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INTRODUCTION

When imagining a modern David and Goliath story, one would not normally think of a group of Wall Street hedge funds versus individuals on a forum on Reddit.com. In January of 2021 though, many headlines made this comparison, as online traders frantically purchased GameStop stock (“GME”) and drove the prices sky-high, while large hedge funds faced up to \$19 billion in losses.¹ Throughout January and mid-February, users of the Reddit forum r/WallStreetBets began buying GME for collective entertainment reasons. What began as a “meme stock” that users purchased to comically pump the stock of a chain of mall video-game stores blew up into a frenzy.² The fact that GME was massively shorted contributed to the hysteria, with Reddit users deciding to try to punish those who were shorting the stock in a classic underdog manner.³ On January 26, Elon Musk tweeted about the company with a link to the Reddit forum which only added momentum to the trend.⁴ The stock rose 1500% in a manner rarely seen on the stock market, and GameStop grew from one of the most shorted companies valued at under \$1.3 billion to a multi-billion dollar corporation valued at \$21 billion.⁵

The exhilarating, almost comical nature of this event had many investors--casual, or professional--wondering what was next in the chain of consequences. The casino-style betting of stocks has always been a grey area in the securities laws, and GameStop's event called into question whether Reddit users openly worked together to manipulate the stock market in violation of Rule 10b-5. Rule 10b-5 is the federal securities law's broadest anti-fraud provision

¹ See Keith Griffith, *GameStop Winners and Losers: How Small 'Wolves of Reddit' Investors Are Now Millionaires on Paper and 'Roaring Kitty' Is Up \$31M – While Hedge Funds Face \$19B in Losses*, DAILY MAIL, (Jan. 29, 2021), <https://www.dailymail.co.uk/news/article-9203101/GameStop-winners-losers-Small-Reddit-investors-hedge-funds-face-19B-losses.html>.

² See Matt Levine, *The GameStop Game Never Stops*, BLOOMBERG (Jan. 25, 2021), <https://www.bloomberg.com/opinion/articles/2021-01-25/the-game-never-stops?sref=1kJVNqnU>.

³ Id.

⁴ See Dorothy Gambrell, *A Brief History of Elon Musk's Recent Market-Moving Tweets*, BLOOMBERG (Feb. 11, 2021) <https://www.bloomberg.com/news/articles/2021-02-11/how-elon-musk-s-tweets-moved-gamestop-gme-bitcoin-dogecoin-and-other-stocks>.

⁵ See Principia Pilot, *David and Goliath in 2021: How Reddit broke Wall Street*, Pilot (Feb. 1, 2021), <https://principiapilot.org/david-and-goliath-in-2021-how-reddit-broke-wall-street/>.

and has been the Securities Exchange Commission’s (“SEC”) most preferred enforcement mechanism.⁶ The rule prohibits individuals from using the securities market to “employ any device, scheme, or artifice to defraud,” to “make any untrue statement of material fact,” or to “engage in any act, practice or course of business which would operate . . . as a fraud or deceit upon any person.”⁷ Courts have construed this rule into a six element requirement, which includes establishing what constitutes “manipulative acts.”⁸

Commentators are also calling for Congress to take action against the short selling of stocks, as well as for Congress to examine the role that online trading platforms play in free market trading.⁹ On February 18, 2021, the U.S. House Financial Services and Senate Banking committees held a hearing in which various individuals, including the CEOs of Robinhood, Melvin Capital, Reddit, and Citadel Securities were questioned.¹⁰ Robinhood, in particular, was in the hot seat, as House Democrats and Republicans alike examined the online trading platform’s decision to halt buy orders of GameStop and other stocks. If Robinhood had restricted the purchase of GameStop shares as part of a deceptive, manipulative, or fraudulent effort to lower its value, Robinhood could also be looked at for violations of Rule 10b-5.¹¹

The actions of hedge funds billionaires also faced criticism from House representatives. In the words of House Representative Maxine Waters, a Democrat who heads the House panel, Congress wanted to address the hedge funds whose “unethical conduct directly led to the recent market volatility.”¹² The GameStop scandal led the panel to examine the market in general and

⁶ See 17 C.F.R. § 240.10b-5(a)–(c); Merritt B. Fox, Lawrence R. Glosten, & Gabriel V. Rauterberg, *Stock Market Manipulation and its Regulation*, 25 YALE L. REV. 67, 118 (2018).

⁷ 17 C.F.R. § 240.10b-5(a)–(c).

⁸ *Onel v. Top Ships, Inc.*, 806 Fed. App’x. 64, 66 (2d Cir. 2020) (quoting *ATSI Commc’ns., Inc. v. Shaar Fund, Ltd.*, 493 F.3d 87, 101 (2d Cir. 2007)) (internal quotation marks omitted). The full six-part test states: “[A] plaintiff must allege: (1) manipulative acts; (2) damage; (3) caused by reliance on an assumption of an efficient market free of manipulation; (4) scienter; (5) in connection with the purchase or sale of securities; (6) furthered by the defendants use of the mails or any facility of a national securities exchange.” *Id.*

⁹ See David Shepardson, *U.S. Congress to hold hearings on GameStop trading, state of stock markets*, REUTERS, (Jan. 28, 2021), <https://www.reuters.com/article/us-retail-trading-usa-congress/u-s-congress-to-hold-hearings-on-gamestop-trading-state-of-stock-markets-idUSKBN29X33T>.

¹⁰ See John Hyatt, *Three Takeaways from Congress’s GameStop (GME) Hearing*, NASDAQ (Feb. 19, 2021), <https://www.nasdaq.com/articles/three-takeaways-from-congresss-gamestop-gme-hearing-2021-02-19>

¹¹ See Joshua F. Bautz, *What Is the SEC Going To Do About GameStop?*, NYSBA, (Feb. 4, 2021), <https://nysba.org/what-is-the-sec-going-to-do-about-gamestop/>.

¹² David Shepardson, *U.S. Congress to hold hearings on GameStop trading, state of stock markets*, REUTERS, (Jan. 28, 2021), <https://www.reuters.com/article/us-retail-trading-usa-congress/u-s-congress-to-hold-hearings-on-gamestop-trading-state-of-stock-markets-idUSKBN29X33T>.

evaluate how long it has been “manipulated” by hedge funds and their financial partners to “benefit themselves while others pay the price.”¹³

This paper argues that there is a deficiency in the legislation in terms of what constitutes “open market manipulation.” Open market manipulation refers to the act of manipulating the market for intentional price-movement and profit through facially legal means.¹⁴ Contrary to traditional manipulation that is regulated by Section 10b, open market manipulators largely falls through the cracks of SEC enforcement, as it is difficult to prove that the manipulator did “bad acts”, such as nondisclosure or fraud. This is kind of manipulation that the GameStop saga brought to light, with both small-scale and institutional investors partaking in the scheme. Although the GameStop instance is perhaps the first of its kind, without legislative consequences, it is likely that investors will repeat this process of artificial inflation and cause significant economic and social harm.

