' claim is simply that Salomon said it would do something in exchange for plaintiffs' fees, and then didn't do what it had promised. The fact that the actions underlying the alleged breach could also form the factual predicate for a securities fraud action by different plaintiffs cannot magically transform every dispute between broker-dealers and their customers into a federal securities claim—the mere 'involvement of securities [does] not implicate the anti-fraud provisions of the securities laws.'").

The Sixth Circuit takes a different approach. It does not consider whether allegations of fraud are required to prove the plaintiffs' contract claim: "[SLUSA] does not ask whether the complaint makes 'material' or 'dependent' allegations of misrepresentations in connection with buying or selling securities. It asks whether the complaint includes these types of allegations, pure and simple." *Segal v. Fifth Third Bank, N.A.*, 581 F.3d 305, 311 (6th Cir. 2009), quoted in *Atkinson v. Morgan Asset Mgmt., Inc.*, 658 F.3d 549, 555 (6th Cir. 2011). This seemingly textual approach is not symmetrical, however. If the *plaintiff* has *omitted* allegations of fraud, the Sixth Circuit instructs district courts to treat the omission as artful pleading, to imply

the toxic allegations, and to dismiss. *Atkinson*, 658 F.3d at 555, following *Segal*, 581 F.3d at 310-11.

Before today's decisions in *Holtz* and *Goldberg*, we applied a third standard for deciding when a contract or fiduciary claim might be preempted. In *Kurz v. Fidelity Management & Research*, 556 F.3d at 641, and *Brown v. Calamos*, 664 F.3d 123, 127 (7th Cir. 2011), we signaled that SLUSA would not preempt contract claims. In *Brown*, we addressed the problems I discuss here. We allowed considerably more room for contract class actions, but under a standard that is difficult to administer. *Brown* requires a court to look at a complaint and to prophesy whether "it is likely that an issue of fraud will arise in the course of the litigation." 664 F.3d at 128-29.

While I believe plaintiff should prevail here under the better rule adopted by the Second, Ninth, and Third Circuits, plaintiff should also prevail under *Brown*. Her breach of contract claim requires her to show only that the contract with the bank authorized certain fees and that the bank breached the contract by charging additional fees (in the form of retaining the "sweep fees" paid for the investment of plaintiffs' funds). There is no need for fraud to become an issue.

In both this case and *Holtz*, however, my colleagues go beyond the *Brown* standard and adopt a new, fourth standard that is different from any other circuit's approach. Under *Goldberg* and *Holtz*, now, virtually any breach of contract claim is preempted. If the defendant had told the plaintiff what it was actually doing, the

plaintiff's acquiescence could have been treated as a modification or waiver of the relevant contract terms. Thus can virtually any breach of contract claim by the customer of a securities firm be transformed into a doomed securities fraud claim that must be dismissed.

My colleagues offer a couple of interesting exceptions, though. One is for negligent breaches of contract, "by mistake." *Holtz*, ___ F.3d at ___, 2017 U.S. App. LEXIS 1112 at *8. Why the defendant's state of mind should matter to a breach of contract claim is not explained, as a matter of either contract law or federal securities law. SLUSA surely preempts claims for negligent misrepresentation as well as those for intentional fraud. (Recall that SLUSA preemption does not include a scienter requirement.) This proposed exception has no apparent basis in the text of SLUSA and seems entirely arbitrary.

The second exception is for breaches of contract that occur after a plaintiff has already invested her money, presumably because such a breach is not "in connection with" the purchase or sale of a covered security. While the statutory text seems to support this exception, it is likely to have little meaning. In this case, for example, if the bank's retention of the sweep fees was a breach of contract, it happened *every day*, and "in connection with" the bank's purchases and sales of the securities with plaintiff's capital. In any event, the limited scope of this exception will surely produce arbitrary results.[2]

2. Circuits have also divided on two related procedural questions: whether SLUSA preemption should be analyzed and applied to the entire civil action or claim-by-claim, and whether a

III. The Merits of Preempting Contract Claims

Only the Supreme Court can settle this three-or four-way circuit split. The Second Circuit's opinion in *Kingate*, the Ninth's in *Freeman*, and the Third's in *Bordier* explain well why the best approach to this preemption problem is to ask whether the plaintiffs would be required to prove a misrepresentation or omission of a material fact. I offer a few additional thoughts prompted by my colleagues' opinions in this case and *Holtz*.

