

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Gordon Gamm v. Sanderson Farms, Inc.

No. 18-0284-cv, United States Court of Appeals for the Second Circuit (December 10, 2019)

SUMMARY

In a securities fraud class action under Section 10(b) and Rule 10b-5, the Second Circuit held that when a complaint alleges that statements were rendered false or misleading through the nondisclosure of illegal activity (here, an antitrust conspiracy), the facts of those underlying illegal acts must be pleaded with particularity under Rule 9(b) and the PSLRA. The court affirmed dismissal because plaintiffs failed to allege the basic elements of an antitrust conspiracy—such as an agreement, restraint of trade, or effect on interstate commerce—with sufficient particularized facts, relying instead on conclusory allegations of parallel conduct and opportunities to conspire. The decision clarifies that the heightened pleading standard applies to predicate illegal conduct that forms the basis of the securities fraud claim.

CASE DETAILS

COURT	United States Court of Appeals for the Second Circuit
WRITING FOR THE COURT	Ralph K. Winter; John M. Walker Jr.; Christopher F. Droney
JURISDICTION	Federal
DECIDED	December 10, 2019
DOCKET	18-0284-cv
DISPOSITION	affirmed
PROCEDURAL POSTURE	Appeal from the United States District Court for the Southern District of New York (Richard M. Berman, Judge) granting appellees' motion to dismiss appellants' complaint for failure to plead securities fraud with particularity.
STANDARD OF REVIEW	de novo
PRECEDENTIAL VALUE	Published
PARTIES	Gordon Gamm and Don Pritchard v. Sanderson Farms, Inc., Joe F. Sanderson, Jr., Michael D. Cockrell, Lampkin Butts

TOPICS

securities fraud

pleadings

motions to dismiss

standard of review

appellate procedure

class actions

civil procedure

PRACTICE AREAS

Securities Litigation

Antitrust

QUESTIONS PRESENTED

1. Whether, in a securities fraud action based on the nondisclosure of illegal activity, the facts of the underlying illegal acts must be pleaded with particularity under Rule 9(b) and the PSLRA.
2. Whether appellants sufficiently pleaded the underlying antitrust conspiracy with particularity.

HOLDINGS

1. When a securities fraud complaint claims that statements were rendered false or misleading through the nondisclosure of illegal activity, the facts of the underlying illegal acts must be pleaded with particularity in accordance with Rule 9(b) and the PSLRA.

KEY QUOTATIONS

“For the foregoing reasons, we hold that when a securities fraud complaint claims that statements were rendered false or misleading through the nondisclosure of illegal activity, the facts of the underlying illegal acts must be pleaded with particularity in accordance with the requirements of Rule 9 and the PSLRA. Because appellants have failed to meet this pleading standard for the underlying allegations of illegal antitrust conspiracy, their complaint was deficient. Accordingly, we affirm.” (28)

“The pleadings are typically subject to Federal Rule of Civil Procedure 8, requiring a ‘short and plain statement of the claim.’ This is understood to require ‘more than an unadorned, the defendant-unlawfully-harmed-me accusation’ but does not require ‘detailed factual allegations.’ Iqbal, 556 U.S. at 678.” (16)

“Under Rule 9(b) and the PSLRA, the circumstances of a fraud include ‘the basis’ for that contention. First, in this matter, the alleged fraud and the facts of the alleged anticompetitive conspiracy are inseparable and the clear language of the statute requires that underlying facts be pleaded with particularity.” (17-18)

“Applying that standard here, appellants were required to plead with particularity sufficient facts to support their contention that Sanderson Farms’ financial disclosures were misleading. This necessarily requires that facts of the underlying anticompetitive conduct be pleaded with particularity.” (23-24)

FACTUAL BACKGROUND

Sanderson Farms is a poultry processing company. The chicken industry is vertically integrated and has an inelastic market, historically marked by boom-and-bust cycles. Appellants alleged that from 2008, Sanderson Farms and other large chicken producers colluded to inflate chicken prices by coordinating supply reductions and manipulating the Georgia Dock price index. They alleged that Sanderson Farms destroyed breeder hens and eggs, exported eggs, and dumped excess inventories in foreign markets. They also alleged that the conspiracy

was facilitated through Agri Stats data sharing and industry meetings. The nondisclosure of this alleged conspiracy rendered Sanderson Farms' SEC filings and public statements false and misleading.

PROCEDURAL HISTORY

Appellants filed a putative class action in the Southern District of New York, were appointed lead plaintiffs, and filed an amended complaint. After pre-motion letters, they filed a second amended complaint. The district court granted appellees' motion to dismiss with prejudice, concluding that appellants failed to support their allegation of a chicken supply reduction conspiracy with particularized facts. This appeal followed.

