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Quarterly Survey of SEC Rulemaking and Major Court Decisions (July 1, 2023 – September 30, 2023)

By Kenneth M. Silverman and Brian Katz[*]

This issue's Survey focuses on the U.S. Securities and Exchange Commission's ("SEC") rulemaking activities and other decisions relating to the Securities Act of 1933, as amended (the "1933 Act"), the Securities Exchange Act of 1934, as amended (the "1934 Act"), and other federal securities laws from July 1, 2023 through September 30, 2023.

This quarter, the SEC proposed six new rules and approved seven final rules. In pertinent part, the final and proposed rules continue the ongoing trend in recent years to modernize current regulatory frameworks in a manner that facilitates increased market resiliency and investor protection.

Final Rules

Money Market Fund Reforms

On July 12, 2023, the SEC adopted final rules to certain regulations that govern money market funds under the Investment Company Act of 1940, as amended (the "Investment Company Act"). Amended Rule 2a-7 sets forth new requirements that, in part, require money market fund managers to increase minimum daily and weekly liquidity requirements of funds, prohibit temporary suspension of redemptions, and require institutional prime and tax exempt money market funds to impose mandatory liquidity fees under certain conditions.

Currently, money market funds (other than those that are tax-exempt) must hold at least 10% of their total assets in "daily liquid assets" and 30% in "weekly liquid assets." Amended Rule 2a-7 increases these requirements to 25% and 50% respectively. Failure to meet these requirements past a certain threshold requires notification to the fund's board within four business days of such event. Additionally, prior to the implementation of these final rules, money market funds had the ability to impose a

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"redemption gate," which permitted the boards of non-government money market funds to suspend redemptions for up to ten business days within a 90-day period if the fund's weekly assets dropped below 30% of its total assets. When the SEC originally adopted a rule in 2014 to permit such money market funds to impose a redemption gate, it was intended to act as a tool to preserve liquidity during times of market volatility, but research since has indicated that it may have had the opposite effect as first mover investors would be incentivized to rush to pull funds out before the redemption gate could be implemented. The new rules remove money market funds' ability to implement a redemption gate.

With the stated goal of protecting shareholders from dilution and unfair cost allocation, the final rules also revise the liquidity fee framework to require institutional prime and institutional tax-exempt money market funds to impose mandatory liquidity fees on redeemed shares when daily net redemptions exceed 5% of a fund's net assets, subject to certain exceptions. Non-government money market funds must impose a discretionary liquidity fee on redeemed shares if the fund's board determines such fee is in its best interest.

The final rules also add provisions for retail and government money market funds operating in negative interest rate environments, providing that such funds may elect to either convert from a stable share price to a floating share price or reduce the number of shares outstanding to maintain a stable net asset value per share, subject to certain board determinations and disclosures to investors.

The SEC did not adopt more controversial provisions from the initially proposed rules that would have required institutional prime and institutional tax-exempt money market funds to implement swing pricing during periods of net redemptions. Instead, the SEC adopted the aforementioned mandatory liquidity fee framework in its place. Representing the SEC's third money market fund reform since 2010, the SEC hopes that these adopted rules will further the SEC's stated goal of rulemaking in this space by improving the resilience and transparency of money market funds. However, the final rules may raise implementation challenges for funds as managers work to increase liquidity.

The final rules provide for certain modifications to Form N-CR regarding the reporting of liquidity thresholds and events, as well as providing for corresponding changes to Form N-MFP and Form N-1A. The final rules become effective on October 2, 2023. However, the SEC has provided a transition period to comply with certain parts of the final rules: by April 2, 2024, money market funds will be required to comply with the portfolio liquidity provisions and discretionary liquidity fee and by October 2, 2024, money market funds will be required to comply with the mandatory liquidity fee.

FINRA Membership Exemption Changes for Broker-Dealers

On August 23, 2023, the SEC adopted final amendments to Rule 15b9-1 of the 1934 Act that narrow an exemption for broker-dealers from the requirement to become a member of the Financial Industry Regulation Authority, Inc. ("FINRA"). Section 15(b)(8) of the 1934 Act requires broker-dealers registered with the SEC to become a member of a national securities association (of which FINRA is currently the only qualifying entity) unless certain exemptions provided for under Rule 15b9-1 are satisfied. The adopted rules amend Rule 15b9-1 of the 1934 Act by empowering FINRA with greater jurisdiction to require most proprietary trading broker-dealers to become a member of FINRA. As a result, practically all broker-dealer will be required to become a member of FINRA.