First, my colleagues take statutory purpose too far. The core of their thinking appears in *Holtz*: "Allowing plaintiffs to avoid [SLUSA] by contending that they have 'contract' claims about securities, rather than 'securities' claims, would render [SLUSA] ineffectual, because almost all federal securities suits could be recharacterized as contract suits about the securities involved." ___F.3d at ___, 2017 U.S. App. LEXIS 1112 at *5.

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plaintiff whose complaint or claim is deemed preempted should have any opportunity to amend the pleading to cure the problem. Compare, e.g., *Kingate*, 784 F.3d at 152-53 (applying SLUSA preemption claim-by-claim), with *Atkinson*, 658 F.3d at 555-56 (in dicta, one preempted claim requires dismissal of entire case); also compare, e.g., *Freeman*, 704 F.3d at 1116 (allowing amendment), and *U.S. Mortgage, Inc. v. Saxton*, 494 F.3d 833, 842-43 (9th Cir. 2007) (allowing amendment), with *Brown*, 664 F.3d at 131 (not allowing amendment). I agree with the claim-by-claim approach and allowing plaintiffs who can avoid SLUSA preemption to do so by amendment. Especially under post-*Iqbal* federal civil pleading standards, plaintiffs have strong incentives to say more than is necessary in their complaints. Alleging a little more than necessary should not be fatal.

My colleagues have lost sight of a point that we and the Supreme Court have made repeatedly: "no legislation pursues its purposes at all costs. Deciding what competing values will or will not be sacrificed to the achievement of a particular objective is the very essence of legislative choice—and it frustrates rather than effectuates legislative intent simplistically to assume that whatever furthers the statute's primary objective must be the law." *Rodriguez v. United States*, 480 U.S. 522, 525-26, 107 S. Ct. 1391, 94 L. Ed. 2d 533 (1987); see also, e.g., *Board of Governors of Federal Reserve System v. Dimension Financial Corp.*, 474 U.S. 361, 373-74, 106 S. Ct. 681, 88 L. Ed. 2d 691 (1986) ("Application of 'broad purposes' of legislation at the expense of specific provisions ignores the complexity of the problems Congress is called upon to address and the dynamics of legislative action. Congress may be unanimous in its intent to stamp out some vague social or economic evil; however, because its Members may differ sharply on the means for effectuating that intent, the final language of the legislation may reflect hard-fought compromises."); *Covalt v. Carey Canada, Inc.*, 860 F.2d 1434, 1439 (7th Cir. 1988) ("Courts do not strive for 'more' of all legislative objectives, however; laws have both directions and limits, and each must be scrupulously honored.").

We have made the same point more colorfully, in a way that applies directly here: "When special interests claim that they have obtained favors from Congress, a court should ask to see the bill of sale. Special interest laws do not have 'spirits,' and it is inappropriate to extend them to achieve more of the objective the lobbyists wanted."

Chicago Prof'l Sports Ltd. P'ship v. Nat'l Basketball Ass'n, 961 F.2d 667, 671 (7th Cir. 1992).

The banks and securities businesses that won passage of SLUSA did not win a broad preemptive provision for all class action claims that might be made in connection with purchases or sales of covered securities. They certainly did not win passage of language preempting state-law claims for breach of contract or fiduciary duty. The enacted language preempts covered class action claims that allege "a misrepresentation or omission of material fact." That language obviously calls to mind the law of fraud and (because there is no mention of scienter) negligent misrepresentation. See also *Chadbourne & Parke LLP v. Troise*, 571 U.S. ___, ___, 134 S. Ct. 1058, 1068-69, 188 L. Ed. 2d 88 (2014) (rejecting purpose-based efforts to expand reach of SLUSA).

My colleagues' approach also fails to give effect to the federalism balance struck in SLUSA. As the Supreme Court pointed out in *Dabit*, the statute was drafted to preserve certain specific roles for state securities law and securities regulators. See *Dabit*, 547 U.S. at 87-88, discussing 15 U.S.C. § 78bb(f)(3), (f)(4), & (f)(5)(C); see also 15 U.S.C. § 77p (parallel provisions under 1933 Securities Act). The *Dabit* Court noted that including these explicit "carve-outs" for state law "both evinces congressional sensitivity to state prerogatives in this field and makes it inappropriate for courts to create additional, implied exceptions." *Id.* (rejecting implied exception for fraud claims alleging inducement *not* to sell or purchase securities); accord, *Chadbourne & Parke*, 571 U.S. at ___,