DISPOSITION

affirmed

CASES CITED

- Novak v. Kasaks, 216 F.3d 300 (2d Cir. 2000)
- Eastman Kodak Co. v. Henry Bath LLC, 936 F.3d 86 (2d Cir. 2019)
- Ashcroft v. Iqbal, 556 U.S. 662 (2009)
- Bell Atl. Corp. v. Twombly, 550 U.S. 544 (2007)
- S.E.C. v. Pimpcos Advisors Fund Mgmt., LLC, 341 F. Supp. 2d 454 (S.D.N.Y. 2004)
- Kramer v. Time Warner, Inc., 937 F.2d 767 (2d Cir. 1991)
- Mills v. Polar Molecular Corp., 12 F.3d 1170 (2d Cir. 1993)
- ATSI Commc'ns, Inc. v. Shaar Fund, Ltd., 493 F.3d 87 (2d Cir. 2007)
- In re IBM Corp. Sec. Litig., 163 F.3d 102 (2d Cir. 1998)
- In re Axis Capital Holdings Ltd. Sec. Litig., 456 F. Supp. 2d 576 (S.D.N.Y. 2006)
- In re Banco Bradesco S.A. Sec. Litig., 277 F. Supp. 3d 600 (S.D.N.Y. 2017)
- Hogan v. Pilgrim's Pride Corporation, 2018 WL 1316979 (D. Col. Mar. 14, 2018)
- In re Tyson Foods, Inc. Sec. Litig., 275 F. Supp. 3d 970 (W.D. Ark. 2017)
- Maric v. St. Agnes Hosp. Corp., 65 F.3d 310 (2d Cir. 1995)
- Mayor and City Council of Baltimore v. Citigroup, Inc., 709 F.3d 129 (2d Cir. 2013)
- Todd v. Exxon Corp., 275 F.3d 191 (2d Cir. 2001)
- Twombly v. Bell Atlantic Corp., 425 F.3d 99 (2d Cir. 2005)
- Capital Imaging Associates, P.C. v. Mohawk Valley Medical Associates, Inc., 996 F.2d 537 (2d Cir. 1993)
- AD/SAT, Div. of Skylight, Inc. v. Associated Press, 181 F.3d 216 (2d Cir. 1999)
- Chicago Title & Trust Co. v. Fox Theatres Corp., 182 F. Supp. 18 (S.D.N.Y. 1960)
- Decker v. Massey-Ferguson, Ltd., 681 F.2d 111 (2d Cir. 1982)
- In re Corning Sec. Litig., 01 Civ. 6580(CJS), 2004 WL 1056063 (W.D.N.Y. Apr. 9, 2004)
- In re Hudson Techs. Sec. Litig., 98 Civ. 1616(JGK), 1999 WL 767418 (S.D.N.Y. Sept. 28, 1999)

OPINION

PER CURIAM.

18-0284-cv Gordon Gamm, et al. v. Sanderson Farms, Inc., et al. United States Court of Appeals for the Second Circuit August Term, 2018 (Argued: August 31, 2018 Decided: December 10, 2019) Docket No. 18-0284-cv _____ GORDON GAMM, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED, DON PRITCHARD, Plaintiffs – Appellants, v. SANDERSON FARMS, INC., JOE F. SANDERSON, JR., MICHAEL D. COCKRELL, LAMPKIN BUTTS, Defendants – Appellees. _____ ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK Before: WINTER, WALKER, AND DRONEY, Circuit Judges.

Appeal from a judgment of the United States District Court for the Southern District of New York (Richard M. Berman, Judge), granting appellees’ motion to dismiss appellants’ complaint for failure to plead, with the requisite particularity, securities fraud under Section 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5.

The complaint alleged that, as a predicate for appellants’ securities fraud claim, appellees had engaged in an illegal antitrust conspiracy, the nondisclosure of which rendered various statements and SEC filings false and misleading.

The law is well established that a party, when making securities fraud allegations on information and belief, must plead material misstatements and omissions with particularity. We clarify that if statements were rendered false or misleading through the nondisclosure of illegal activity, the facts of those underlying illegal acts must also be pleaded with particularity.

Because appellants have failed to allege the details of the underlying antitrust conspiracy with particularity, the judgment of the district court is AFFIRMED. TAMAR A. WEINREB (Marc I. Gross, Jeremy A. Lieberman, Pomerantz LLP, New York, NY, on the brief) for Plaintiffs-Appellants. JOSHUA Z. RABINOVITZ (Robert J. Kopecky, Nathaniel J. Kritzer, Stacy Pepper, Kirkland & Ellis LLP, Chicago, IL and New York, NY, on the brief) for Defendants-Appellees.

WINTER, Circuit Judge: 1 Gordon Gamm and Don Pritchard (“appellants”) appeal from the district 2 court’s dismissal of their complaint under Fed. R. Civ. P. 12(b)(6). The complaint 3 alleged as a basis for a securities fraud class action suit, that appellees, producers 4 of chicken, engaged in an illegal antitrust conspiracy, the nondisclosure of which 5 rendered various SEC filings false and misleading under Section 10(b) of the 2 1 Securities Exchange Act of 1934 (“the Exchange Act”) and Rule 10b-5 2 promulgated thereunder.¹ The district court dismissed, with prejudice, 3 appellants’ second amended complaint pursuant to Fed.

R. Civ. P. 12(b)(6) for 4 failure to plead with sufficient particularity facts of the underlying antitrust 5 conspiracy. This appeal followed. 6 In light of the Private Securities Litigation Reform Act (“PSLRA”) and 7 binding precedent of the Second Circuit, we hold that the district court was

8 correct in its dismissal. It has long been recognized that private plaintiffs in 9 securities fraud actions must plead material misstatements and omissions with 10 particularity when making allegations on information and belief.