Circuits have been split on the legality of open market manipulation, but the SEC and the courts need to devise a better solution to these attempts at manipulation from small-scale individuals and wealthy hedge funds alike. Individuals with significant influence like Elon Musk can also openly manipulate the market for their own benefit. Trends have shown that Musk’s tweets can bump the companies he promotes up to 5,100%. Courts must find a better solution to address these attempts at manipulation, as ultimately anyone with a big enough following can manipulate the market.

I. An Overview of the GameStop Saga

A. GameStop’s Struggle Turns It Into A Cult-Stock

GameStop Corp. is a video game retailer, selling video game hardware, physical and digital video game software, and video game accessories via its GameStop, EB Games, and Micromania stores.¹⁵ It operates as a retailer in the United States, Canada, Australia, and Europe.¹⁶ It was founded in 1984, and had a simple business model of

¹³ David Shepardson, *U.S. Congress to hold hearings on GameStop trading, state of stock markets*, REUTERS, (Jan. 28, 2021), <https://www.reuters.com/article/us-retail-trading-usa-congress/u-s-congress-to-hold-hearings-on-gamestop-trading-state-of-stock-markets-idUSKBN29X33T>.

¹⁴ See Maxwell K. Multer, *Open-Market Manipulation Under SEC Rule 10b-5 and its Analogues: Inappropriate Distinctions, Judicial Disagreement and Case Study: FERC’s Anti-Manipulation Rule*, 39 Sec. Reg. L.J. 97, 100 (2011).

¹⁵ Reuters, *GameStop Corp*, REUTERS,, <https://www.reuters.com/companies/GME>, (last visited April 19, 2021).

¹⁶ Yahoo, *GameStop Corp. (GME)*, YAHOO, https://finance.yahoo.com/quote/GME/profile/?guccounter=1&guce_referrer=aHR0cHM6Ly93d3cuZ29vZ2xiLmN

selling video games and equipment out of physical locations. GameStop earnings in 2011 reflected a net income of \$408 million on a revenue of \$9.5 billion.¹⁷ However, as times changed and less people bought physical games, GameStop's stock had been in a steady decline since 2015. In April of 2020, GameStop was struggling financially, with its brick-and-mortar model proving unreliable as the Covid-19 pandemic hit.¹⁸ The chain was losing money, and as the pandemic worsened, consumer trends shifted. More people were downloading video games at home instead of visiting stores in-person.¹⁹ The company had posted \$470 million in losses in 2019, and by the time the pandemic hit, the company announced that it would be permanently closing 300 locations.²⁰ On April 1, 2020, GameStop's stock price was \$3.25 per share.²¹

In August 2020, investor Ryan Cohen, founder and former CEO of Chewy Inc. bought a 13% stake in GameStop and issued a public letter advocating for corporate reforms.²² Cohen's experience in building and running e-commerce companies in the digital era letter was the foundation of his criticism. Cohen chastised GameStop's board of directors and advocated that GameStop can turn things around by shifting its focus away from physical stores in favor of building a robust e-commerce platform.²³ The letter generated significant press and garnered the attention of Reddit users via the r/WallStreetBets subreddit.²⁴ By January of 2021, Cohen and two associates from his investment company were appointed to serve on GameStop's expanded board.²⁵ Cohen

vbS8&guce_referrer_sig=AQAAANylRfxDyAsuFff-MBZ0fw6pIZNhNrDKe0TeFBMtD21Q605jm0LXpIaEJViSHYzhXzWRsgaJQZrGiPRhp_gdsYN1q_3B6YT7Hxcwq4LID-MSnt5ErljQD1TcY6Vsv3nA9K9d8mFBYXJXUTYp_bBfJS1mQhcoUcFQdwHFm7i0dw, (last visited April 19, 2021).

¹⁷ See, e.g., Matt Levine, *GameStonk Rocket Rocket Rocket*, Bloomberg (Jan. 27, 2021),

<https://www.bloomberg.com/opinion/articles/2021-01-27/reddit-driven-surge-puts-gamestop-and-ryan-cohen-in-a-weird-spot>

¹⁸ See Alex Kirshner, *What the Hell is Going On With GameStop's Stock?*, SLATE (Jan. 26, 2021),

<https://slate.com/technology/2021/01/gamestop-reddit-wallstreetbets-gme.html>.

¹⁹ Id.

²⁰ Id.

²¹ Id.

²² See Kenneth Squire, *Former Chewy CEO tries to push GameStop to become the Amazon of the video-game industry*, CNBC, (Nov. 21, 2020) <https://www.cnbc.com/2020/11/20/former-chewy-ceo-ryan-cohen-urges-gamestop-to-become-the-amazon-of-video-games.html>.

²³ Id.

²⁴ See Alex Kirshner, *What the Hell is Going On With GameStop's Stock?*, SLATE (Jan. 26, 2021),

<https://slate.com/technology/2021/01/gamestop-reddit-wallstreetbets-gme.html>.

²⁵ Alex Kirshner, *What the Hell is Going On With GameStop's Stock?*, SLATE (Jan. 26, 2021),

<https://slate.com/technology/2021/01/gamestop-reddit-wallstreetbets-gme.html>.

was instantly deemed as a “corporate savior” by many retail investors, and his move into the board propelled GameStop’s stock into a “cult-stock.”²⁶ Two days after the announcement that Cohen joined the board, GME surged more than 50%, going from \$20.42 per share to \$31.40 after reaching as high as \$38.65 per share.²⁷

B. GameStop Gets Massively Shorted By Institutional Investors.

Despite growing traction amongst individual retail investors, institutional investors and hedge funds, including Citron Research and Melvin Capital were skeptical of any real change in GameStop’s financials.²⁸ These investors took out massive short positions against the stock, believing that any rise in GME was solely due to Cohen’s presence and that the stock was artificially overvalued.²⁹ These professional investors betted that GME would fall and tried to profit off of this by shorting millions of shares of GameStop.³⁰ “Shorting” refers to an investment strategy where a position is opened by borrowing shares of stock that the investor believes will decrease in value.³¹ Afterwards, the investor sells the borrowed shares to buyers willing to pay the market price.³² Before returning the borrowed shares, the investor is essentially betting that the price of the stocks will fall and that the investor can repurchase the borrowed shares at a lower price.³³ The difference in the market price that the investor initially got from selling the borrowed shares and the lowered price the investor paid to purchase them back is pocketed by the investor.³⁴ Short positions in GME became notorious, with Bloomberg

²⁶ Bailey Lipschultz, *GameStop Tug of War Gives Reddit Army A Win On Record Volatility*, BLOOMBERG, (Jan. 22, 2021), <https://www.bloomberg.com/news/articles/2021-01-22/gamestop-tug-of-war-gives-reddit-army-a-win-on-record-volatility?sref=1kJVNqnU>.