134 S. Ct. at 1068-69 (interpreting SLUSA to respect its limits and to preserve roles for state law and state courts).

That same federalism balance should persuade federal courts not to find in SLUSA implied authority to sweep up claims arising only under state law of contract and fiduciary duty. The Congress that took such care to leave room for certain state securities laws and enforcement powers would be surprised by these decisions. It would be surprised to learn that federal courts are reading the statute to give special privileges to banks and securities businesses by preventing effective enforcement against them of such core areas of state law as contract and fiduciary law.[3]

My colleagues' expansive reading of SLUSA also conflicts with the Supreme Court's approach to a closely

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3. My colleagues find support for their expansive treatment of SLUSA in *Northwest, Inc. v. Ginsberg*, 572 U.S. ___, 134 S. Ct. 1422, 188 L. Ed. 2d 538 (2014), which held that a state-law claim against an airline for breaching an implied covenant of good faith and fair dealing was preempted by the Airline Deregulation Act. See *Holtz*, ___ F.3d at ___, 2017 U.S. App. LEXIS 1112 at *6. The simple answer to this argument is that the preemptive language in the Airline Deregulation Act is much broader than the relevant language in SLUSA. The Airline Deregulation Act provides that states "may not enact or enforce a law, regulation, or other provision having the force and effect of law *related to* a price, route, or service of an air carrier that may provide air transportation under this subpart." 49 U.S.C. § 41713(b)(1) (emphasis added). To the extent *Northwest* is relevant here, it might affect only plaintiff's fiduciary duty claim, not her claim that the bank simply breached the fee provision of the written contract by charging extra fees not authorized by the contract.

related federalism issue in *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Manning*, 578 U.S. ___, 136 S. Ct. 1562, 194 L. Ed. 2d 671 (2016). The issue in *Manning* was whether section 27 of the Securities Exchange Act of 1934, which grants exclusive federal jurisdiction over actions "brought to enforce" Exchange Act requirements, extends to a complaint that is filed in state court and alleges only state-law claims, but mentions federal securities law. The unanimous Court said no, holding that the standard under section 27 is the same as the "arising under" rule for federal question jurisdiction under 28 U.S.C. § 1331, so that it applies when federal law creates the cause of action asserted and in a narrow category of cases where a state-law claim will necessarily raise a disputed and substantial issue of federal law. 578 U.S. at ___, 136 S. Ct. at 1569-70.

Most salient for these cases is the Court's federalism reasoning. 578 U.S. at ___, 136 S. Ct. at 1573-75 (Part II-C). The Court warned against reading grants of exclusive federal jurisdiction too broadly, so as to interfere with state law and state courts:

> Out of respect for state courts, this Court has time and again declined to construe federal jurisdictional statutes more expansively than their language, most fairly read, requires. We have reiterated the need to give "[d]ue regard [to] the rightful independence of state governments"— and more particularly, to the power of the States "to provide for the determination of controversies in their courts."

> *Romero*, 358 U.S., at 380 (quoting *Healy v. Ratta*, 292 U.S. 263, 270, 54 S. Ct. 700, 78 L. Ed. 1248 (1934); *Shamrock Oil & Gas Corp. v. Sheets*, 313 U.S. 100, 109, 61 S. Ct. 868, 85 L. Ed. 1214 (1941)). Our decisions, as we once put the point, reflect a "deeply felt and traditional reluctance ... to expand the jurisdiction of federal courts through a broad reading of jurisdictional statutes." *Romero*, 358 U.S., at 379. That interpretive stance serves, among other things, to keep state-law actions like Manning's in state court, and thus to help maintain the constitutional balance between state and federal judiciaries.

578 U.S. at ___, 136 S. Ct. at 1573.

Manning shows that Congress must use clear language if it intends to order federal courts to intrude into long-estab-lished realms of state law and state courts. The statutory language and standards in these cases are not identical, of course, but *Manning* was enforcing limits on a grant of exclusive federal jurisdiction. The Court explained that "it is less troubling for a state court to consider such an issue of [federal securities law] than to lose all ability to adjudicate a suit raising only state-law causes of action." 578 U.S. at ___, 136 S. Ct. at 1574. In *Manning* itself, the state-law complaint actually mentioned the federal securities laws but did not rely upon them for relief. The Court rejected Merrill Lynch's argument, akin to my colleagues' approach here and in *Holtz*, that a judge should go beyond the face of the complaint and find "artful pleading," leaving no room for

state law in the case simply because the plaintiff might have tried to assert a claim under federal law, but did not. Proper respect for the role of states and their laws should lead us to reject the similar attempted expansion of SLUSA preemption in this case and *Holtz*.

