

“I Won’t Let You Lose Money” Does Not Make a Federal Securities Fraud Case

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In federal securities fraud cases, the Ninth Circuit will enforce the pleading requirements for such claims, and dismiss cases brought by plaintiffs who – however sympathetic – fail to meet those requirements, as shown in the Ninth Circuit’s October 2007 decision concerning *Foster v. Wilson*.

In that matter, plaintiffs’ first amended complaint alleged they had been defrauded in connection with a \$150,000 purchase of stock, because the defendant had allegedly used the plaintiffs’ money to buy stock for himself, rather than for plaintiffs.

Specifically, plaintiffs alleged that:

- Plaintiffs provided defendant Wilson, a “consultant,” with a total of \$150,000 for the purchase of shares in a company called Car Rental Direct (“CRD”)
- Wilson had told plaintiffs that they should not buy shares of CRD through a broker, but instead should buy shares through him because of his “special relationship” with CRD
- Further, Wilson convinced plaintiffs to buy the shares through him, by promising plaintiffs that “I won’t let you lose money on this deal.”
- Plaintiffs provided the \$150,000 to Wilson, but Wilson did not provide the shares to plaintiffs
- Instead, Wilson allegedly used the majority of the investment to purchase shares on his own behalf and on behalf of his company

CRD thereafter went bankrupt.

Plaintiffs alleged claims for federal securities law fraud, California securities law fraud, common law deceit and breach of contract.

The Ninth Circuit affirmed the dismissal of the matter, noting two requirements of pleading a federal securities fraud claim:

- “Federal securities fraud, like its common law fraud ancestor, requires knowingly making a false statement with intent to deceive, reliance upon which injures the victim.”
- The Private Securities Litigation Reform Act requires plaintiffs to “state with particularity both the facts constituting the alleged violation, and the fact evidencing scienter, the defendant’s intention ‘to deceive, manipulate, or defraud.’ “

In the federal securities claim, the plaintiffs had not alleged that the defendant made the representations with the intent to deceive.

The Ninth Circuit concluded that plaintiffs were not basing the federal securities claim on intentional misrepresentation, because plaintiffs had alleged the intent to deceive in their state law claims, and because plaintiffs had been given the opportunity to amend and chose not to do so.

The Ninth Circuit termed this a “fatal deficiency,” going far beyond a failure to satisfy the Private Securities Litigation Reform Act.

Absent an allegation that the defendant had intended not to purchase the stock when he took the payment, the “failure to carry out a promise made in connection with a securities transaction” amounted to, at most, a breach of contract, not a claim for securities fraud under Section 10(b) of the Securities Exchange Act of 1934.

In short, “he took my money, and didn’t do what he promised” does not create a federal securities fraud case.