²⁷ Alex Kirshner, *What the Hell is Going On With GameStop’s Stock?*, SLATE (Jan. 26, 2021), <https://slate.com/technology/2021/01/gamestop-reddit-wallstreetbets-gme.html>.

²⁸ Emily Stewart, *The GameStop Stock Frenzy, Explained*, Vox (Jan. 29, 2021), https://www.vox.com/the-goods/22249458/gamestop-stock-wallstreetbets-reddit-citron?fbclid=IwAR1If3ANoY7Jq8MgEr67J4iTztXI__R2EcHwr1SvQOSrw4dbdpWoTPpSouU

²⁹ Id.

³⁰ Alex Kirshner, *What the Hell is Going On With GameStop’s Stock?*, SLATE (Jan. 26, 2021), <https://slate.com/technology/2021/01/gamestop-reddit-wallstreetbets-gme.html>.

³¹ Adam Hayes, *What is Short Selling?*, Investopedia, (Mar 13, 2021), <https://www.investopedia.com/terms/s/shortselling.asp>.

³² Id.

³³ Id.

³⁴ Id.

reporting in early January 2021 that GameStop had up to 71.2 million shares in short positions.³⁵

On the other hand, Reddit users of r/WallStreetBets have been priming to “take over” GameStop as a joke since 2019.³⁶ A user called “delaneydi” argued on Reddit that GME was getting underpriced on the market, with the thesis that there is potential upside catalysts from continued strength in digital and accessories sales.³⁷ For a while, it was a running joke that r/WallStreetBets would take over GameStop. However, the joke turned into reality when users began to take on institutional investors in order to punish them for short-selling by forcing them into a short squeeze.³⁸ A short squeeze is where investors target short sellers by attempting to drive up stock prices in order to force those traders to sell their positions at a loss to forestall greater financial exposure should the stock keep rising.³⁹

Reddit users began advocating to punish these Wall Street giants, posting guidelines titled “Bankrupting Institutional Investors for Dummies, ft. GameStop”⁴⁰ which outlined pumping the stock to short squeeze the investors.⁴¹ The initial common enemy within the users was Andrew Left of Citron Research, who was a loud and large bettor against GameStop. Left tweeted out why GME would plummet to \$20 (after climbing up to \$41 following the initial buzz), writing, “We understand short interest better than you and will explain.”⁴² Forcing him to buy more shares at a higher price to cover his short position was the initial goal for Reddit users, with calls to buy the stocks,

³⁵ Elizabeth Lopatto, *How R/WallStreetBets Gamed the Stock of GameStop*, VERGE (Jan. 27, 2021), <https://www.theverge.com/22251427/reddit-gamestop-stock-short-wallstreetbets-robinhood-wall-street>.

³⁶ Id.

³⁷ u/delaneydi, *GameStop Investment Thesis*, Reddit (2019), https://www.reddit.com/r/wallstreetbets/comments/b4zlkz/gamestop_investment_thesis/.

³⁸ Elizabeth Lopatto, *How R/WallStreetBets Gamed the Stock of GameStop*, VERGE (Jan. 27, 2021), <https://www.theverge.com/22251427/reddit-gamestop-stock-short-wallstreetbets-robinhood-wall-street>.

³⁹ See Cory Mitchell, *Short Squeeze*, Investopedia, <https://www.investopedia.com/terms/s/shortsqueeze.asp#:~:text=What%20is%20a%20Short%20Squeeze,pressure%20on%20the%20stock's%20price>.

⁴⁰ u/Player896, *Bankrupting Institutional Investors for Dummies, ft GameStop*, Reddit (Sept. 19, 2020), https://www.reddit.com/r/wallstreetbets/comments/ivs6dw/bankrupting_institutional_investors_for_dummies/.

⁴¹ See Alex Kirshner, *What the Hell is Going On With GameStop's Stock?*, SLATE (Jan. 26, 2021), <https://slate.com/technology/2021/01/gamestop-reddit-wallstreetbets-gme.html>.

⁴² Cecilia D'Anastasio, *A Fight Over GameStop's Soaring Stock Turns Ugly*, WIRED (Jan. 22, 2021), <https://www.wired.com/story/gamestop-stock-wall-street-bets-short-squeeze/>.

alongside rocket ship and diamond “emojis” flooding the social media site.⁴³ On January 15, 2021, 194 million shares were traded, hitting over 12 times its average trading volume. The stock continued to rise, peaking at \$73.09 by midday.⁴⁴ In the words of Jaime Rogozinski who founded the subreddit, the stock “certainly started as a meme... but [the Reddit users] pushed it to a different level. They’re no longer commenting on the story. They’re wanting to become the story and have effectively done that.”⁴⁵

By the end of January, GME closed at \$325 per share, with more than a 1,500% increase.⁴⁶ Hedge funds and other institutions that shorted GME sat on losses of about \$19 billion, both Melvin Capital and Citron Research stating they had closed their short positions, realizing a misguided bet. “Roaring Kitty”, or Keith Gill, a Reddit user and former financial educator for an insurance firm in Massachusetts was at the front and center of gathering redditors to purchase GameStop stock. In mid-2019, he invested \$53,000 in GameStop options⁴⁷, which in 2021 soared in value to \$48 million—more than 900 times his initial investment.⁴⁸

C. Robinhood Enters the Saga—The Online Platform Halts GameStop Trading.

On January 28, Robinhood, an online financial trading platform restricted trades on GameStop, AMC Entertainment, and other stocks that were being driven up by individual investors on Reddit.⁴⁹ Robinhood struggled for cash and was forced to quickly raise more than \$1 billion from its own investors and bank credit lines so it could have enough money to post cash with market clearinghouses amid the high level of trading.⁵⁰

⁴³ Id.

⁴⁴ Id.

⁴⁵ Id.

⁴⁶ See GameStop Corp. (GME), Yahoo! Fin., <https://finance.yahoo.com/quote/GME/chart>.

⁴⁷ A call option gives the owner the right, but not the obligation, to buy a given stock at a specified price within a specific time period. See Jason Fernando, *Call Option Definition*, Investopedia, <https://www.investopedia.com/terms/c/calloption.asp> [<https://perma.cc/RCR2-C34N>]. Essentially, an option allows the owner to purchase stock in the future at its current price if the price goes up, or else let the option lapse if the prices decrease. Thus, if one owns an option to purchase ten shares of a given stock for \$5 in one year, and the stock price rises to \$15 per share, that option holder may still purchase the stock for just \$5. Exercising their option would thus net the user \$10 of gain per share.

