Securities Regulation Daily Wrap Up, FRAUD AND MANIPULATION —2d Cir: Dismissal of fraud claims stemming from Barclay's LIBOR manipulation reversed, (Apr. 25, 2014)

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By Matthew Garza, J.D.

The Second Circuit reversed a decision of the U.S. District Court in Manhattan to dismiss a securities fraud suit against British bank Barclays for manipulating the London Interbank Offered Rate (LIBOR) interest rate. A class of purchasers alleged that the bank and several top executives, including president Robert Diamond, manipulated the rate by misrepresenting the bank's cost of borrowing funds in violation of Exchange Act Section 10(b) and Rule 10b-5. Judge Scheindlin dismissed the case after ruling that the investor's complaint failed to plead loss causation or actionable misstatements or omissions. District Judge Richard Berman of the Southern District of New York, sitting by designation, vacated the decision in part after finding that allegations that Diamond made misleading statements on a 2008 conference call were plausible. Loss causation was also sufficiently established by pleadings that the bank's ADRs dropped 12 percent on June 28, 2012, the day after a $450 million settlement with the Department of Justice, CFTC, and the U.K.'s Financial Services Authority was announced (*Carpenters Pension Trust Fund of St. Louis v. Barclays PLC*, April 25, 2014, Berman, R.).

The LIBOR is calculated daily by Thomson Reuters Corporation after several banks answer the question "[a]t what rate could you borrow funds, were you able to do so by asking for and then accepting inter-bank offers in a reasonable market size just prior to 11 am?" The suit alleged that Barclays submitted artificially low rates between August 2007 and January 2009 to enhance the view of its financial results and boost its stock price.

The suit also alleged that Diamond, in a 2008 conference call with analysts, falsely denied that the bank was paying higher rates than other banks, saying "[w]e're categorically not paying higher rates in any currency." The plaintiffs also alleged that the bank misstated in SEC filings that it had appropriate internal controls in place.

Judge Berman noted that the Southern District of New York's dismissal concluded that even if Diamond's statements misled the market and inflated the bank's stock, any share inflation would have been rectified by an efficient market prior to announcement of the settlement with U.S. and U.K regulatory authorities. Internal control statements could not be materially false or misleading because they were mere puffery, held the lower court.

Loss causation. To plead loss causation, the court wrote, plaintiffs must allege that the fraudulent statement or omission was the cause of the loss suffered by showing (1) the existence of cause-in-fact on the ground that the market reacted negatively to a corrective disclosure of the fraud, or (2) that the loss was foreseeable and caused by the materialization of the risk concealed by the fraudulent statement. The allegations in this complaint were persuasive as to corrective disclosure, the court found, although the allegations under the risk materialization theory were not tenable.

Judge Berman wrote that the dismissal prematurely "perceived a temporal 'disconnect' between Barclays's submission of false LIBOR rates and the disclosure of the fraud in June 2012, and concluded that Barclays's (unchallenged) submission rates after January 2009 necessarily would have supplanted any prior LIBOR-related misinformation." The company could have provided accurate submission rates after 2009, but those submissions did not necessary correct the earlier misstatements, the court held. It concluded that "the efficient market hypothesis, premised upon the speed (efficiency) with which new information is incorporated into the price of a stock, does not tell us how long the inflationary effects of an uncorrected misrepresentation remain reflected in the price of a security." The record must be more fully developed to reach this conclusion, the court said.

Materiality was also established because the plaintiffs alleged that there was a substantial likelihood that the disclosure of Barclays's true borrowing costs between 2007 and 2009 would have been viewed by the reasonable investor as having significantly altered the total mix of information available to the market.

Internal controls. Allegations regarding misrepresentations about the bank's internal controls in SEC filings were not materially false because they were not specifically tied to the bank's LIBOR practices, held the court. These statements did not even mention LIBOR, nor did they claim to have internal controls specific to LIBOR submission rates, the court said, affirming dismissal of these claims. The lower court also correctly denied leave to amend the allegations regarding internal control statements.

The court's dismissal of the second amended complaint was covered in *Securities Regulation Daily* on May 14, 2013, and dismissal of the third amended complaint was covered June 14, 2013.

Companies: Barclays Bank PLC; Thomson Reuters Corp.

The case is No. 13-2678-cv.

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