

Securities Regulation Daily Wrap Up, BENEFICIAL OWNERSHIP—W.D. Tenn.: Individual Defendants’ grantor/trustee/beneficiary status misstated, not entitled to short-swing profits, (Nov. 18, 2024)

Securities Regulation Daily Wrap Up

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By [Jay Fishman, J.D.](#)

All of the individual defendant’s arguments fell like a house of cards because he could not prove his status as a grantor, trustee or beneficiary.

Tennessee’s Western District Court denied the individual defendant’s motion to dismiss the plaintiff shareholder’s complaint to recover short-swing profits under Securities Exchange Act Section 16(b). The defendants’ argument for a SEC Rule 16a-13 exemption was built on two incorrect assumptions: (1) that the individual defendant was a grantor, trustee and beneficiary entitled to the short-swing profits; and (2) that the facts supporting his grantor/trustee/beneficiary status was in the complaint—in reality, the supporting facts were outside the complaint (*Nosirrah Management v. Autozone*, No. 2:24-cv-02167-JPM-atc (W.D. Tenn. Nov. 15, 2024)).

Defendants’ path to short-swing profits. The plaintiff, a management company shareholder in the defendant company, alleged in its complaint that between December 2021 and January 2024, the individual defendant purchased shares of the defendant company’s stock and then sold the stock, thereby attaining over \$1 million in short-swing profits. A subsequent conversation between the plaintiff and defendant company revealed it would not “pursue disgorgement” from the individual defendant because the purchases were from the individual defendant’s grantor retained annuity trusts (GRATs). GRATs exist for a specified time-period with annuity payments made to the individual defendant, after which the assets, if any in the GRATs, are transferred to the residual beneficiaries. The plaintiff brought suit to recover the short-swing profits on the defendant company’s behalf [the defendant company would retain those profits upon recovery].

Defendant’s contentions. The individual defendant contended:

- He was the settlor, trustee and sole lifetime beneficiary of the GRATs at issue;
- The transactions were not purchases of defendant company stock but rather in-kind annuity payments under the GRATs terms;
- As GRAT annuities, they were exempt from 16(b) under SEC Rule 16a-13; and
- His acquisition of the stock from the GRAT’s “merely changed the form of his beneficial owners over the stock, from indirect to direct, without changing his pecuniary interest in the securities.”

Plaintiff’s arguments. The plaintiff’s overall argument asserted that the U.S. Supreme Court’s 2024 decision in *Loper Bright Enterprises v. Raimondo*, by overruling the court’s 1984 *Chevron* decision, weakened the individual defendant’s above-stated contentions.

Court rules for plaintiff—denies individual defendant’s motion to dismiss. The court began by stating that for a plaintiff to succeed on a Section 16(b) claim for liability against the individual defendant, the plaintiff must prove that there was: (a) a purchase, (b) a sale of securities, (c) by an officer or director of the issuer [here, the defendant company] or by a shareholder who owns more than 10 percent of any one class of the issuer’s securities, and (d) within a six-month period. But the court also provided a caveat for liability: the SEC Rule 16a-13 exemption will apply to “a transaction...that effects only a change in the form of beneficial ownership without changing a person’s pecuniary interest in the subject equity securities....”

Individual defendant’s grantor, trustee and sole lifetime GRAT beneficiary status. On this first issue, the court disagreed with the individual defendant that support for his status as a grantor, trustee and sole lifetime

beneficiary was contained in the complaint. At most, the court said, the complaint stated the defendant was the creator of the GRATs—not enough support in the complaint to substantiate his grantor/trustee/beneficiary status. And furthermore, that status was not supported by any exhibits, public records or other attachments.

Sufficient pleading of Section 16(b) liability elements. Pertaining the “purchase element,” the individual defendant relied on a no-action letter which granted a defendant in similar circumstances the Rule 16a-13 exemption. The court, however, declared that unlike cases, no-action letters are time-bound and, therefore, cannot be precedents. But moreover, this case is distinguished because the opportunity existed for the individual defendant to abuse inside information as the defendant company’s officer/director in order to substitute property of equal value to get the GRAT shares back just before the shares appreciated drastically. Lastly, the court agreed with the plaintiff’s allegation that the individual defendant obtained the defendant company stock and profited off it, which was enough to show at the motion to dismiss stage of the litigation that there was a purchase “that best serves the congressional purpose of curbing short-swing speculation by corporate insiders.”

The court automatically found for the plaintiff on the other three 16(b) liability elements because the individual defendant could not prove his grantor/trustee/beneficiary status from the complaint or from any supporting documents.

SEC Rule 16a-13 exemption applying to “a transaction...that effects only a change in the form of beneficial ownership without changing a person’s pecuniary interest in the subject equity securities....”

To resolve this issue, the court had to examine two requirements:

1. Whether there was no change in the defendant’s pecuniary interest in the defendant company stock; and
2. Whether there was only a change in the form of the individual defendant’s beneficial ownership of the stock.

After analysis, the court ended up ruling against the individual defendant on both of the above requirements because the individual defendant was unable to prove his grantor, trustee and/or sole life-time beneficiary status either in the complaint or by providing supporting attachments or exhibits.

The case is [No. 2:24-cv-02167-JPM-atc](#).

Judge: McCalla, J.

Attorneys: Ann Heimberger Jernow (Sterlington, PLLC) for Nosirrah Management, LLC. Brian Francis Irving (Bass, Berry & Sims PLC) for Autozone, Inc. Kristine L. Roberts (Baker, Donelson, Bearman, Caldwell & Berkowitz, PC) for William C. Rhodes, III.

Companies: Nosirrah Management, LLC; Autozone, Inc.

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