⁴⁸ See Nathaniel Popper & Kellen Browning, *The ‘Roaring Kitty’ Rally: How A Reddit User and His Friends Roiled the Markets*, N.Y. Times (Jan. 29, 2021), <https://www.nytimes.com/2021/01/29/technology/roaring-kitty-reddit-gamestop-markets.html>.

⁴⁹ See Avie Schneider, *Game Back On: GameStop Stock Rebounds as SEC Warns Against Market Manipulation*, Nat’l Pub. Radio (Jan. 29, 2020), <https://www.npr.org/2021/01/29/962047287/game-back-on-gamestop-stock-rebounds-as-sec-warns-against-market-manipulation>.

⁵⁰ Id.

Clearinghouses settle the trades and need brokerages like Robinhood to have the cash to be good for the trades. Robinhood's decision was met with criticism, with Congressman Ro Khanna who represents the 17th District of California located in Silicon Valley stating that the move "showed how the cards are stacked against the little guy in favor of billionaire Wall Street Traders."⁵¹ Reddit users also chastised Robinhood's decision, with a member of the forum stating that Robinhood is "simultaneously" manipulating the system by taking advantage of people with less funds while preventing a greater number of shares to be purchased.⁵² Both Democrats and Republicans denounced Robinhood's ban of trading--with Representative Alexandria Ocasio-Cortez calling the decision "unacceptable", and Senator Ted Cruz "fully agree[ing]" with her.⁵³

Robinhood, however, claimed that the move to limit trading was a tough decision made amongst "extraordinary" conditions in the market.⁵⁴ A company blog post noted that Robinhood had many financial requirements, including SEC net capital obligations and clearinghouse deposits which they have the responsibility to comply with seriously.⁵⁵ This did not stop the dozens of proposed class action lawsuits, however, as many customers accused Robinhood of breaching its contract when it restricted trading of certain stocks.⁵⁶

More than 90 federal lawsuits were filed, claiming that Robinhood's actions were unfair and unlawful.⁵⁷ Many of the suits focused on Robinhood's trading restrictions, with allegations of breaches of contract, breaches of the implied duty of good faith and

⁵¹ Id.

⁵² Id.

⁵³ Alexandria Ocasio-Cortez (@AOC) Twitter (Jan. 28, 2021), <https://twitter.com/AOC/status/1354830697459032066>; See also Ted Cruz (@TedCruz) Twitter (Jan. 28, 2021), <https://twitter.com/tedcruz/status/1354833603943931905>.

⁵⁴ Avie Schneider, *Game Back On: GameStop Stock Rebounds as SEC Warns Against Market Manipulation*, Nat'l Pub. Radio (Jan. 29, 2020), <https://www.npr.org/2021/01/29/962047287/game-back-on-gamestop-stock-rebounds-as-sec-warns-against-market-manipulation>.

⁵⁵ Id.

⁵⁶ Tom Hals, *Analysis: Robinhood and Reddit protected from lawsuits by user agreement*, Congress, Reuters, (Jan. 30, 2021), <https://www.reuters.com/article/us-retail-trading-robinhood-liability-an/analysis-robinhood-and-reddit-protected-from-lawsuits-by-user-agreement-congress-idUSKBN29Z0HI>.

⁵⁷ See, e.g., Courtney v. Robinhood Financial LLC et al., 21 Civ. 60220 (S.D. Fla.); Daniels v. Robinhood Financial, LLC et al., No. 21 Civ. 290 (D. Colo.).

fair dealing, negligence, and breaches of fiduciary duty.⁵⁸ One class action lawsuit in Massachusetts alleged that Robinhood’s actions were undertaken “purposefully and knowingly” to “manipulate the market for the benefit of people and financial institutions who were not Robinhood’s customers.”⁵⁹ Another investor brought a putative class action alleging that limitations on trading implemented amidst this volatility had “deprived retail investors of the ability to invest in the open market.”⁶⁰ Claims have also been brought under Rule 10b-5.⁶¹

Although too early to know whether these lawsuits will prove to be a real threat to Robinhood, the trading platform received harsh criticism from Congress at the House Financial Services Committee hearings in February and March 2021.⁶² Democrats in particular called on regulators to consider banning the practice of payment for order flow and to rein in “gamification” features of the app. Sean Casten, a Democrat of Illinois, accused the company of taking advantage of inexperienced traders—including a customer who died of suicide after believing he had run up huge losses via the Robinhood app.⁶³

In addition, the SEC has announced that it was “actively monitoring the ongoing market volatility” and working to “assess the situation and review the activities of regulated entities, financial intermediaries, and other market participants.”⁶⁴ News outlets have also reported that the SEC is looking at a possible “market manipulation” case, by analogizing the online traders’ hyping shares of particular companies to a “pump and

⁵⁸ Gibson Dunn, *The GameStop Short Squeeze - Potential Regulatory and Litigation Fall Out and Considerations*, Gibson Dunn (Feb. 1, 2021), <https://www.gibsondunn.com/the-gamestop-short-squeeze-potential-regulatory-and-litigation-fall-out-and-considerations/>.

⁵⁹ Megan Leonhardt, *Robinhood now faces roughly 90 lawsuits after GameStop trading halt--here's how customers might actually get their day in court*, CNBC, (Feb. 17, 2021), <https://www.cnbc.com/2021/02/17/robinhood-faces-lawsuits-after-gamestop-trading-halt.html>.

⁶⁰ *Nelson v. Robinhood Financial LLC*, No. 21 Civ. 777, Dkt. 1 (S.D.N.Y. Jan. 28, 2021).

⁶¹ 17 C.F.R. § 240.10b-5(a)-(c).

⁶² *Following Recent Market Instability, Waters Announces Hearing on Short Selling, Online Trading Platforms* (Jan. 28, 2021),

<https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=407096#:~:text=Press%20Releases-.Following%20Recent%20Market%20Instability,%20Waters%20Announces%20Hearing,Short%20Selling,%20Online%20Trading%20Platforms&text=Private%20funds%20engaging%20in%20predatory,hurt%20workers%20must%20be%20stopped.>

⁶³ Andrew Ross Sorkin, *Something Very Wrong Happened Here*, The New York Times, (Feb. 19, 2021), <https://www.nytimes.com/2021/02/19/business/dealbook/robinhood-hearing-congress.html>.