Prior to this final rule, a broker-dealer could avoid FINRA membership under Rule 15b9-1 if it was (i) a member of a national securities exchange, (ii) carried no customer accounts and (iii) had annual gross income derived from securities transactions other than those on a national securities exchange of which it was a member in an amount no greater than $1,000, excluding income derived from transactions through the broker-dealer's own account with or through another registered broker-dealer. As amended, Rule 15b9-1 eliminates the proprietary trading exclusion set forth in the foregoing third prong.

Now, as a result of the final rules, an SEC registered broker or dealer will be required to become a member of FINRA pursuant to Section 15(b)(8) if it effects securities transactions other than on an exchange where it is a member, unless (i) it is a member of a national securities exchange, (ii) it carries no customer accounts and (iii) such transactions (a) result solely from orders that are routed by a national securities exchange of which the broker or dealer is a member to comply with order protection regulatory requirements (e.g., Rule 611 of Regulation NMS or the Options Order Protection and Locked/Cross Market Plan) or (b) are solely for purposes of executing the stock leg of a stock-option order. This third option will be largely unavailable for many proprietary broker-dealers, so impacted entities should note the potentially significant implications of becoming subject to FINRA compliance and examination requirements once the final rule becomes effective November 6, 2023 and prior to the compliance deadline of September 6, 2024.

Private Fund Adviser Rules

On August 23, 2023, the SEC adopted long-awaited final rules promulgated under the Investment Advisers Act of 1940, as amended (the "Advisers Act"), that substantially affect SEC-registered investment advisors ("RIAs") and exempt reporting advisers ("ERAs"). The final rules consist of five rules referred to as the Preferential Treatment Rule, Restricted Activities Rule, Adviser-Led Secondaries Rule, Private Fund Audit Rule and Quarterly Statement Rule (together, the "Private Fund Adviser Rules"). The Preferential Treatment Rule and the Restricted Activities are applicable to both RIAs and ERAs, while the remaining three rules are only applicable to RIAs.

Preferential Treatment Rule

Under the Preferential Treatment Rule set forth under Rule 211(h)(2)-3 under the Advisers Act, no private fund adviser, including ERAs, may directly or indirectly (i) provide preferential redemption terms to an investor in a private fund or in a similar pool of assets or (ii) provide certain information about the fund's portfolio holdings to any private fund investor if the adviser reasonably expects such redemption terms or information would have a material negative effect on other investors in that private fund or similar pool of assets.

There are certain exceptions to this rule. Providing preferential redemption rights is not prohibited if an investor is required to redeem under applicable laws (explicitly excluding redemptions mandated by an investor's internal policies or compliance requirements) or if the adviser has offered the same redemption ability to all existing investors and will continue to do so to all future investors. The latter exception does not require that investors be offered identical redemption rights, rather the end result must be the same. Preferential redemption rights may also be permitted if such treatment is disclosed in a written notice to prospective and current investors, subject to certain additional requirements.

Restricted Activities Rule

Under new Rule 211(h)(2)-1 under the Advisers Act, fund advisers cannot engage in the following activities without providing appropriate specified disclosures, and, in some cases, obtaining investor consent: (i) charging or allocating to the private fund any fees or expenses associated with any regulatory or compliance requirements or examination fees or costs of the adviser or its related persons, (ii) reducing adviser clawback obligations for taxes, (iii) charging or allocating fees and or expenses related to a portfolio investment on a non-pro rata basis where there are multiple entities advised by the same adviser investing in the same portfolio investment, and (iv) borrowing or receiving funds from a client.

Fund advisers must provide written notice of any fees or costs associated with regulatory, compliance or examination requirements on at least a quarterly basis if such fees or costs are to be charged or allocated to the private fund. For adviser clawbacks, written notice must be provided disclosing the dollar amount before and after any planned or actual reduction of a clawback for taxes. In practice, compliance with this subpart of the Restricted Activities Rule will likely impact a large number of advisers as it is common practice to net taxes against an adviser clawback obligation. Regarding the charging or allocating of fees or expenses related to a portfolio investment on a non-pro rata basis, such allocations are restricted unless (i) the allocations are fair and equitable under the circumstances and (ii) the adviser has provided written notice to each investor before charging or allocating such expenses. The SEC provided some insight as to what may considered "fair and equitable," but noted that such determinations will ultimately be made on a case-by-case basis.