Finally, the rule of the Second, Ninth, and Third Circuits also has the benefit of being easier to administer fairly. As noted, our earlier *Brown* opinion requires judges to be prophets, looking at complaints and predicting whether fraud is likely to be an issue. The more expansive approach taken in this case and *Holtz* will likely produce results that are unpredictable, unfair, or both. When the defendants in *Manning* suggested a similar approach, the Supreme Court said it had "no idea how a court would make that judgment" and said that avoiding this "tortuous inquiry into artful pleading is one more good reason to reject" the approach. 578 U.S. at ___, 136 S. Ct. at 1575.

We should focus instead on whether a misrepresentation or omission of material fact is an element of the plaintiff's cause of action, as the Second and Ninth Circuits did in *Kingate* and *Freeman*. This would provide a straightforward standard consistent with the statutory language of fraud—"a misrepresentation or omission of a material fact." It can be applied fairly at the pleading stage, preventing both truly artful pleading by plaintiffs and unfair recasting of contract and fiduciary claims as securities claims.

APPENDIX C — MEMORANDUM OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION, FILED AUGUST 4, 2011

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

Case No.: 10-cv-6779

STEPHEN D. RICHEK, AS TRUSTEE OF THE RESIDUARY TRUST UNDER THE SEYMOUR RICHEK REVOCABLE TRUST, ON BEHALF OF THE TRUST AND ALL OTHERS SIMILARLY SITUATED,

Plaintiff,

v.

BANK OF AMERICA, N.A.,
AND LA SALLE BANK N.A.,

Defendants.

Judge Robert M. Dow, Jr.

MEMORANDUM OPINION AND ORDER

This matter is before the Court on a motion to dismiss [24] filed by Defendant Bank of America, N.A. (the "Bank" or "Defendant"), as successor to LaSalle Bank, N.A. Because Plaintiff's lawsuit is precluded by the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), 15

U.S.C. § 77p(b) and § 78bb(f)(1), Defendant's motion [24] is granted.

I. Background[1]

Plaintiff Stephen Rickek ("Plaintiff"), a trustee of a residuary trust under the Seymour Richek Revocable Trust (the "Trust"), filed this action in the Circuit Court of Cook County, Illinois on behalf of a class of other persons and entities who maintained custody accounts for which LaSalle Bank or Bank of America acted as agent and received fees on cash balances transferred from the custody accounts into money market or other investment vehicles from July 18, 1985 though the later of August 1, 2009, or the date on which these daily fees were eliminated. Defendant removed the case to this Court and then moved to dismiss, arguing that SLUSA permits the removal of, and precludes, Plaintiff's claim. Plaintiff disputes the applicability of SLUSA.[2]

In July 1985, Plaintiff entered into a written agreement with LaSalle Bank on behalf of the Trust to open and maintain a custodian account for the investment

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1. For purposes of Defendant's motion, the Court assumes as true all well-pleaded allegations set forth in Plaintiff's amended complaint. See, *e.g.*, *Killingsworth v. HSBC Bank Nevada, N.A.*, 507 F.3d 614, 618 (7th Cir. 2007).

2. In the alternative to their SLUSA preclusion argument, Defendant asserts additional bases for dismissal. Because the Court agrees that dismissal based on SLUSA is warranted, the Court need not address those arguments.

of moneys, securities, and other Trust properties. Under the agreement, LaSalle was to buy, sell, and exchange securities, and hold dividends, interest, and other income for the Trust, all subject to Plaintiff's instructions. Plaintiff alleges that his account had a daily cash re-investment feature (known as a "sweep" feature). Because the account had a sweep feature, cash balances remaining in the account at the end of each day—from deposits, sales of securities, dividends, interest, and other income earned—were automatically transferred or "swept" into certain investment vehicles, including shares of certain money market mutual funds, which had been selected by the Plaintiff from a list of eligible vehicles. The "approved list" of mutual funds allegedly included the Bank of America Money Market Savings Account, various Dreyfus cash management mutual funds, and other institutional cash management funds. These investment vehicles then invested the cash balances swept from the custodian account.

Plaintiff alleges that LaSalle transferred cash balances from Plaintiff's account to shares of money market mutual funds and other mutual fund investment vehicles that had undisclosed fee arrangements with LaSalle. The money market funds and other mutual fund investment vehicles in turn directly paid LaSalle daily cash re-investment fees (or "sweep fees"). Plaintiff believes that these sweep fees were as much as 35 or 45 "basis points" (0.35 or 0.45 percent) of the average daily cash balance swept from the custodian account into the particular fund. Also, Plaintiff maintains that LaSalle did not disclose these sweep fees to Plaintiff, and that Plaintiff

never agreed to the sweep fees. According to the amended complaint, Plaintiff asked Bank of America for a schedule or document reflecting sweep fee charges relating to the Trust's account and eventually was told that there was no recorded fee schedule for sweep fees, that they were "automatically deducted per each vehicle's unique fee basis," and that the Bank could not "accurately portray how sweep fees were assessed inception to current." Am. Compl. at ¶¶ 17- 18.