⁶⁴ Dean Seal, *White House, SEC ‘Monitoring’ Volatile GameStop Stock*, Law360 (Jan. 27, 2021), [https://www.law360.com/media/articles/1349195/white-house-sec-monitoring-volatile-gamestop-](https://www.law360.com/media/articles/1349195/white-house-sec-monitoring-volatile-gamestop-stock?nl_pk=ef15795b-2462-46f9-bdad-117fcfcc6a0f&utm_source=newsletter&utm_medium=email&utm_campaign=media)

[stock?nl_pk=ef15795b-2462-46f9-bdad-](https://www.law360.com/media/articles/1349195/white-house-sec-monitoring-volatile-gamestop-stock?nl_pk=ef15795b-2462-46f9-bdad-117fcfcc6a0f&utm_source=newsletter&utm_medium=email&utm_campaign=media)

[117fcfcc6a0f&utm_source=newsletter&utm_medium=email&utm_campaign=media.](https://www.law360.com/media/articles/1349195/white-house-sec-monitoring-volatile-gamestop-stock?nl_pk=ef15795b-2462-46f9-bdad-117fcfcc6a0f&utm_source=newsletter&utm_medium=email&utm_campaign=media)

dump” scheme.⁶⁵ It is notable that the Securities Act of 1933, often referred to as the “truth in securities” law, has two basic objectives: (1) require that investors receive financial and other significant information concerning securities being offered for public sale; and (2) prohibit deceit, misrepresentations, and other fraud in the sale of securities.⁶⁶

D. The GameStop Volatility Proves that the Stock Market is a “Casino” and the Courts Must Address This.

On January 29, 2021, Senator Elizabeth Warren wrote a letter to Allison Lee, the Acting Chair of the SEC, to express her concern in the “casino-like” swings in the value of GameStop and other companies.⁶⁷ She stated that this event was a prime example of the “gamesmanship” that impedes upon the “fairly, orderly and efficient” function of the market.⁶⁸ Warren’s letter asked how the SEC intended to address these concerns to prevent future incidents of “potential market manipulation.”⁶⁹ Warren likened the “contest between Wall Street traders... and legions of small-scale investors” to the tail-end of the dot-com boom, stating that this level of speculation raises questions about broader instabilities in the market and the financial systems.⁷⁰

Warren noted that several other publicly traded companies, including AMC; Blackberry; Bed, Bath, and Beyond; Nokia; and Tootsie Roll Industries have also seen huge shifts in their share price that were driven up by internet trading schemes.⁷¹ In Warren’s opinion, the recent GameStop scandal is the latest indication that private hedge funds and institutional investors, as well as small-scale retail investors, are “treating the

⁶⁵ Charles Gasparino, *Sic the SEC? Not so Fast – Case Near Impossible to Prove*, N.Y. Post (Jan. 28, 2021), <https://nypost.com/2021/01/28/will-the-sec-probe-the-gamestop-stock-mania-not-so-fast/>. In a “pump and dump” scheme an investor spreads false or misleading information about a company in an attempt to induce other market participants to buy stock in that company. Once the stock price has been “pumped” up by the increased, but unwarranted, market enthusiasm, the investor will then “dump” their shares at a profit before the market accounts for the false information and returns the stock to a more appropriate baseline price.

⁶⁶ *The Laws That Govern the Securities Industry*, Investor.gov, <https://www.investor.gov/introduction-investing/investing-basics/role-sec/laws-govern-securities-industry> (last visited April 20, 2021).

⁶⁷ Elizabeth Warren, Senator, Letter to Allison H. Lee, Acting Chair, SEC (Jan. 29, 2021), <https://www.warren.senate.gov/imo/media/doc/01.29.2021%20Letter%20from%20Senator%20Warren%20to%20Acting%20Chair%20Lee.pdf>

⁶⁸ Id.

⁶⁹ Id.

⁷⁰ Id.

⁷¹ Id; See also Sebastian Pellejero and Marco Quiroz-Gutierrez, “BlackBerry, AMC and Other Reddit YOLO Favorites That Aren’t GameStop,” Wall Street Journal, (Jan. 26, 2021), <https://www.wsj.com/articles/blackberry-amc-and-otherreddit-yolo-favorites-that-arent-gamestop-11611681716>; Maggie Fitzgerald, “Bed Bath & Beyond, AMC rally with GameStop as little investors squeeze hedge funds in more stocks,” CNBC, (Jan. 25, 2021).

stock market like a casino, giving little consideration to the companies, communities, workers, and consumers” that may be affected by these risky bets.⁷²

There is also a concern that this style of betting has led to a “short-squeeze revolt.” Short-sellers faced losses of up to \$91 billion for the month of January, and much of that is due to shares in other heavily shorted companies being the target of short-squeezers.⁷³ While the strategy used by both hedge fund billionaires and Reddit users to openly manipulate the stock market has clearly been effective, there are significant economic and social costs. The stock market is founded upon consumer confidence and is used as a useful instrument that roughly represents companies’ actual financial values. With such artificial inflation of stock prices, the market efficiency and resource allocation benefits of the stock market is reduced to mere speculation and exaggerated bloating of company valuations.

Furthermore, the SEC is struggling to find a way to take action against these attempts at manipulation, as they are unable to enforce the securities laws without clear signs of fraud. Officials at the SEC are reported to have started watching internet chat rooms for signs of potential market manipulation, there has become a trend towards systematic targeting of highly shorted stocks.⁷⁴ Yet there is little the SEC can do in terms of enforcing its securities laws. It is difficult to prove malfeasance to the level of fraud in the event where a large group of investors simply decide to buy options on a stock at the same time. A lack of accountability suggests an increased tendency from the public suggests that there is something systematically wrong with the way the securities laws are enforced and it is imperative that the courts step up to the challenge to bridge the gap. The judiciary must start openly prohibiting intentional, and financially harmful acts of open-market manipulation from both hedge funds and small-scale investors. Without such action, the stock market is becoming an unregulated casino, where investors are free to make bets on any stock, hence undermining any actual value that is represented by these securities.

⁷² Elizabeth Warren, *Senator, Letter to Allison H. Lee, Acting Chair, SEC* (Jan. 29, 2021), <https://www.warren.senate.gov/imo/media/doc/01.29.2021%20Letter%20from%20Senator%20Warren%20to%20Acting%20Chair%20Lee.pdf>

⁷³ Andrew Ross Sorkin, *Can Anything Stop GameStop*, *The New York Times*, (Jan. 22, 2021), <https://www.nytimes.com/2021/01/27/business/dealbook/reddit-wallstreetbets-gamestop.html>

⁷⁴ *Id.*

II. The Securities Exchange Act of 1934

The Securities Exchange Act of 1934 (“‘34 Act”) created the Securities and Exchange Commission to govern securities transactions on the secondary market in order to ensure greater financial transparency and eliminate fraud or manipulation.⁷⁵ The ‘34 Act was enacted as a response to rampant securities misinformation and irresponsible financial practices that were the chief causes of the 1929 stock market crash and the ensuing Great Depression.⁷⁶ In order to protect investors, Congress created mandatory disclosure processes that were designed to force companies to disclose information that investors would find significant in making investment decisions.⁷⁷ Additionally, Congress stated that the ‘34 Act was drafted because transactions in securities are effected with a “national public interest” making it necessary to provide for “regulation and control.”⁷⁸ Congress gave the SEC the authority as well as the flexibility to create and revise rules in the hope that it could effectively deter manipulative and deceptive practices.