Adviser-Led Secondaries Rule

The Adviser-Led Secondaries Rule set forth under Rule 211(h)(2)-2 under the Advisers Act requires that RIAs conducting an adviser-led secondary transaction (as described below) must distribute to investors a fairness opinion or a valuation opinion from an independent opinion provider (i.e., an entity that provides such opinion in its ordinary course of business and is not a related person of the adviser) and a summary of any material business relationships the adviser or any related persons has or has had within the two-year period immediately prior to the issuance date of the opinion. Such opinion and summary must be provided to investors prior to the due date of the election form for the secondary transaction, in a marked change from the proposed rule that stated it must be prior to the closing of the secondary transaction. The furnished opinion must additionally include a written summary of any material business relationships between the adviser or its related persons and the independent opinion provider.

The final rule defines an adviser-led secondary transaction as any transaction initiated by the adviser or any related person that offers the private fund's investors the choice between (i) selling all or a portion of their interests in the private fund or (ii) converting or exchanging all or some of their interest in the private fund for interest in another investment vehicle managed by the same adviser or any related persons. The Adviser-Led Secondaries Rule does not apply to tender offers so long as the investor is not faced with the aforementioned decision, or to a cross-funds trade.

Private Fund Audit Rule

RIAs will now be required to obtain an annual financial audit for each private fund managed subject to the requirements of new Rule 206(4)-10 under the Advisers Act. In part, RIAs will be required to undergo an annual financial statement audit of all private funds advised that satisfy the requirements of the custody rule under the Advisers Act. The audit must be performed by an independent public accountant and must be completed in accordance with generally accepted accounting principles, or principles that are substantially similar with any such material differences reconciled. The results of this audit must be provided to investors within 120 days of the private fund's fiscal year end. The Audit Rule is not expected to impose a large burden on RIAs as many of these entities already provide audited financial statements in compliance with the custody rule. Advisers will no longer be able to opt out of an annual audit by electing to be subject to surprise examinations.

Quarterly Statement Rule

Under new Rule 211(h)(1) to (2) under the Advisers Act, RIAs must prepare and distribute to investors a quarterly statement furnishing certain information regarding fees, expenses and performance for any private fund that it advises. The deadline to furnish such information is within 45 days following the end of each of the first three fiscal quarters, and 90 days following the end of the fiscal year (for funds of funds, these deadlines are 75 days and 120 days, respectively). The Quarterly Statement Rule primarily seeks to address a perceived lack of transparency in private fund fees, expenses and performance. The final rules do not mandate a uniform reporting structure, but there are general format and content requirements for the quarterly statement. Accordingly, among other requirements, the quarterly statement must include fund-level disclosure of adviser compensation and fund fees and expenses, and portfolio investment-level disclosure on compensation and ownership. The disclosure must also report de minimis expenses and such disclosure may not group smaller expenses into broad categories such as "miscellaneous." Quarterly statements may be distributed electronically, but the final rule nonetheless may present challenges for RIAs as they work to meet deadlines for statement preparation.

The timeline to comply with the new Private Fund Rules varies on the specific rule and the size of the adviser. The Preferential Treatment Rule, Adviser-Led Secondaries Rule, and Restricted

Activities Rule have a compliance date of May 13, 2025 for smaller advisers, and November 13, 2024 for larger advisers. The Private Fund Audit Rule and the Quarterly Statement Rule have a compliance date of May 13, 2025 for all covered RIAs. For calculating the size of an adviser for the purposes of these rules, the SEC has indicated that such calculations should be done in the same manner as that done on Form PF by using the total assets under management as of the last day of the adviser's most recently completed fiscal year.

Cybersecurity Disclosure

On July 26, 2023, the SEC adopted final rules to enhance and standardize disclosures regarding cybersecurity risk management, strategy, governance and material cybersecurity risk management. The final rules will require reporting companies to make new disclosures on Current Reports on Form 8-K or Form 6-K (for foreign private issuers) and Annual Reports on Form 10-K or Form 20-F (for foreign private issuers).