Plaintiff alleges that he first learned of the sweep fees on June 30, 2009, when Bank of America wrote to inform him that it was eliminating the sweep fees. In August 2009, the LaSalle account was converted to a Bank of America account and the sweep fee was eliminated.

II. Legal Standard for Rule 12(b)(6) Motions to Dismiss

A motion to dismiss pursuant to Federal Rule of Civil Procedure 12(b)(6) tests the sufficiency of the complaint, not the merits of the case. See *Gibson v. City of Chicago*, 910 F.2d 1510, 1520 (7th Cir. 1990). To survive a Rule 12(b)(6) motion to dismiss, the complaint first must comply with Rule 8(a) by providing "a short and plain statement of the claim showing that the pleader is entitled to relief" (Fed. R. Civ. P. 8(a)(2)), such that the defendant is given "fair notice of what the * * * claim is and the grounds upon which it rests." *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 555 (2007) (quoting *Conley v. Gibson*, 355 U.S. 41, 47 (1957)).

Second, the factual allegations in the complaint must be sufficient to raise the possibility of relief above the

"speculative level," assuming that all of the allegations in the complaint are true. *E.E.O.C. v. Concentra Health Servs., Inc.*, 496 F.3d 773, 776 (7th Cir. 2007) (quoting *Twombly*, 550 U.S. at 555, 569 n.14). "[O]nce a claim has been stated adequately, it may be supported by showing any set of facts consistent with the allegations in the complaint." *Twombly*, 550 U.S. at 562. The Court accepts as true all of the well-pleaded facts alleged by the plaintiff and all reasonable inferences that can be drawn therefrom. See *Barnes v. Briley*, 420 F.3d 673, 677 (7th Cir. 2005).

III. Analysis

Congress enacted SLUSA to remediate an "unintended consequence" of the Private Securities Litigation Reform Act of 1995 (the "PSLRA"): a spike in previously rare state-court litigation of class actions involving nationally traded securities. *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 82 (2006). The goal of the PSLRA was to curb nuisance suits and other perceived abuses of securities class actions. *Id.* at 81-82. But rather than stem the tide of such suits, the PSLRA prompted some plaintiffs (or rather their lawyers) to avoid the PSLRA's stringent pleading requirements and other provisions designed to ward off meritless suits by simply reformulating their claims as state law causes of action and bringing them in state courts. *Id.* To prevent private plaintiffs from frustrating the objectives of the PSLRA in this way, Congress enacted SLUSA, which provides:

> No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging-
>
> (1) an untrue statement or omission of a material fact in connection with the purchase or sale of a covered security; or
>
> (2) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.

15 U.S.C. § 77p(b).

The SLUSA preempts and precludes a claim if it: (i) is brought by a private party; (ii) is brought as a covered class action; (iii) is based on state law; (iv) alleges that the defendant misrepresented or omitted a material fact or employed a manipulative or deceptive device or contrivance; and (v) asserts that defendant did so in connection with the purchase or sale of a covered security. See 15 U.S.C. § 78bb(f)(1); 15 U.S.C. § 77p(b);[3] *Erb v. Alliance Capital Mgmt., L.P.*, 423 F.3d 647, 651 (7th Cir. 2005). A "covered class action" is a lawsuit in which damages are sought on behalf of more than 50 people. § 78bb(f)(5)(B). A "covered

3. SLUSA amends the Securities Act of 1933 and the Securities Exchange Act of 1934 in "substantially identical ways." *Dabit*, 547 U.S. at 82 n.6.

security" is one traded nationally and listed on a regulated national exchange. § 78bb(f)(5)(E). Pursuant to SLUSA, cases that meet these qualifications are removable. § 78bb(f)(2); see also *Kircher v. Putnam Funds Trust*, 547 U.S. 633, 642-43 (2006).

