D.C. Circuit Rejects "Co-Conspirator Theory of Venue" in Securities Litigation

On June 28, 2011, the United States Court of Appeals for the District of Columbia Circuit held in *Securities and Exchange Commission v. Charles Johnson, Jr., et. al.*[1] that the "co-conspirator theory of venue" cannot be used to support venue under 15 U.S.C. § 78aa, the Private Securities Litigation Reform Act of 1995 ("PSLRA").[2] The court stated that: "at least one statutory basis for venue, no matter how broadly or narrowly that particular requirement might be construed, must have occurred in the chosen forum."[3]

In doing so, the D.C. Circuit both clarified its stance on where venue may lie in securities violations suits post-*Central Bank of Denver v. First Interstate Bank of Denver*[4] and created a potential circuit split between itself and the 2nd, 5th and 9th Circuits.

I. Alleged Facts and Procedural History

Chris Benyo served as Senior Vice President for Marketing and Network Development for PurchasePro, a software company, from 2000 to 2001. During that time, PurchasePro recorded sham transactions designed to inflate its reported revenue. One of these sham transactions portrayed PurchasePro as a subcontractor under a pre-existing agreement between America Online, Inc. (AOL) and AuctioNet, Inc. The company's attorneys and auditors had relied upon a "Statement of Work" dated February 5, 2001 in their work for PurchasePro.

In January 2005, the SEC filed a civil enforcement action in the District of Columbia in which it alleged that Benyo had "worked on drafting or caused others to draft" the Statement of Work regarding the AuctioNet, Inc. deal.[5] The SEC alleged Benyo had aided and abetted in PurchasePro's fraud, and was therefore in violation of 15 U.S.C. § 78t(e).

In the district court, Benyo argued that the SEC's allegation showed he had acted only in Nevada and that no "act or transaction constituting the violation[s]" had occurred in the District of Columbia.[6] He argued venue in the District of Columbia was impermissible under 15 U.S.C. § 78aa. In response, the SEC argued that the "co-conspirator venue theory" permits venue in a district where a co-conspirator has acted. The SEC pegged the theory to PurchasePro's filing of periodic reports with the SEC in the District of Columbia. The civil jury in the District of Columbia found Benyo liable for aiding and abetting. Benyo was fined $35,000 and barred from serving as officer or director of a publicly traded company for five years.

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1 *S.E.C.* v. *Johnson*, No. 09-5399, slip op. (D.C. Cir. June 28, 2011), available at http://www.cadc.uscourts.gov/internet/opinions.nsf/745B8D234FE99F6B852578BD005042E4/$file/09-5399-1315523.pdf.

2 *Id.* at 10.

3 *Id.* at 9.

4 511 U.S. 164 (1994).

5 *S.E.C.* v. *Johnson*, No. 09-5399, slip op at 4.

6 *Id*. at 5.

II. Co-conspirator Theory of Venue

The co-conspirator theory of venue has some support in circuit court case law, particularly in securities litigation. As articulated by the Court of Appeals for the Ninth Circuit: "Under the co-conspirator venue theory, where an action is brought against multiple defendants alleging a common scheme of acts or transactions in violation of securities statutes, so long as venue is established for any of the defendants in the forum district, venue is proper as to all defendants."[7] The co-conspirator theory of venue has proven popular, and indeed, has been espoused in the past by the District Court of the District of Columbia.[8]

Courts have invariably justified the theory under the policy of avoiding multiple proceedings and litigating related claims in the same venue.[9] This policy makes for efficient pretrial discovery, saves time and expense for parties and witnesses, and minimizes the risk of inconsistent results.[10] Some courts have been willing to overlook extreme inconvenience to a defendant resulting from the application of the theory.[11] The theory has even been applied in cases where the defendant had no apparent contact whatsoever with the forum.[12]

III. S.E.C. v. Johnson

15 U.S.C. § 78aa provides, in relevant part:

> "Any suit or action to enforce any liability or duty created by this chapter or rules and regulations thereunder, or to enjoin any violation of such chapter or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business . . . ."[13]

The D.C. Circuit's ruling in *S.E.C. v. Johnson* states that "§ 78aa by its terms forecloses the use of the co-conspirator theory of venue . . . ."[14] Judge Ginsburg, writing for the court, noted that the filing of the Form 10-Q (the jurisdictional link to the D.C. Circuit) is not a "violation attributed to Benyo . . . as § 78aa requires . . . "[15] because the revenue item Benyo allegedly falsified did not appear in the 10-Q.