Material Cybersecurity Incident Disclosure

The final rules create a new Item 1.05 under Form 8-K that will require a reporting company to disclose any cybersecurity incident that such reporting company determines to be material. If the cybersecurity incident is material, the reporting company must disclose in a Form 8-K the material aspects of the nature, scope and timing of the incident, as well as the material impact or reasonably likely material impact of the incident on the reporting company, including any impact on its financial condition and operations. The deadline to file such Form 8-K event is within four business days following the date that the company determines the cybersecurity incident is material.

The onus will be on the reporting company to investigate and determine whether a cybersecurity incident rises to the level of being material. The final rules provide that the analysis for materiality of cybersecurity incidents is the same as the materiality analysis for other securities laws purposes, and that the analysis should take into account qualitative and quantitative factors to assess materiality.

An interesting aspect of this final rule is that reporting companies must determine whether a cybersecurity incident is material "without unreasonable delay after discovery of the incident." This presumably will provide reporting companies some time to investigate and gather information on the incident without having to rush to make a public disclosure on the matter. The final rules broadly define a cybersecurity incident as "an unauthorized occurrence, or a series of related unauthorized occurrences, on or conducted through a registrant's information systems that jeopardizes the confidentiality, integrity, or availability of a registrant's information systems or any information residing therein." The final rules define "information system" to mean any electronic systems "owned or used by" a company. This means that a reporting company may need to make this disclosure if a third-party service provider's system that they use experiences a cybersecurity incident that impacts the reporting company and rises to the level of materiality.

The SEC recognized that this disclosure, if released too early, could create national security or public safety risks. Thus, the final rules permit reporting companies to delay disclosure of a material cybersecurity incident on Form 8-K for up to 30 days if the U.S. Attorney General notifies the SEC in writing that such disclosure poses a substantial risk to national security or public safety, with the ability to extend such delay to a maximum of 60 days for extraordinary circumstances. Additionally, in very limited circumstances, reporting companies subject to the Federal Communications Commission's notification rule for breaches of customer proprietary network information may delay disclosure of a material cybersecurity incident on Form 8-K for up to seven business days following notification to the U.S. Secret Service and the Federal Bureau of Investigation.

In the event that information that is required to be disclosed under this new Item 1.05 is not determined or available at the time the filing is required, reporting companies must note the missing information in its initial disclosure on Form 8-K and then file an amendment to that Form 8-K within four business days after such information is determined or becomes available.

For foreign private issuers, the final rules amend Form 6-K to require foreign private issuers to make similar disclosure on Form 6-K. However, foreign private issuers will be required to file a Form 6-K to disclose a material cybersecurity incident if the foreign private issuer makes or is required to make public or otherwise discloses such an incident in a foreign jurisdiction to any stock exchange or to stockholders.

Cybersecurity Risk Management, Strategy and Corporate Governance

The final rules also create new Item 106 of Regulation S-K, which will require reporting companies to provide a description in its Form 10-K of its processes, if any, for assessing, identifying and managing material risks from cybersecurity threats in sufficient detail for a reasonable investor to understand. Such disclosure should include, but is not limited to, (i) whether and how any processes have been integrated into the company's over-all risk management system or processes, (ii) whether the company engages assessors, consultants, auditors or other third parties in connection with such processes, (iii) whether the company has processes to oversee and identify risks from cybersecurity threats associated with its use of any third-party service providers and (iv) if applicable, whether any risks from cybersecurity threats, including as a result of any prior cybersecurity incidents, have materially affected or are reasonably likely to materially affect the company, including business strategy, results of operations or financial condition and if so, how. In addition, Item 106 will require reporting companies to describe its board of directors' oversight of risks and management's role and expertise in assessing and managing material risks from cybersecurity threats.

For foreign private issuers, the final rules amend Form 20-F to include the same requirements described above for Item 106.

The final rules became effective on September 5, 2023, however, there is a transition period to comply with such final rules. With respect to the disclosure requirements under Item 1.05 of Form 8-K and in Form 6-K, all reporting companies, other than smaller reporting companies, must begin complying with the new disclosure requirements on December 18, 2023. Smaller reporting companies will be required to begin complying with the new disclosure requirements on June 15, 2024. With respect to the disclosure requirements under Item 106 of Regulation S-K and the comparable requirements in Form 20-F, all reporting companies must provide such disclosure beginning with annual reports for fiscal years ending on or after December 15, 2023. Finally, all reporting companies will be required to tag these disclosures in Inline XBRL beginning one year after initial compliance with the related disclosure requirement.