Novak v. 11 Kasaks, 216 F.3d 300, 313-14 (2d Cir. 2000). We further clarify that, when a 12 complaint claims that statements were rendered false or misleading through the 13 nondisclosure of illegal activity, the facts of those underlying illegal acts must 14 also be pleaded with particularity.

Because appellants have failed to meet this 15 pleading standard for the underlying allegations of illegal antitrust conspiracy, 1 Appellants also brought a claim for violation of Section 20(a) of the Exchange Act against appellees for control person liability, which depends on there first being a primary violation of Section 10(b). 3 1 we affirm the district court.

We do not reach the issue of scienter or reliance as 2 alternate grounds for affirmance. 3 BACKGROUND 4 In assessing a motion to dismiss, a court must view the evidence – and 5 interpret any allegations – in the light most favorable to the plaintiffs, and it must 6 draw reasonable inferences in plaintiffs’ favor. See Eastman Kodak Co. v. Henry 7 Bath LLC, 936 F.3d 86 (2d Cir.

2019). 8 Appellants Gordon Gamm and Don Pritchard acquired shares of 9 Sanderson Farms, Inc. (“Sanderson Farms”) between December 17, 2013 and 10 November 17, 2016, the “Class Period” alleged in the relevant complaint. 11 Appellee Sanderson Farms is a fully integrated poultry processing 12 company engaged in the production, processing, marketing, and distribution of 13 fresh and frozen chicken and other prepared food items.

Appellees Joe F. 14 Sanderson Jr., Michael Cockrell, and Lampkin Butts serve as the company’s Chief 15 Executive Officer, Chief Financial Officer, and Chief Operations Officer, 16 respectively. 4 1 The chicken2 industry is vertically integrated in that a relevant company 2 tends to own or control every aspect of the breeding, hatching, feeding, basic 3 processing, and selling of chicken.

There are high barriers to market entry: A 4 new entrant faces significant start-up costs and lengthy periods of regulatory 5 approval. 6 In addition, the market for chicken is inelastic. When chicken prices go up, 7 consumers’ buying habits remain about the same. When prices go down, 8 consumers’ buying habits also do not change.

Therefore, industry-wide profits 9 are driven by the price of chicken, rather than by increased or decreased market 10 demand. 11 Because of the inelastic market, the chicken industry has historically been 12 marked by “boom and bust cycles” in which producers increase chicken 13 production in response to rising prices, causing an oversupply in the market. 14 The oversupply of chicken, along with stable demand, then forces down the 2 The industry term for the chicken at

issue in this case is “broilers,” which is ready-to-cook chicken available at grocery stores, making up “approximately 98% of all chicken meat sold in the United States.” (JA 130 ¶ 32).

For simplicity, this opinion refers to “broilers” as “chicken.” 5 1 market price. Chicken becomes less profitable and producers must cut supply 2 until the price eventually rises again. 3 Appellants explain that this cyclical market pattern changed, beginning in 4 2008, when Sanderson Farms and several other large chicken producers began 5 colluding in an anticompetitive conspiracy to inflate the price of chicken by 6 coordinating supply reductions and manipulating a chicken price index.

7 The crux of the alleged conspiracy was that, to defeat the natural “boom- 8 and-bust” cycle of chicken prices, producers all agreed to keep their supply low 9 while chicken prices were high, so that they would all enjoy the high price of 10 chicken. 11 Sanderson Farms accomplished its supply reductions by destroying 12 breeder hens and eggs, exporting eggs from the U.S. starting in 2013, and 13 “dumping” excess chicken inventories in foreign markets where they sold for a 14 fraction of the U.S. price.

15 Furthermore, Sanderson Farms and its competitors were able to monitor 16 one another’s reductions, and ensure that all producers maintained low supply 17 through the use of Agri Stats, Inc., a private company that generates chicken 18 industry data reports. Producers provide Agri Stats with detailed data about 6 1 their operations through actual sales invoices.

Agri Stats then generates detailed 2 reports, including in them data on weighted average price, top third average, and 3 bottom third average; on volume traded on a daily, weekly, and monthly basis; 4 on supply and sales volume by detailed product type and form; and on pricing 5 information for whole and cut-up chickens.

Although Agri Stats purports to 6 maintain the confidentiality and anonymity of individual companies in their 7 reports, the reports are detailed enough that a reasonably informed producer 8 could discern the identity of competitors. 9 Sanderson Farms allegedly planned the antitrust conspiracy with its 10 competitors during industry meetings and conferences, including those of the 11 National Chicken Council, of which appellees and its co-conspirators were 12 members.

The conspiracy was also facilitated at investor conferences organized 13 by Wall Street analysts and attended by Sanderson Farms and its competitors 14 and through competitor plant tours. 15 Relatedly, Sanderson Farms and its competitors allegedly manipulated 16 poultry prices by colluding to inflate the price of chicken reflected in an index 17 referred to as the Georgia Dock.

Chicken prices are reported by three entities: 18 Urner Barry, the United States Department of Agriculture (“USDA”), and the 7 1 Georgia Department of Agriculture’s (“GDA”) Georgia Dock. The USDA and 2 Urner Barry’s indices are based upon a system of double verification, which 3 includes telephonic and written surveys of chicken producers as well as 4 verification of prices reported to chicken purchasers such as brokers and 5 customers.