"Consistent with Congress's intent, courts construe SLUSA's 'expansive language broadly' to prevent frustration of the PSLRA's objectives." *Brown v. Calamos*, 2011 WL 1414168, at *2 (N.D. Ill. March 14, 2011) (Bucklo, J.) (quoting *Daniels v. Morgan Asset Management, Inc.*, 2010 WL 4024604, at *5 (W.D. Tenn. Sept 30, 2010) and *Segal v. Fifth Third Bank, N.A.*, 581 F.3d 305, 309 (6th Cir. 2009)); see also *Dabit*, 547 U.S. at 86. In particular, the Supreme Court held in *Dabit* that the "in connection with the purchase or sale of securities" requirement should be construed broadly to preclude suits by holders of securities, not just purchasers and sellers. 547 U.S. at 86-87. Similarly, as a general rule, litigants cannot avoid SLUSA preemption by bringing claims that effectively incorporate securities claims under state law theories. *Appert v. Morgan Stanley Dean Witter, Inc.*, 2009 WL 3764120, at *5 (N.D. Ill. Nov. 6, 2009); *Rabin v. JP Morgan Chase Bank*, 2007 WL 2295795, at *6 (N.D. Ill. Aug. 3 2007). "Consequently, when analyzing SLUSA preclusion, courts are guided by the substance rather than the form of a claim." *Id.*

Plaintiff does not dispute that this is a "covered class action," that it is based on state law, or that the securities in question are "covered securities." Rather, he argues that the amended complaint does not allege that Defendant

misrepresented or omitted a material fact or employed a manipulative or deceptive device or contrivance "in connection with" the purchase or sale of securities. Plaintiff contends that the purchase and sale of mutual fund shares was merely incidental to Defendant's alleged misconduct. In other words, Plaintiff does not deny that his class action claims are predicated upon allegations of misstatements, omissions, deception, and manipulation (nor does he argue that these allegations are inadvertent or ancillary to Plaintiff's state law class action claims). However, Plaintiff contends that SLUSA does not preempt his claims because the statute's "in connection with" requirement is narrow and preempts only those state law class claims where: (1) misrepresentations, omissions, deceptions, or manipulations are alleged to have influenced or caused an "investment decision" by a plaintiff; (2) a plaintiff is dissatisfied with a "discretionary" investment made for him by the defendant; or (3) a plaintiff's factual allegations could give rise to an implied private right of action under federal securities laws. Defendant in turn argues that Plaintiff's position is irreconcilable with the plain language of the statute, the Supreme Court's decision in *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, 547 U.S. 71 (2006), and other controlling legal authorities, and that SLUSA is much broader than Plaintiff asserts.

Under *Dabit*, 547 U.S. at 87-88, the Court may not construe SLUSA in a manner that would "create" any "additional, implied exceptions." In *Dabit*, the Supreme Court held that SLUSA's "in connection with" requirement should receive the same "broad construction" given to the "in connection with" language of Section 10(b) of

the Exchange Act and Rule 10b-5. The Court further explained that this broad construction extended "flexibly" to prohibit any misstatements and omissions touching upon the purchase or sale of a security—"whether by the plaintiff or someone else." *Id.* at 85. In reaching this conclusion, the Supreme Court expressly considered and rejected a narrower reading of the statutory language similar to the one advanced by Plaintiff—*i.e.*, a reading that assumes that SLUSA's "in connection with" language embraces only those particular cases where a plaintiff has made an investment decision to buy or sell securities in reliance on misstatements, omissions, or deceptive or manipulative conduct and where a plaintiff's factual allegations demonstrate all the other elements necessary to support an implied private right of action under federal securities laws. See *Dabit*, 547 U.S. at 84-88.

In this regard, *Dabit* closely followed *SEC v. Zandford*, 535 U.S. 813 (2002). In *Zandford*, the SEC brought a civil action against a broker who repeatedly sold his clients' stockholdings and diverted the sales proceeds to his own accounts. The Supreme Court held that the broker's scheme occurred "in connection with" the sale of the securities, even though his victim did not make any investment decision to purchase or sell a security "in reliance" on the broker's misrepresentations and omissions or authorize such transactions. *Id.* at 820. The broker's misrepresentations and omissions to his clients "coincided with the sales themselves," and each transaction was deceptive because the diversions of sales proceeds were "neither *authorized* by, nor *disclosed* to" the broker's clients. *Id.* at 820-21 (emphasis added). Thus,