A. Rule 10b-5—The Anti-Fraud Rule and the SEC’s Preferred Enforcement Tool.

In 1948, the SEC began to enact rules against fraud in securities trading under the authority it was given by the ‘34 Act. Section 10b of the ‘34 Act was created to give the SEC the power to promulgate and regulate rules against “manipulative and deceptive practices” in the field of securities trading. Section 10b is broad and complex and includes rules prohibiting fraud and requiring brokers and dealers to disclose certain information in writing to customers before completing a securities transaction.⁷⁹ The most well-known and well-used rule out of Section 10b is Rule 10b-5. Rule 10b-5 is the catch-all provision and widely used as an anti-fraud securities rule, although courts have expanded its reach to beyond blatant fraud. Frequently, the SEC would charge a so-called “pump and dump” scheme under this rule. Rule 10b-5 states that it is unlawful for any

⁷⁵ *Securities Exchange Act of 1934*, Cornell Law School, https://www.law.cornell.edu/wex/securities_exchange_act_of_1934 (last visited April 20, 2021).

⁷⁶ *Id.*

⁷⁷ *Id.*

⁷⁸ *Id.*

⁷⁹ *Securities and Exchange Act Rule 10b*, FindLaw, <https://www.findlaw.com/consumer/securities-law/securities-and-exchange-act-rule-10b.html> (last visited April 20, 2021).

individual to use the stock market to employ any “device, scheme, or artifice to defraud,” to “make any untrue statement of material fact,” or “to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.”⁸⁰

B. Traditional Market Manipulation Under Rule 10b-5

Traditional market manipulation encapsulates activity that is inherently illegal and involves a “bad act.” In order to manipulate the market, there generally needs to be: (1) the manipulator moving the price of the security; and (2) the manipulator selling at a higher price than his purchase price, plus transaction costs.⁸¹ The Supreme Court has defined “manipulative conduct” as any conduct that is “intended to mislead investors by artificially affecting market activity.”⁸² Manipulation connotes the “intentional or willful conduct” designed to deceive or defraud investors by controlling or artificially affecting the price of securities.⁸³ Furthermore, there is a six-part test promulgated by the court, in which to state a claim of market manipulation under Section 10(b) and Rule 10b-5, a plaintiff must allege: (1) manipulative acts; (2) damage; (3) caused by reliance on an assumption of an efficient market free of manipulation; (4) scienter; (5) in connection with the purchase or sale of securities; (6) furthered by the defendant’s use of the mails or any facility of a national securities exchange.⁸⁴

The court has stated that the essence of “manipulation” is “deception of investors into believing the prices at which they purchase and sell securities are determined by the natural interplay of supply and demand.”⁸⁵ In order to determine whether such activity falls outside of that “natural interplay”, the courts generally ask whether a transaction “sends a false pricing signal to the market.”⁸⁶ Lastly, to be manipulative, the court has stated that the market activity in question must “involve misrepresentation or

⁸⁰ 17 C.F.R. § 240.10b-5(a)–(c)

⁸¹ See Maxwell K. Multer, *Open-Market Manipulation Under SEC Rule 10b-5 and its Analogues: Inappropriate Distinctions, Judicial Disagreement and Case Study: FERC’s Anti-Manipulation Rule*, 39 Sec. Reg. L.J. 97, 100 (2011); Keller, *supra* note 29, at 335, 348.

⁸² See *Santa Fe Indus. v. Green*, 430 U.S. 462, 476 (1977).

⁸³ *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 476 (1977).

⁸⁴ *Onel v. Top Ships, Inc.*, 806 Fed. App’x. 64, 66 (2d Cir. 2020) (quoting *ATSI Commc’ns., Inc. v. Shaar Fund, Ltd.*, 493 F.3d 87, 101 (2d Cir. 2007)) (internal quotation marks omitted).

⁸⁵ *Id.*

⁸⁶ *Wilson v. Merrill Lynch & Co.*, 671 F. 3d 120, 129 (quoting *Gurary v. Winehouse*, 190 F. 3d 37, 45 (2d Cir. 1999)).

nondisclosure.”⁸⁷ The market is not misled when a transaction’s terms are fully disclosed. In other words, a claim of market manipulation requires the claimant to show that the defendants’ actions were intended to mislead the investors about the price of the securities, as well as an allegation that the defendants’ actions included a nondisclosure or misrepresentation.

III. Circuits Split on Open Market Manipulation

It is unclear to the courts as to whether Rule 10b-5 regulates open market manipulation, and circuits have been split on the legality of this act. In contrast to the traditional theory of market manipulation articulated above, open market manipulation is accomplished without employing any objectively “bad behavior.”⁸⁸ Some courts have conceptually separated what can be characterized as traditional from an alleged “open market manipulation.”⁸⁹ Open market manipulation refers to a manipulative scheme where the alleged scheme is accomplished through the use of “facially legitimate open market transactions.”⁹⁰ The manipulator has not engaged in any conduct that is inherently illegal, such as fictitious transactions, or false reporting.⁹¹ However, these transactions have both manipulative intent and effect and lead to intentional price-movement and profit capture.⁹²

These schemes involve price moving trades that go largely undetected and unprosecuted, as they are accomplished through unremarkable purchases, sales, or short sales. These transactions may be divided into two types: (1) trade-based manipulations and (2) contract based manipulations.⁹³ A trade based manipulation involves a manipulator attempting to increase the price of a security by trading, and to sell at a profit before the price falls back to its “correct” level.⁹⁴ This is achieved without any illegal

⁸⁷ Id.

⁸⁸ See Maxwell K. Multer, *Open-Market Manipulation Under SEC Rule 10b-5 and its Analogues: Inappropriate Distinctions, Judicial Disagreement and Case Study: FERC’s Anti-Manipulation Rule*, 39 Sec. Reg. L.J. 97, 100 (2011).

⁸⁹ See e.g., *U.S. v. Mulheren*, 938 F.2d 364, 370–71 (2d Cir. 1991).

⁹⁰ See Maxwell K. Multer, *Open-Market Manipulation Under SEC Rule 10b-5 and its Analogues: Inappropriate Distinctions, Judicial Disagreement and Case Study: FERC’s Anti-Manipulation Rule*, 39 Sec. Reg. L.J. 97, 100 (2011).

⁹¹ Id.

⁹² Id.

⁹³ Id.