However, no such verification process existed for the Georgia Dock. 6 This, appellants argue, rendered the Georgia Dock susceptible to manipulation. 7 Additionally, in order to manipulate the Georgia Dock, appellees would 8 have had to work in coordination with their competitors. This is so because the 9 Georgia Dock has a rule whereby a preliminary dock price calculation is made 10 based on the single price quotation from each company.

Then, any company 11 whose quote is more than one cent above or below the initial dock price 12 calculation will not be included in the dock price for that week. Its quote is taken 13 out and the dock price is recalculated without it.

The purpose of this rule is to 14 prevent one company from having the ability to greatly influence the price. 15 Beginning in January 2015, the Georgia Dock price began to depart 16 significantly from the pricing reflected by the other indices, which appellants 17 attribute to Sanderson Farms and its competitors collectively submitting similar, 18 artificially high prices to the Georgia Dock.

In August 2016, the USDA stopped 8 1 using the Georgia Dock index, and the GDA suspended the index permanently in 2 December 2016. 3 Appellants claim that the failure to disclose these collusive acts rendered 4 various statements issued by Sanderson Farms during the class period false and 5 misleading. 6 Specifically, in its Annual Report on Form 10-K filed with the Securities 7 and Exchange Commission (“SEC”) on December 17, 2013, Sanderson Farms 8 stated “The Registrant [Sanderson Farms] is subject to significant competition 9 from regional and national firms in all markets in which it competes.” SAC ¶ 82.

10 “The increase in cash flows from operating activities of \$47.0 million resulted 11 primarily from improved market prices for poultry products during fiscal 2013 as 12 compared to fiscal 2012, and a \$27.2 million decrease in live chicken, feed, and 13 egg inventories attributable to the declining costs of feed grains experienced as 14 we moved through the fourth quarter of fiscal 2013.” SAC ¶ 84.

15 In its Quarterly Report on Form 10-Q filed with the SEC on February 25, 16 2014, Sanderson Farms represented that “The Company competes with regional 17 and national firms, some of which have greater financial and marketing resources 18 than the Company.” SAC ¶ 87.

In an accompanying press release, appellees 9 1 stated that Sanderson Farms “competes with regional and national firms.” SAC ¶ 2 88. 3 Sanderson Farms made similar disclosures on May 29, 2014, and every 4 subsequent quarterly disclosure through August 25, 2016. These statements were 5 materially false and misleading, according to appellants, because “Sanderson 6 Farms did not compete with its industry peers but instead engaged in collusive 7 conduct, facilitated by their extensive information sharing via Agri Stats, to prop 8 up broiler prices through systemic reductions of the broiler supply, destruction 9 of eggs, and manipulation of poultry prices reflected on the Georgia Dock index.” 10 SAC ¶ 138.

Appellants further claimed that the undisclosed anticompetitive conduct “rendered Sanderson Farms vulnerable to litigation and regulatory scrutiny for potential violations of the federal antitrust laws as well as reputational damage.” *Id.* In the fall of 2016, several antitrust complaints were filed against U.S. chicken producers, including the following: On September 2, 2016, Maplevale Farms, Inc. filed its antitrust class action complaint (the “Maplevale Complaint”) in the Northern District of Illinois against Sanderson Farms and several other poultry producers, alleging that they had conspired since 2008 to manipulate the prices of chicken in violation of the Sherman Antitrust Act, 15 U.S.C. §§ 1-7 (the “Sherman Act”).

On October 4, 2016, a group of individual consumers filed an antitrust class action complaint in the Northern District of Illinois against Sanderson Farms and several of its competitors, alleging violations of the Sherman Act (the “Monahan Complaint”). Following the filing of the Monahan Complaint, Sanderson Farms’ share price fell \$3.98 or 4.14%, to close at \$92.21 on October 4, 2016.

On October 7, 2016, Pivotal Research downgraded Tyson from “Hold” to “Sell” citing the “powerfully convincing” allegations of price manipulation by the defendants in the Maplevale Complaint. Soon after, Sanderson Farms’ share price fell \$4.03 or 4.32%, to close at \$89.15 on October 7, 2016. On November 3, 2016, the New York Times published an article entitled “You Might be Paying Too Much for Your Chicken,” which revealed that the United States Department of Agriculture had started an inquiry into the Georgia Dock index.

The article pointed out that the Georgia Dock price for chicken differed significantly from the prices provided in similar indices. Following this news, Sanderson Farm stock fell \$6.31, or almost 7%. On November 17, 2016, the Washington Post published an article entitled, “If you thought you were paying fair prices for chicken at the supermarket, think again.” The article revealed new information, provided by Arty G. Schronce of the GDA, suggesting issues with the credibility of the Georgia Dock index.

The price of Sanderson Farms shares continued to fall for the next three consecutive trading days, closing on November 21, 2016 at \$78.98, or a three-day loss of almost 8%. a) Procedural History This case is one of several shareholder suits brought against chicken producers following the wave of antitrust suits and accompanying stock price drops.³ On October 20, 2016, a putative class action was filed in the District of Colorado against Pilgrim’s Pride Corporation, and its executives, for violations of the Exchange Act.