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7 *SIPC* v. *Vigman*, 764 F2.d 1309, 1317 (9th Cir. 1985).

8 *S.E.C.* v. *National Student Marketing Corp*., 360 F. Supp. 284, 291-292 (D.D.C. 1973).

9 *SIPC* v. *Vigman*, 764 F.2d at 1318 ("The strong policy favoring the litigation of related claims in the same forum supports the application of a co-conspirator venue theory in actions based upon violations of federal securities statutes.").

10 *Wyndham Assocs*. v. *Bintliff*, 398 F.2d 614, 619 (2d Cir. 1968).

11 *SIPC* v. *Vigman*, 764 F.2d at 1318 ("the inconvenience of requiring one defendant in a multi-defendant action to litigate in a distant forum is greatly outweighed by the interest of judicial economy and bringing together in one lawsuit, all related claims and alternative theories").

12 *Id*. at 1317 ("It does not appear from the briefs filed in this case, or from the record below, that [the defendants] had any actual contacts with the forum ... or that they performed any act within the forum in violation of the Act").

13 15 U.S.C. § 78aa.

14 *S.E.C.* v. *Johnson*, No. 09-5399, slip op. at 8.

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Judge Ginsburg relied in part on *Central Bank of Denver*, which "strongly implied there could be no cause of action for any form of 'secondary liability' for fraud that does not require proof of each of the elements of the primary violation . . . ."[16] Judge Ginsburg notes that "Congress enacted 15 U.S.C. § 78t(e) to give the SEC express authority to pursue a person who has aided and abetted a securities fraud."[17] However, § 78t(e) gave rise to aiding and abetting liability; it did not do the same for conspiracy liability. Therefore, "an allegation is not by itself -- that is, without proof of . . . actual participation in a fraud -- a sufficient basis for liability under *Central Bank of Denver* and therefore cannot be a sufficient basis for venue."[18] Since the statute does not provide for liability for conspiracy, there is no statutory basis for venue, rendering the co-conspirator theory of venue impermissible in such cases.[19]

IV. Impact of the Decision

At least three circuits have previously applied the co-conspirator theory of venue in multi-defendant securities litigation.[20] However, these cases were all decided before the Supreme Court's decision in *Central Bank of Denver*. It remains to be seen how these circuits would rule if faced with the question today. If they continue to apply the co-conspirator theory of venue, a circuit split would arise.

Under § 78aa, no venue can stand except as provided in the statute. As the D.C. Circuit held, to entertain the co-conspirator theory of venue in such litigation "add[s] a gloss to the operative language of the statute quite different from its commonly accepted meaning."[21]

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Jon Mark at 212.701.3100 or jmark@cahill.com; John Schuster at 212.701.3323 or jschuster@cahill.com.

16 *Id.* at 7 (citing *Central Bank of Denver*, 511 U.S. at 180, 184).

17 *Id.*

18 *Id.*

19 *Id.* at 8 (citing *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 199 (1976)).

20 *Id.* (citing *SIPC* v. *Vigman*, 764 F.2d at 1317; *Hilgeman* v. *Nat'l Ins. Co. of Am.*, 547 F.2d 298, 302 & n.12 (5th Cir. 1977); *Wyndham Assocs.* v. *Bintliff*, 398 F.2d at 620).

21 *Id.* at 8 (quoting *Ernst & Ernst* v. *Hochfelder*, 425 U.S. at 199).