Investment Company Names

On September 20, 2023, the SEC adopted final rules to modernize Rule 35d-1 under the Investment Company Act of 1940, as amended, the so-called "Names Rule," to alter the nomenclature standards for investment fund names and related notice and disclosure requirements.

First adopted in 2001, the Names Rule prohibits a registered investment company from adopting any words in the name of its fund that the SEC finds may be materially deceptive or misleading to investors. The prior and amended Names Rule specifically calls out certain types of fund names that can be considered materially deceptive or misleading unless certain conditions are satisfied.

As amended, the rule expands the types of names that could be deemed materially misleading or deceptive if a fund does not adopt a policy to invest at least 80% of its assets with an investment focus as the name would suggest. The 80% threshold has remained unchanged from the prior rule, but the final rules have significantly broadened the scope of terms that necessitate compliance with the 80% requirement. For example, words that were previously considered to speak to fund strategy such as "growth" or "value" are now deemed to pertain to characteristics of the nature of investments the fund engages. Additionally, the amended rule will specifically address the proliferation of environmental, social or governance ("ESG") related funds in recent years to require funds that use any terms in its name that suggest either a specific investment focus or provide for tax-exempt distributions must use words that have a plain English meaning or established industry use consistent with such suggestion.

In addition, new disclosures will be required in funds' prospectuses and on Form N-PORT. Funds will be required to provide disclosures to define the terms used in its name as well as the criteria the fund uses to select the investments the term describes. These disclosures may provide some leeway to fund managers as they have the opportunity to reasonably define the terms used, so long as the definitions remain consistent with the plain-language requirements noted above.

These final rules are seemingly in line with the Biden administration's efforts to promote ESG-related initiatives and could combat practices such as "greenwashing," that were addressed in the SEC's adopting press release. The press release pointed out that investor-driven demand for ESG products has resulted in certain investment vehicles that do not provide an underlying investment mix that would be reasonably implied by the product's name.

The final rules will become effective 60 days after publication in the Federal Register. Fund groups having net assets of $1 billion or more will have 24 months to comply with the final rules, and fund groups with net assets of less than $1 billion will have an additional six months, or 30 months, to comply with the final rules.

Proposed Rules

SEC Proposes New Conflicts of Interest Rule for Predictive Analytics Tools and AI

On July 26, 2023, the SEC proposed new rules under the 1934 Act and the Advisers Act that aim to prevent broker-dealers and investment advisers from using predictive data analytics ("PDA") and other technologies, such as artificial intelligence programs, to benefit its own interests over investors' interests. Additionally, the proposed rules would mandate broker-dealers and investment advisers to adopt and implement written policies and procedures reasonably designed to prevent violations of (in the case of investment advisers) or achieve compliance with (in the case of broker-dealers) the new proposed rules. Finally, investment advisers and broker-dealers would be required to maintain books and records in compliance with the proposed rules.

Under the proposed rules, a conflict of interest would typically arise if a firm were to utilize a covered technology in its engagement with an investor, including the solicitation of an investor or in the exercise of discretion over an existing investor's account. Covered technologies, or PDAs, would include many technologies that are presently commonplace such as statistical and valuation tools, as well as more nascent technologies such as artificial intelligence and natural-language models. A broker-dealer or investment adviser would need to assess any current or reasonably foreseeable future utilization of a covered technology by the firm or its affiliated individuals in any interaction with investors. The objective of the proposal is to have covered firms identify any conflicts of interest that arise or may arise in the future when utilizing covered technologies and eliminate or limit the use of such covered technologies that can create such conflicts of interest. Ultimately, the proposed rules would mandate that firms eliminate or counterbalance any covered technology that prioritizes the firm's or its affiliated individuals' interests over those of its investors.

The proposed rules would require any firm engaging in investor interactions with covered technologies to establish written policies and procedures aimed at ensuring compliance with the proposed rules. These policies and procedures would encompass, among other things, a documented description of the process for evaluating the use, or foreseeable potential use, of covered technology in investor interactions and a documented description of the process for addressing such conflicts of interest to ensure that investor interactions prioritize the interests of the investor, not the firm or an affiliated individual.