under *Dabit*, "it is enough that the fraud alleged 'coincide' with a securities transaction— whether by the plaintiff or by someone else." *Dabit*, 547 U.S. at 85; see also *Siepel v. Bank of America, N.A.*, 526 F.3d 1122, 1127 (8th Cir. 2008) (explaining that "[w]hen [*Dabit*] rejected the *Blue Chip Stamps* limitation [on implied private rights of action under Section 10(b) and Rule 10b-5], [it] rejected wholesale the proposition that limitations on private Rule 10b-5 actions may be applied to limit the scope of SLUSA"); *Segal v. Fifth Third Bank, N.A.*, 581 F.3d 305, 312 (6th Cir. 2009) (noting that under *Dabit*, SLUSA precludes even state law claims that would not meet the 'policy'-based standing limitations the Court has attached to Rule 10b-5"); *U.S. Mortgage, Inc. v. Saxton*, 494 F.3d 833, 843-45 (9th Cir. 2007) (holding that it was immaterial that the plaintiffs did not personally make an investment decision to purchase, sell, or hold any stock in reliance on deceptive statements or conduct); *Rabin v. JPMorgan Chase Bank, N.A.*, 2007 WL 2295795, at *5-8 (N.D. Ill. Aug. 3, 2007); *Daniels v. Morgan Asset Management, Inc.*, 2010 WL 4024604 (W.D. Tenn. Sept. 30, 2010) (finding SLUSA preemption where plaintiffs alleged that defendants breached various duties by investing assets from the trust and custodian accounts in shares of expensive and poorly performing mutual funds and then failing to disclose fees and other compensation that the bank allegedly received from the funds).

Plaintiff attempts to distinguish this case from the above-cited authorities by arguing that in those cases there was no allegation of a breach of a "written contract" or that the defendants made "discretionary" investments on the plaintiff's behalf. Yet a review of these

cases indicates that Plaintiff's arguments simply are incorrect: the cases cited above did involve allegations that the defendants breached agreements and did assert claims for breach of contract, breach of fiduciary duties, and unjust enrichment comparable to Plaintiff's claims. Furthermore, the cited authorities do not turn on whether the plaintiff was dissatisfied with a "discretionary" investment made on his behalf by the defendant. Rather, SLUSA applied because the alleged misstatements and omissions touched upon and coincided with the purchase or sale of a covered security.

In addition to trying to distinguish the cases offered by Defendant, Plaintiff relies on *Gavin v. AT&T Corp.*, 464 F.3d 634 (7th Cir. 2006), to support his construction of SLUSA's "in connection with" requirement. *Gavin* was a consumer fraud action arising after a merger between AT&T and MediaOne. *Gavin*, 464 F.3d at 638-39. As a result of the merger, MediaOne's shareholders became the beneficial owners of AT&T stock. *Id.* Several months after the merger, AT&T hired a "post merger clean-up" specialist to notify former MediaOne shareholders about the process for exchanging their old MediaOne stock certificates for new certificates representing the AT&T shares that they had acquired through the merger. The service provider notified shareholders of a fee based process for obtaining new AT&T certificates but failed to inform them about an alternative, free process. *Id.* The plaintiffs in *Gavin* complained that defendants' conduct constituted fraud under state law and argued that SLUSA did not apply. *Id.* The Seventh Circuit agreed that the post-merger clean-up service at issue had nothing to do with the

purchase or sale of any security but only with the process for exchanging stock certificates. The court further held that SLUSA did not apply because the alleged fraud of failing to inform MediaOne shareholders of the free option occurred long after the securities transaction—the merger—took place. The court concluded that the connection between the defendants' conduct and the securities transaction was too attenuated to satisfy even the post-*Dabit,* broadly-interpreted "in connection with" requirement. *Id.* at 638–639.[4]

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4. Plaintiff also cites *Fishback v. Memory Gardens Management Corp.*, 2008 WL 2037308 (S.D. Ind. May 12, 2008) and *Kurz v. Fidelity Management & Research Co.*, 556 F.3d 639 (7th Cir. 2009), in support of his construction of SLUSA's "in connection with" requirement. In *Fishback v. Memory Gardens Mgmt. Corp.*, the plaintiff's complaint alleged looting of a trust fund created to finance the maintenance of cemeteries, but it contained no allegations "link[ing]" the alleged looting to the purchase or sale of any covered security in the trust account. 2008 WL 2037308, at *1 (S.D. Ind. May 12, 2008). The court found SLUSA inapplicable, but the five-paragraph order contains no substantive discussion of the factual allegations and no analysis of SLUSA's plain language, *Dabit, Zandford,* or any of the other authorities cited by Defendant. Plaintiff also contends that *Kurz v. Fidelity Mgmt. & Research Co.*, 556 F.3d 639, 641 (7th Cir. 2009), "recognize[s] that SLUSA does not displace contract law claims." *See* Pl. Resp. at 9. In *Kurz*, the Seventh Circuit affirmed the dismissal of a putative class action complaint for breach of contract based on SLUSA. The plaintiff argued that SLUSA did not apply to his putative class action because his "suit rest[ed] on contract law rather than 'a misrepresentation or omission of a material fact;'" however, the Seventh Circuit held that "[Plaintiff's] argument [was] frivolous, given *Dabit* * * * and *SEC v. Zandford* * * *." *Id.* (citations omitted).