⁹⁴ Id.

acts, and are historically difficult to trace.⁹⁵ A contract based manipulation is achieved through making price-moving trades that are intended to trigger or benefit some other contractual right--such as an executive receiving a bonus if the share price reaches a specific level.⁹⁶

Circuits have been split on the legality of these open market manipulations, and many courts have been reluctant to impose liability under Rule 10b-5, as these transactions are facially legitimate. As discussed below, the Second and Third Circuits have categorically excluded open market manipulation from the grasp of Rule 10b-5.⁹⁷ Other courts have disagreed with this strict analysis and hold that traders can manipulate the market and violate Rule 10b-5 without blatant fraud or misrepresentations. The D.C. Circuit has held that even legitimate trades can be illegal solely because of the actor's "purpose."⁹⁸

A. *U.S. v. Mulheren* and the Requirement of Subjective Intent.

In this Second Circuit case, the court found that a manipulation of securities in violation with Rule 10b-5 occurs when the purpose of the transaction is *solely* to affect the price of a security.⁹⁹ John A. Mulheren Jr., the chief trader and general partner of Jamie Securities Co., was charged in a 42-count indictment, alleging that he conspired and manipulated the price of the stock of Gulf & Western Industries, Inc. ("G&W") in violation of Rule 10b-5.¹⁰⁰ Mulheren purchased 75,000 shares of G&W on the open market, after several meetings with prominent investors, as well as the chairman of G&W.¹⁰¹ The purchase caused the stock price to rise to \$45 per share.¹⁰² Despite this, slow trading led to G&W to close at \$43 ⁵/₈ per share, causing Mulheren to lose \$64,406.¹⁰³

⁹⁵ Id.

⁹⁶ Id.

⁹⁷ See, e.g., GFL Advantage Fund, Ltd. v. Colkitt, 272 F.3d 189 (3d Cir. 2001); see also, U.S. v. Mulheren, 938 F.2d 364, 370–71 (2d Cir. 1991).

⁹⁸ See U.S. v. Mulheren, 938 F.2d 364, 367 (2d Cir. 1991).

⁹⁹ Id.

¹⁰⁰ Id.

¹⁰¹ Id.

¹⁰² Id. at 368.

¹⁰³ Id.

The government argued that when an investor who is neither a fiduciary nor an inside engages in a securities transaction in the open market with the sole intent to affect the price of the security, the transaction is manipulative and violates Rule 10b-5.¹⁰⁴ In adopting this view, the court stated that the issue then became one of Mulheren's subjective intent, and that the government must demonstrate that Mulheren purchased the shares with the intent to raise its price, rather than the intent to invest.¹⁰⁵

The court ultimately found that the government failed to carry this burden, reasoning that the government relied on speculation reported in the media and rumors floating on Wall Street.¹⁰⁶ There was no evidence to suggest that Mulheren read these articles or heard the rumors, and Mulheren testified of not knowing of their existence. Furthermore, the court found that knowledge of a rumor on Wall Street "can hardly substitute for knowledge of a fact."¹⁰⁷ Furthermore, the court stated that Mulheren suffered a loss of \$65,000 in this transaction, and that it can be inferred that one who is manipulating stock prices would not incur such a loss.¹⁰⁸ The court noted in dicta that "none of the traditional badges of manipulation are present in this case... [as Mulheren] conspicuously purchased the shares... in the open market."¹⁰⁹

B. GFL Advantage Fund, Ltd. v. Colkitt and the Requirement of Inaccurate Information.

In this Third Circuit case, the court strictly held that no facially legal securities trades can create legal liability, even where the trades clearly manipulate the market.¹¹⁰ In this case, Douglas Colkitt obtained a loan of \$3,000,000 from GFL, with the note that GFL had the right after 30 days of the date of the note to exchange up to \$1.5 million of its outstanding principal for shares of National Medical stock held by Colkitt at an exchange rate of 82% of the average market price.¹¹¹ GFL then entered into another transaction with Colkitt for a \$10,000,000 loan, with a similar note that stated that GFL could convert the debt into shares of Colkitt's other business, EquiMed Inc., at an

¹⁰⁴ Id.

¹⁰⁵ Id.

¹⁰⁶ Id.

¹⁰⁷ Id. at 639.

¹⁰⁸ Id.

¹⁰⁹ Id. at 370-371.

¹¹⁰ *GFL Advantage Fund, Ltd. v. Colkitt*, 272 F.3d 189, 194 (3d Cir. 2001).

¹¹¹ Id.

exchange rate of 83% of the average market price.¹¹² GFL then converted its outstanding principal into EquiMed stock, receiving 150,555 shares at an exchange rate of \$3.72.¹¹³

Unknown to Colkitt at the time, GFL began to short sell National Medical, as well as EquiMed shares. GFL claimed that it engaged in short sales of these stocks as a hedging strategy against “delivery risk”, and that it wanted to protect itself in the event that the price of the stock declined further after GFL made the exchange request but before GFL was able to sell the shares.¹¹⁴ Colkitt, on the other hand, argued that GFL sold National Medical and EquiMed shares short in an effort to depress the prices of the stock.¹¹⁵ Colkitt contended that the market price of National Medical dropped 17.5% between GFL’s first and last short sales of National Medical stock, and the market price of EquiMed declined by 18.5 % between GFL’s first short sale and first exchange demand.¹¹⁶

The court referred to the United States Supreme Court’s construction of a Section 10(b) market manipulation claim, stating that the Supreme Court has indicated that market manipulation “generally refers to practices, such as wash sales, matched orders, or rigged prices that are intended to mislead investors by artificially affecting market activity.”¹¹⁷ The court stated that Colkitt need not prove that GFL’s manipulative conduct *actually* depressed the prices, although any damages Colkitt would be entitled to recover under Section 10(b) and Rule 10b-5 would be contingent on proving that GFL’s conduct actually depressed prices.¹¹⁸ However, the court stated that in order to prove a manipulation in violation of Rule 10b-5, Colkitt must present evidence that “(1) in connection with the purchase or sale of securities, (2) GFL engaged in *deceptive* or *manipulative* conduct by injecting inaccurate information into the marketplace or creating a false impression of supply and demand for the security (3) for the purpose of artificially depressing or inflating the price of the security.”¹¹⁹

¹¹² Id. at 195.

¹¹³ Id.

¹¹⁴ Id. at 196.

¹¹⁵ Id.

¹¹⁶ Id.

¹¹⁷ Id. at 205 (citing *Santa Fe Indus. v. Green*, 430 U.S. 462, 476 (1977)).

¹¹⁸ Id. at 206.

¹¹⁹ Id. at 207.

The court held that Colkitt failed to present any evidence that GFL did anything but lawfully engage in short sales of National Medical and EquiMed stock.¹²⁰ The court reasoned that the fact that “these short sales may have contributed to a decline in the stocks’ prices is not evidence of deceptive or manipulative conduct, for there is no reason to believe these prices were depressed artificially.”¹²¹ Ultimately, the court found that despite whether the manipulation is achieved through deceptive trading activities or deceptive statements as to the corporation’s value, the “essential element of the claim is that *inaccurate* information is being injected into the marketplace.”¹²² Without such inaccurate information, GFL was not guilty of market manipulation in violation of Rule 10b-5.