Additionally, firms would be obligated to create and maintain records related to the requirements outlined in the proposed rules by amending Rules 17a-3 and 17a-4 of the 1934 Act, and Rule 204-2 of the Advisers Act. Such recordkeeping requirements would include, among other things, records of the conflict of interest evaluation (including a list of all covered technologies, the implementation dates, intended versus actual use, and outcomes), disclosures made to investors about the firm's use of covered technologies, and records of any changes or restrictions placed on the implemented technologies.

The proposed rule is likely to garner significant feedback due to the wide scope of potentially covered technologies and the "technology-agnostic" phrasing that would presumably require sweeping internal evaluations of many technologies presently used. Furthermore, the current language of the proposed rule presents ambiguities in its definitions that would potentially create a significant compliance burden absent clarification, as investment advisers and broker-dealers may be tasked with justifying a majority of the technologies routinely used in their day-to-day business. To this point, the SEC specifically sought comment on the proposed scope of the rule, the proposed definition of "investor" and the proposed definition of "investor interaction."

The public comment period for the proposed rules closed on October 10, 2023.

Exemption for Internet Investment Advisers

On July 26, 2023, the SEC proposed changes to Rule 203A-2(e) of the Advisers Act (the "Internet Adviser Exemption"). The proposed rule would modernize the language within to reflect the evolution in technology and change in current practices in the investment advisory industry since the Internet Adviser Exemption was first adopted in 2002.

The Internet Adviser Exemption is among a series of exemptions established by the SEC to allow investment advisers to register with the SEC even if they don't normally fulfill the criteria for federal registration. Under the current rule, investment advisers that provide investment advice solely through the internet and do not maintain physical locations are not required to register with the SEC so long as they comply with recordkeeping requirements and manage less than $25 million in assets and render advice to fewer than 15 clients in the preceding 12 months. The proposed rule would remove the aforementioned 15-client threshold and seek to clarify that internet investment advisers seeking to rely on the exemption must have a properly operating website and/or mobile application at all times. Additionally, such advisers must make a representation on Form ADV that they are relying on the exemption and have an operational website.

The public comment period for the proposed rule changes to the Internet Adviser Exemption closed on October 2, 2023.

Safeguarding Advisory Client Assets

On August 23, 2023, the SEC reopened the comment period for the Safeguarding Advisory Client Assets proposal that was initially proposed on February 15, 2023. The proposed rules would redesignate and amend the current custody rule under the Advisors Act. In light of the adoption of the Private Fund Advisers Rule described herein, the SEC believes that reopening the comment period, which originally closed on May 8, 2023, will allow interested persons additional time to assess the proposed rules to the current custody rule's audit provision.

The public comment period for the proposed rule closed on October 30, 2023.

The District of Columbia Circuit Court Vacated SEC Order Denying the Public Listing of Bitcoin Exchange-Traded Product

On August 29, 2023, the United States Court of Appeals for the District of Columbia Circuit considered whether a bitcoin exchange-traded product ("ETP") satisfied the significant market test and therefore should have been approved and listed by the SEC. The D.C. Circuit rejected the SEC's findings and held that a bitcoin ETP is "materially similar" to previously approved bitcoin futures ETPs using the significant market test and vacated the SEC's order. While the D.C. Circuit's decision was informed by administrative law in that the court found the SEC acted arbitrarily and capriciously by failing to adequately differentiate bitcoin ETPs from bitcoin futures ETPs, the ruling's effect on securities law is broader. Moreover, the court acted in an unprecedented manner by creating a new asset class, the first since the invention of the exchange-traded fund, forcing the SEC to reconsider its treatment of bitcoin securities without any clear instruction moving forward.

Plaintiff Grayscale Investments, LLC ("Grayscale") petitioned for review of a SEC order that denied Grayscale's application to convert its trust, the Grayscale Bitcoin Trust, into the first ever spot bitcoin ETP. Under Section 16 of the 1934 Act, to list a new product for trading, the SEC must approve of a securities exchange's proposed rule change. In 2022, the SEC approved the trading of two bitcoin futures ETPs, the Teucrium Bitcoin Futures Fund in April 2022 and the Valkyrie XBTO Bitcoin Futures Fund in May 2022. However, the SEC has never approved a bitcoin ETP traded in a spot, rather than a futures, market. After a period of public notice and comment in which thousands of public comments supported listing Grayscale, the SEC rejected Grayscale's application. In Grayscale's petition to the D.C. Circuit, it claimed its bitcoin ETP was materially similar to approved bitcoin futures ETPs under the significant market test and that the SEC acted in an arbitrary and capricious manner by rejecting the listing of Grayscale.