On November 28, 2016, a similar class action complaint was filed against Tyson Foods, Inc. and its executives in the Western District of Arkansas. The complaint against Tyson Foods, Inc. was dismissed on July 26, 2017, in a detailed memorandum opinion.

The Western District of Arkansas (Timothy L. Brooks, J., presiding) dismissed the shareholder suit on July 26, 2017, *In re Tyson Foods, Inc. Sec. Litig.*, 275 F. Supp. 3d 970 (W.D. Ark. 2017), and then declined to provide leave to amend on March 31, 2018, *In re Tyson Foods, Inc. Sec. Litig.*, 2018 WL 1598670 (W.D. Ark. Mar. 31, 2018).

The complaint against Pilgrim's Pride, Inc. was not dismissed until March 14, 2018. *Hogan v. Pilgrim's Pride Corporation*, 2018 WL 1316979 (D. Col. Mar. 14, 2018). On October 28, 2016, appellants filed a putative class action in the Southern District of New York on behalf of all persons who purchased Sanderson Farms shares between December 17, 2013 and November 17, 2016.

On February 13, 2017, appellants Gordon Gamm and Don Pritchard were appointed lead plaintiffs, and Pomerantz LLP was appointed lead counsel. *Gamm et al., v. Sanderson Farms, Inc., et al.*, 16-8420, Dkt. No. 23 (Feb. 13, 2017).

On March 30, 2017, appellants filed an amended complaint. On May 18, 2017, at a conference before Judge Berman, counsel for the parties set a briefing schedule for a motion to dismiss and response. Judge Berman, pursuant to his individual practices, requested that the parties submit pre-motion letters.

The court explained to appellants that, through the pre-motion letters, appellants would be able to determine appellees' "bases" for dismissal, and amend their complaint a second time, accordingly. However, the court cautioned that any second amended complaint "would be the last amendment," stating, that "if [appellants] were to lose the motion [to dismiss]" the court would not provide further leave to amend.

Pre-motion letters were submitted on May 25 and June 1, 2017. On June 15, 2017, appellants filed a second amended complaint, alleging that appellee Sanderson and its Chief Executive Officer Joe F. Sanderson, Jr., Chief Financial Officer Michael D. Cockrell, and Chief Operations Officer Lampkin Butts violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, as well as Section 20(a) of the Exchange Act, by making statements that were materially false and misleading because "they failed to disclose material adverse information and misrepresented the truth about Sanderson Farms' finances and business prospects." SAC ¶ 169.

Appellees moved to dismiss for failure to adequately plead the elements of securities fraud on June 29, 2017. On January 19, 2018, the district court granted appellees' motion to dismiss with prejudice. Decision and Order, *Gamm et al., v. Sanderson Farms, Inc., et al.*, 16-8420, Dkt. No. 55 (S.D.N.Y. Jan. 19, 2018). Observing that the case was "strikingly similar" to the suit against Tyson Foods, Inc., the district court concluded that because "[p]laintiffs fail to support their

allegation of a chicken supply reduction conspiracy with particularized facts,” 15 they had not properly alleged a Section 10(b) violation.

Decision and Order at 5. 16 The case was timely appealed. 17 18 14 1 DISCUSSION 2 We review de novo a district court’s dismissal pursuant to Fed. R. Civ. P. 3 12(b)(6). Absolute Activist Value Master Fund Ltd. v. Ficeto, 677 F.3d 60, 65 (2d 4 Cir. 2012). Generally, when undertaking this review, we ask whether the 5 complaint contains “sufficient factual matter, accepted as true, to ‘state a claim to 6 relief that is plausible on its face.’” Ashcroft v. Iqbal, 556 U.S. 662, 678 (2009) 7 (quoting Bell Atl.

Corp. v. Twombly, 550 U.S. 544, 570 (2007)). The court accepts 8 as true “all well-pleaded factual allegations in the complaint,” draws “all 9 reasonable inferences in favor of the nonmoving party,” S.E.C. v. Pimpcio 10 Advisors Fund Mgmt., LLC, 341 F. Supp. 2d 454, 463 (S.D.N.Y. 2004), and 11 considers, in addition to the complaint, and written instruments attached, 12 statements incorporated by reference, and public disclosure documents filed with 13 the SEC, Kramer v. Time Warner, Inc., 937 F.2d 767, 774 (2d Cir.

1991). The court 14 may also consider items of which it has taken judicial notice under Federal Rule 15 of Evidence 201. See id. 16 The pleadings are typically subject to Federal Rule of Civil Procedure 8, 17 requiring a “short and plain statement of the claim.” This is understood to 18 require “more than an unadorned, the defendant-unlawfully-harmed-me 15 1 accusation” but does not require “detailed factual allegations.” Iqbal, 556 U.S. at 2 678.

3 This appeal involves a different pleading standard. Claims of fraud must 4 be “state[d] with particularity” under Federal Rule of Civil Procedure 9(b). The 5 pleading standard for securities fraud suits under Section 10(b) is further affected 6 by the requirements of the PSLRA: 7 [i]n any private action arising under this chapter in 8 which the plaintiff alleges that the defendant— 9 (A) made an untrue statement of a material fact; or 10 (B) omitted to state a material fact necessary in order to 11 make the statements made, in the light of the 12 circumstances in which they were made, not 13 misleading; 14 the complaint shall specify each statement alleged to 15 have been misleading, the reason or reasons why the 16 statement is misleading, and, if an allegation regarding 17 the statement or omission is made on information and 18 belief, the complaint shall state with particularity all 19 facts on which that belief is formed.