In contrast to *Gavin*, the essence of Plaintiff's amended complaint is that the Bank made misrepresentations and omitted material facts regarding conflicts of interest and fees *relating to* the transfer of trust assets into mutual funds. See also *Wells Fargo Bank, N.A., v. Superior Court*, 159 Cal. App. 4th 381, 390-91 (Cal. App. Ct. 1st Dist. 2008) (rejecting narrow construction advanced by plaintiffs and distinguishing *Gavin* from situations where a defendant is alleged to have used account assets to purchase mutual shares and received and retained undisclosed fees and compensation in connection with that securities transaction). Plaintiff's amended complaint alleges that LaSalle decided which mutual funds to include as investment options for the custodian account's sweep feature, giving Plaintiff an "approved list" from which to choose. The approved list included mutual funds, like the Bank of America Money Market, that had agreed to pay fees in exchange for the purchase of mutual fund shares. Am. Compl. ¶¶2, 14, 26. The complaint also alleges that LaSalle had a legal duty to disclose any fees that it would receive from the money market mutual funds or other registered investment companies in exchange for investing daily cash balances in shares of the funds, and that LaSalle should have provided such information to Plaintiff both before and after cash balances were used to purchase mutual fund shares. Am. Compl. ¶¶ 1-2, 10, 23(a) & (b), 28(a) & (b), 35, 40-41. Further, Plaintiff alleges that LaSalle received and retained these undisclosed fees directly from these mutual funds (not from Plaintiff's custodian account) in exchange for the Bank's use of daily cash balances to purchase shares of the funds: "Defendants were aware that they were receiving substantial benefits in the form of

re-investment (sweep) fees based on the value and earnings of the cash balances that were transferred to investment vehicles from Custody Accounts." See Am. Compl. ¶¶ 2, 15, 23(a) &(b), 28(a) & (b), 37, 40-41. According to the amended complaint, LaSalle never disclosed or reported these fees to Plaintiff either on a fee schedule provided in advance of a securities transaction or an account statement issued after a securities transaction.

Id.

Additionally, Plaintiff maintains that LaSalle's misstatements, omissions, and related misconduct respecting the undisclosed fees were material to his decision to maintain a custodian account with the Bank and continue to have the Bank reinvest daily cash balances in these mutual fund shares. *Id.* ¶¶ 1-2, 10, 14-18; Pl. Mem. in Opp. 11. Finally, and perhaps more importantly for present purposes, Plaintiff ties his alleged injury to the value of the fees that Defendant allegedly received—fees that are alleged to be based expressly on the value of the mutual fund shares purchased for his account. Am. Compl. ¶¶ 2, 15, 18, 29-31, 38, 40-43, 46-48. By acknowledging that the fees generated were dependent on the value of the shares purchased, Plaintiff cannot escape the conclusion that Defendant's alleged scheme occurred "in connection with" the sale of the securities. Simply put, every aspect of the conduct at issue touches on or coincides with the purchase of mutual fund shares for Plaintiff's custodian account.

In sum, Plaintiff's amended complaint is replete with allegations that the Bank failed to disclose (or omitted) details regarding fees and the conflicts of interest inherent

in the Bank's "approved list" of mutual funds, and that these omissions caused injury to Plaintiff. Put another way, Plaintiff alleges that the Bank failed to disclose the financial gain retained by the Bank as a result of these transfers. This alleged misconduct occurred contemporaneously with the security transaction of investing[5] the trust's assets into mutual funds. Thus, at a minimum, the Bank's alleged fraudulent conduct "coincided" with a securities transaction (*Dabit*, 547 U.S. at 85), and Plaintiff's claims are precluded by SLUSA.

IV. Conclusion

For the reasons set forth above, the Court grants Defendant's motion to dismiss [24]. Judgment is entered for Defendants and against Plaintiff.

Dated: August 4, 2011

/s/
Robert M. Dow, Jr.
United States District Judge

5. Plaintiff amended his complaint to allege that cash balances were "transferred," rather than "invested,"in shares of money market mutual funds and other investment vehicles. Compare Compl. at ¶¶ 1-2, 14- 15 with Am. Compl. at ¶¶ 1-2, 14-15. Regardless of the word used to describe the process, the substance of the act of transferring the trust's assets into mutual funds is that they are invested, or re-invested, into mutual funds.