The significant market test assesses whether a listing in a surveilled market will result in market manipulation. The D.C. Circuit held that the trading of Grayscale would not reasonably produce market manipulation. The first prong of the test looks to whether there is reasonable likelihood someone "attempting to manipulate" a security "would . . . have to trade on [the related] market to successfully manipulate" it. The second prong examines whether trading in the security would have "the predominant influence on prices" in the market. Determinative in the D.C. Circuit's analysis was the "obvious financial and mathematical relationship" between the spot market and the futures market. Further, bitcoin and bitcoin futures are closely correlated, and existing surveillance sharing agreements were sufficient to detect fraud or manipulation in the bitcoin spot market. Additionally, given that Grayscale holds only 3.4 percent of outstanding bitcoin, the D.C. Circuit found the SEC failed to prove Grayscale could dominate bitcoin spot market prices. Manipulation in the spot market, therefore, should be "more difficult, not less" than in the futures market. As a result, the SEC's contrary finding without sufficient and satisfactory evidence was held arbitrary and capricious decision-making.

Grayscale Invs. LLC v. SEC, case no. 22-1142, in the U.S. Court of Appeals for the District of Columbia Circuit.

The Second Circuit Reversed the District Court's Class Certification of Goldman Shareholders Upon Third Glance

On August 10, 2023, after a decade of ongoing litigation, the United States Court of Appeals for the Second Circuit reversed the district court's decision and held that Goldman shareholders could not be certified as a class pursuant to Federal Rule of Civil Procedure 23(b)(3). The court contemplated whether the district court properly applied the Supreme Court's "mismatch framework" to its analysis of Goldman's alleged misrepresentations and considered the lower court's application of certain evidence. Ultimately, the Second Circuit held that the district court erred in certifying the shareholder class because Goldman had in fact rebutted the *Basic* presumption by a preponderance of the evidence that the alleged misrepresentations did not alter its stock price, seemingly marking the end to an arduous legal battle.

In 2011, individual and institutional shareholders of Goldman Sachs Group, Inc. brought a class action lawsuit, accusing Goldman of various misrepresentations leading up to the financial crisis in 2008 in violation of Section 10(b) of the 1934 Act and Rule 10b-5 promulgated thereunder. Further, they alleged Goldman Sachs misrepresented its business practices and management of conflicts internally and publicly, and as such, directly caused the artificial inflation of the bank's stock price. At first, the district court denied Goldman's motion to dismiss and certified the class. Upon appeal, the Second Circuit vacated the district court's certification and remanded. *Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc. (ATRS I)*, 879 F.3d 474 (2d Cir. 2018). On remand, the district court certified the class yet again and upon interlocutory appeal, the Second Circuit affirmed. *Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc. (ATRS II)*, 955 F.3d 254 (2d Cir. 2020), *cert. granted*, 141 S. Ct. 950 (2020), *and vacated and remanded*, 141 S. Ct. 1951 (2021). The Supreme Court then granted Goldman's writ for certiorari and vacated the Second Circuit's judgment, remanding for consistent proceedings. The Second Circuit, upon remand from the Supreme Court, vacated the district court's class certification and remanded to the lower court. *Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc. (ATRS III)*, 11 F.4th 138 (2d Cir. 2021). Again, the district court certified the class.

Before the court for a third time, the Second Circuit held in August 2023 that no sufficient causal link existed between Goldman's alleged misrepresentations and its subsequent corrective public disclosures so as to impact the decline in the Goldman stock price in 2008. As such, Goldman shareholders were unable to be certified as a class. Relying partially on the Supreme Court's mismatch theory, the Second Circuit found that to prove causality, a considerable gap between alleged misrepresentations and resulting misconduct cannot exist. A mere association is not enough. Rather, a showing that the alleged misrepresentation *maintained* the ensuing price inflation is required. As a result, *Arkansas Teacher Retirement System* makes it harder for plaintiffs who bring securities fraud class actions that allege corporate misrepresentation as a cause of price inflation to be successful and consequently strengthens a defense to such an action.

Ark. Tchr. Ret. Sys. v. Goldman Sachs, case no. 22-484, in the U.S. Court of Appeals for the Second Circuit.