20 21 15 U.S.C. § 78u-4(b)(1). Additionally, where “proof that the defendant acted with 22 a particular state of mind” is at issue, the PSLRA requires that “the complaint 23 shall, with respect to each act or omission alleged to violate this chapter, state 16 1 with particularity facts giving rise to a strong inference that the defendant acted 2 with the required state of mind.” 15 U.S.C. § 78u-4(b)(2).

3 We have held that Rule 9(b) and the PSLRA require a securities fraud 4 complaint to “(1) specify the statements that the plaintiff contends were 5 fraudulent, (2) identify the speaker, (3) state where and when the statements 6 were made, and (4) explain why the statements were fraudulent.” *Mills v. Polar 7 Molecular Corp.*, 12 F.3d 1170, 1175 (2d Cir. 1993).

This rule “serves to provide a 8 defendant with fair notice of a plaintiff’s claim, safeguard his reputation from 9 improvident charges of wrongdoing, and protect him against strike suits.” *ATSI 10 Commc’ns, Inc. v. Shaar Fund, Ltd.*, 493 F.3d 87, 99 (2d Cir. 2007). 11 To state a claim for securities fraud under Section 10(b) and Rule 10b-5 12 promulgated thereunder, a plaintiff must allege that the defendant: “(1) made 13 misstatements or omissions of material fact; (2) with scienter; (3) in connection 14 with the purchase or sale of securities; (4) upon which plaintiffs relied; and (5) 15 that plaintiffs’ reliance was the proximate cause of their injury.” *In re IBM Corp. 16 Sec. Litig.*, 163 F.3d 102, 106 (2d Cir.

1998) (citations omitted). 17 Appellants acknowledge that their allegations of misstatements and 18 omissions – also known as the “falsity” prong of a 10(b) action – must be pleaded 17 1 with particularity. However, they disagree as to whether facts of the underlying 2 antitrust conspiracy must similarly be pleaded with particularity or must merely 3 meet the Rule 8 plausibility standard.

Appellants argue that “there is no public 4 policy reason” supporting the use of a heightened pleading standard for 5 allegations of anticompetitive conduct “simply because they underpin a 6 securities fraud class action.” They argue that their complaint was “replete with 7 factual allegations” providing sufficient notice to appellees. Appellees respond 8 that the district court was correct to require that allegations of antitrust 9 conspiracy be pleaded with particularity.

10 Under Rule 9(b) and the PSLRA, the circumstances of a fraud include “the 11 basis” for that contention. First, in this matter, the alleged fraud and the facts of 12 the alleged anticompetitive conspiracy are inseparable and the clear language of 13 the statute requires that underlying facts be pleaded with particularity.

As 14 discussed above, 15 U.S.C. § 78u-4(b)(1) requires that a securities fraud claim 15 based on information and belief must “state with particularity all facts on which 16 that belief is formed.” (emphasis added).

In this case, appellants’ nondisclosure 17 and material omission claims are entirely dependent upon the predicate 18 allegation that Sanderson participated in a collusive antitrust conspiracy. In 18 1 order to properly provide “all facts” upon which their securities fraud claim is 2 based, their allegations must also provide particularized facts about the 3 underlying conspiracy.

Until and unless they have done so, appellants’ 4 complaint had not met the burden of explaining what rendered the statements 5 materially false or misleading. 6 District courts within this circuit

have correctly taken the view that when 7 the nondisclosure of an illegal act is the basis of a 10(b) complaint, the illegal act 8 must be alleged with particularity.

See, e.g., *In re Axis Capital Holdings Ltd. Sec. 9 Litig.*, 456 F. Supp. 2d 576, 585 (S.D.N.Y. 2006) (“If the complaint fails to allege 10 facts which would establish such an illegal scheme, then the securities law claims 11 premised on the nondisclosure of the alleged scheme are fatally flawed.”); *In re 12 Banco Bradesco S.A. Sec. Litig.*, 277 F. Supp. 3d 600, 631 (S.D.N.Y.

2017) (“As part 13 of the ‘circumstances constituting fraud,’” an alleged bribery scheme, 14 nondisclosure of which formed the basis of the securities suit, “must be pleaded 15 with particularity.”) (quoting Fed. R. Civ. P. 9(b)). 19 1 District courts in other circuits that have considered follow-on securities 2 class actions arising out of allegations of antitrust conspiracy have all concluded 3 that antitrust schemes must be pleaded with particularity.^{4 4} The rationale for a heightened pleading standard for predicate acts 5 hearkens back to *Novak v. Kasaks*.

See 216 F.3d at 313-14. There, we prescribed 6 the proper pleading standard for securities fraud suits in light of the recent 7 passage of the PSLRA. We acknowledged that the PSLRA “does not require that 8 plaintiffs plead with particularity every single fact upon which their beliefs 9 concerning false or misleading statements are based,” but rather that plaintiffs 10 must “plead with particularity sufficient facts to support those beliefs.” 11 (emphasis in original).

Accordingly, this court held that “a complaint can meet 4 In *Hogan*, the District of Colorado recognized that “[r]equiring that allegations of underlying wrongdoing that rest on information and belief be supported by particularized facts comports with the PSLRA’s dictate that ‘if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is made.’” 2018 WL 1316979 at *5 (March 14, 2018) (quoting 15 U.S.C. § 78u-4(b)(1)).

Similarly, in *In re Tyson Foods*, the Western District of Arkansas concluded that “to the extent that a plaintiff’s allegations of underlying wrongdoing ‘regarding the statement or omission’ rest ‘on information and belief,’ those allegations must be supported by particularized facts.” 275 F. Supp. 3d at 985 (quoting 15 U.S.C. § 78u-4(b)(1)). 20 1 the new pleading requirement imposed by [the PSLRA] by providing 2 documentary evidence and/or a sufficient general description of the personal 3 sources of the plaintiffs’ beliefs,” although there is no requirement that the 4 plaintiffs name confidential sources.

Id. 5 Applying that standard here, appellants were required to plead with 6 particularity sufficient facts to support their contention that Sanderson Farms’ 7 financial disclosures were misleading. This necessarily requires that facts of the 8 underlying anticompetitive conduct be pleaded with particularity. Otherwise, 9 the complaint provides no basis as to what rendered Sanderson’s statements false 10 or misleading.

Because Sanderson Farms' statements were materially false or misleading only to the extent that anticompetitive conduct actually occurred, appellants must plead sufficient — though not exhaustive — facts describing the essential elements of that underlying conduct. Requiring that illegal acts underpinning a securities fraud suit be pleaded with particularity also comports with the stated intent and public policy rationale of the PSLRA.

The requirements of Rule 9(b) and the PSLRA operate “to deter strike suits wherein opportunistic private plaintiffs file securities fraud claims of dubious merit in order to exact large settlement recoveries.” *Novak*, 216 F.3d at 211, 306. See also H.R. Conf. Rep. No. 104-369, at 31 (1995) (observing “significant evidence of abuse in private securities lawsuits,” including “the routine filing of lawsuits against issuers of securities and others whenever there is a significant change in an issuer’s stock price, without regard to any underlying culpability of the issuer,” and “the abuse of the discovery process to impose costs so burdensome that it is often economical for the victimized party to settle”) (reprinted in 1995 U.S.C.C.A.N.

730, 730). As we have previously noted, it “is a serious matter to charge a person with fraud and hence no one is permitted to do so unless he is in a position and is willing to put himself on record as to what the alleged fraud consists of specifically.” *Decker v. Massey-Ferguson, Ltd.*, 681 F.2d 111, 115 (2d Cir. 1982). A stock-issuing company like Sanderson cannot be required, whenever accused of illegal activity, to simultaneously defend itself in an accompanying securities fraud suit based on facts not alleged with the level of particularity required by the statute.

Such a reality would harm the company’s stock and contravene the purpose of the securities laws — to protect shareholders’ interests. The clear language of the statute, the existing case-law, and the stated intent of the securities laws all lead us to recognize that, when a complaint claims that statements were rendered false or misleading through the non-disclosure of illegal activity, the facts of the underlying illegal acts must also be pleaded with particularity, in accordance with the heightened pleading requirement of Rule 9(b) and the PSLRA.

In practical terms, the pleading standard required appellants to have alleged the basic elements of an underlying antitrust conspiracy, which are: “(1) a contract, combination, or conspiracy; (2) in restraint of trade; (3) affecting interstate commerce.” *Maric v. St. Agnes Hosp. Corp.*, 65 F.3d 310, 313 (2d Cir. 1995).

The first element, and the “crucial question” in any antitrust claim, has to do with “whether the challenged anticompetitive conduct stems from independent decision[s] or from an agreement, tacit or express.” *Twombly*, 550 U.S. at 553. An agreement can be alleged through direct evidence; however, in most antitrust cases “this type of ‘smoking gun’ can be hard to come by,

16 especially at the pleading stage.” Mayor and City Council of Baltimore, Md. v. 17 Citigroup, Inc., 709 F. 3d 129, 136 (2d Cir.

2013). As an alternative, a complaint 18 may “present circumstantial facts supporting the inference that a conspiracy 23 1 existed.” Id. This inference may arise through the alleging of “conscious 2 parallelism, when such interdependent conduct is accompanied by circumstantial 3 evidence and plus factors.” Todd v. Exxon Corp., 275 F.3d 191, 198 (2d Cir. 2001).

4 Such “plus factors” may include: “a common motive to conspire, evidence that 5 shows that the parallel acts were against the apparent individual economic self- 6 interest of the alleged conspirators, and evidence of a high level of interfirm 7 communications.” Twombly v. Bell Atlantic Corp., 425 F.3d 99, 114 (2d Cir. 8 2005).

In sum, an agreement may be alleged through conscious parallelism 9 together with plus factors, but “alleging parallel conduct alone is insufficient, 10 even at the pleading stage.” Citigroup, 709 F.3d at 136. 11 Although appellants do allege that Sanderson engaged in 12 “anticompetitive” conduct, there is virtually no explanation as to how that 13 collusive conduct occurred, and whether and how it affected trade.

14 On the first element – tacit agreement – appellants allege mere parallel 15 conduct, and lack indicia of mutuality or otherwise interdependent action. 16 Specifically, appellants allege that Sanderson Farms and its industry peers 17 engaged in supply reductions through a variety of means, including destroying 18 broiler breeder hens, Compl. ¶ 38; destroying eggs, Compl. ¶¶ 38, 41; exporting 24 1 excess eggs and flocks, Compl. ¶¶ 38, 39; and dumping excess inventory in 2 foreign markets, Compl. ¶ 40.

But appellants provide no facts alleging that 3 Sanderson or its peers actually reduced supply, and that these reductions were 4 the result of an agreement, or were even interrelated. Appellants instead merely 5 use stock phrases such as “worked in concert” and “coordinated.” Appellants 6 could have alleged when Sanderson Farms decided on its course of supply 7 reduction, which industry peers were a part of that decision, how specific supply 8 reductions were performed by each of the different poultry producers, what 9 information Sanderson Farms knew about its peers’ supply reductions, if any, 10 and — perhaps most basic of all — whether Sanderson Farms actually reduced 11 chicken supply, and if so, by what volume.

Appellants have provided none of 12 these facts. 13 Appellants’ “plus factors” fail to remedy the deficient pleadings. Although 14 appellants allege that, through Agri Stats, Sanderson Farms and its industry 15 peers were able to “facilitate” the supply reductions, they do not allege when and 16 how Sanderson Farms used Agri Stats to know of their peers’ supply reductions.

17 Rather, appellants merely allege that by reverse-engineering the Agri Stats data, 18 Sanderson Farms “could” determine whether or not its peers were reducing 25 1 supply. Compl. ¶ 49.

Similarly, they allege that Sanderson Farms had 2 “numerous opportunities to conspire” through its participation in trade 3 associations and plant tours, and that the general structure of the poultry market 4 made it “susceptible to price-fixing.” Compl. ¶¶ 69 and 74.

But the law is clear 5 that “[t]he mere opportunity to conspire does not by itself support the inference 6 that such an illegal combination actually occurred.” *Capital Imaging Associates*, 7 P.C. v. *Mohawk Valley Medical Associates, Inc.*, 996 F.2d 537, 545 (2d Cir. 1993). 8 See also *AD/SAT, Div. of Skylight, Inc. v. Associated Press*, 181 F.3d 216, 234 (2d 9 Cir.

1999) (“[A]lthough the nature of trade associations is such that they are 10 frequently the object of antitrust scrutiny, every action by a trade association is 11 not concerted action by the association’s members.”) (internal citation omitted). 12 Separately, appellants allege that Sanderson Farms and its peers 13 manipulated the pricing reported to the Georgia Dock, and that this 14 manipulation would necessarily require coordination because “[a]s a producer, 15 your high price quote doesn’t work unless others go along because it will be an 16 outlier that gets thrown out per the GDA’s methodology.” Compl. ¶ 62.

The 17 detail of this allegation exceeds that of the allegations of supply reductions 18 because here appellants have provided a theory for why price reporting would 26 1 have had to be coordinated. However, the allegation regarding the Georgia Dock 2 is still insufficient. Appellants have pleaded no facts regarding Sanderson Farms’ 3 communications with the Georgia Dock such as what information Sanderson 4 Farms provided to the Georgia Dock, on what occasions, and whether it was 5 false.

6 For these reasons, appellants have failed to plead the first element of 7 antitrust conspiracy agreement at even a basic level, much less with particularity. 8 Furthermore, on the second and third elements of an antitrust conspiracy, 9 appellants have provided no allegations.

The complaint is entirely silent as to 10 whether the supply reductions or the Georgia Dock manipulations unreasonably 11 restrained trade, and whether that restraint affected interstate commerce. This 12 complaint merely attempts to “establish fraud by innuendo,” and accordingly, its 13 pleadings are insufficient. *Chicago Title & Trust Co. v. Fox Theatres Corp.*, 182 F. 14 Supp. 18, 33 (S.D.N.Y.

1960). 15 In view of our disposition of this matter, we need not reach the issues of 16 scienter, reliance, or control person liability under Section 20 of the Exchange Act, 17 15 U.S.C. § 78(t)(a). See, e.g., *In re Corning Sec. Litig.*, 01 Civ. 6580(CJS), 2004 WL 27 1 1056063, at *32 (W.D.N.Y. Apr. 9, 2004); *In re Hudson Techs. Sec. Litig.*, 98 Civ. 2 1616(JGK), 1999 WL 767418, at *13 (S.D.N.Y.

Sept. 28, 1999). 3 **CONCLUSION** 4 For the foregoing reasons, we hold that when a securities fraud complaint 5 claims that statements were rendered false or misleading through the 6

nondisclosure of illegal activity, the facts of the underlying illegal acts must be 7 pleaded with particularity in accordance with the requirements of Rule 9 and the 8 PSLRA.

Because appellants have failed to meet this pleading standard for the 9 underlying allegations of illegal antitrust conspiracy, their complaint was 10 deficient. Accordingly, we affirm. 1 2 3 4 5 6 7 8 9 10 11 12 13 28