C. The D.C. Circuit Split—Markowski v. SEC and the *Chevron Doctrine* Analysis.

In this D.C. Circuit Case, the SEC took the position that intent alone is enough for a facially legal open market transaction to constitute a violation of Rule 10b-5 and section 10(b).¹²³ Michael Markowski was the chairman, CEO, and majority shareholder of Global America, Inc., (“Global”) who underwrote an initial public offering (“IPO”) of Mountaintop Corporation.¹²⁴ After the IPO, Global owned a vast majority of the market for Mountaintop securities, accounting for both purchase and sale volume. The SEC alleged that from the IPO in June 1990, until Global’s closing in January 1991, Global supported the price of Mountaintop securities.¹²⁵ The SEC claimed that this support was in two ways: (1) Global maintained high bid prices for Mountaintop securities, and (2) Global absorbed all unwanted securities into inventory, preventing sales from depressing market prices.¹²⁶ However, these efforts were unsuccessful, and led Global to close down as of January 1991, and Mountaintop price dropped up to 75% in one day.¹²⁷ The SEC concluded that even though Global’s activity was effectuated through open market transactions, this violated Rule 10b-5.

¹²⁰ Id.

¹²¹ Id.

¹²² Id. at 205 (quoting *In re Olympia Brewing Co. Secs. Litig.*, 613 F. Supp. 1286 (N.D. Ill. 1985)).

¹²³ *Markowski v. S.E.C.*, 274 F.3d 525, 529 (D.C. Cir. 2001).

¹²⁴ Id. at 527.

¹²⁵ Id.

¹²⁶ Id.

¹²⁷ Id.

On the other hand, Global argued that because their bids and trades were “real,” involving real customers and real transactions, they cannot be constituted as unlawful manipulation.¹²⁸ The court agreed that the activities were unlike schemes that involved fraudulent devices, such as “wash sales” or “matched sales.”¹²⁹ The court noted that without such fictitious transactions, it may be difficult to separate a “manipulative investor from one who is simply over-enthusiastic, a true believer in the object of investment.”¹³⁰ The court realized that such an investor may amass huge inventories and place high bids, even though there is no data supporting the estimate of the stock’s value.¹³¹ However, the court stated that given the ambiguous nature of figuring out an investor’s “intent” was for an investment purpose or to affect the price of the security, the court is unable to find the SEC’s interpretation of “intent” to be unreasonable.¹³² The court referred to the administrative law principal of the *Chevron Doctrine*, stating that courts should accept an agency’s reasonable statutory interpretation.¹³³ The court found that Congress clearly endorsed sanctions against manipulations, within the phrase “manipulative... device” in the drafting of Section 10(b).¹³⁴ Furthermore, the court stated that the SEC’s interpretation is consistent with its rules governing an issuer’s purchase of its own securities. Giving deference to the SEC, the court ruled that the SEC’s position was not unreasonable, and that Global’s facially legitimate transactions are illegal solely because of the investor’s purpose.¹³⁵

IV. Reddit’s GameStop Scandal Likely Constitutes Open Market Manipulation and Harms the Economy.

The Reddit saga demonstrates that courts should follow the D.C. Circuit’s footsteps in prohibiting open market manipulation in certain circumstances under Rule 10b-5. Redditors and other GameStop stock purchasers intentionally manipulated the market—either to punish hedge fund short sellers, to make a quick profit, or both. The

¹²⁸ Id.

¹²⁹ Id.

¹³⁰ Id. at 528.

¹³¹ Id.

¹³² Id.

¹³³ Id. (citing Section 9(a)(2) of the Securities Exchange Act, 15 U.S.C. § 78i(a)(2); *Chevron U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837, 843–44 (1984)).

¹³⁴ Id.

¹³⁵ Id.

casino-style “investing” in GameStop and similar corporations likely constitutes an illegal open market manipulation that harms the economy. Under the *Mulheren* analysis, Reddit users possessed the subjective intent of wanting to harm hedge fund billionaires, and/or make money. From the comments and general attitude of Redditors, the court may find that this intent is more than mere speculation or based on rumors. Under the *GFL* analysis, the court may find that Redditors and hedge fund investors did not act fraudulently by injecting inaccurate information into the marketplace for the purpose of artificially inflating or depressing the price of the security. However, the fact that Redditors and institutional investors had the intent to manipulate and artificially change the price of GME should be sufficient to constitute open market manipulation that is in violation of Rule 10b-5.

As stated in *Markowski*, the *Chevron Doctrine* gives the SEC the authority to interpret its own statutes, and courts should give deference to the agency.¹³⁶ Furthermore, the legislature should realize that such schemes pollute the market and effectuate a disconnect between actual value and disoriented inflations that are based on trivial information and do not constitute valuable information. The purpose of the stock market is to accurately state the value of companies in order to allocate scarce economic resources, and distorted market prices are contrary to this purpose.¹³⁷ Increases in market volatility suggests that stock prices are artificial, and thereby reduces consumer confidence in the wake of a pandemic where such consumer confidence is already at a low.¹³⁸

Refusing to hold these market manipulators accountable exacerbates these issues. Courts will essentially incentivize these kinds of manipulations by refusing to take action, as just about anyone with a large enough following can bump up prices for a quick profit at the expense of the public. Another consequence from the GameStop scandal is that there are ultimately losers on the other side of the coin. Large hedge funds lost billions of dollars in short bets, while many small-scale investors still continued to purchase GME at its overvalued price. Many of the current stock purchasers—a vast majority of whom are

¹³⁶ *Markowski*, 274 F.3d at 529.

¹³⁷ Merritt B. Fox, Lawrence R. Glosten, & Gabriel V. Rauterberg, *Stock Market Manipulation and its Regulation*, 25 *Yale J. Reg.* 67, 118 (2018).

¹³⁸ See, e.g., Paul Krugman, *Stocks Are Soaring. So Is Misery*, N.Y. Times: Opinion (Aug. 20, 2020), <https://www.nytimes.com/2020/08/20/opinion/stock-market-unemployment.html>.

unprofessional and small-scaled, will lose money as GME falls back down to its normal valuation. The eventual outcome of whether this will create additional financial panic or impose danger on small market investors who cannot afford to lose any money is purely speculative at this point.

CONCLUSION

The frenzy in trading GameStop shares in January 2021 was one of the first of its kind, and poses many unanswered questions for the judiciary to answer. Reddit users' artificial inflation of prices likely constitutes market manipulation that should be prosecuted. Although circuits have been split on what exactly constitutes open market manipulation, it is clear that the securities laws were not written to permit large groups of people to purchase stocks in a facially legitimate transaction and consequently inflate the prices sky-high. The primary purpose of the securities laws is to protect investors, and allowing such conduct without accountability will only increase the harm to both the public and investors. The GameStop saga demonstrated that the current application of Rule 10b-5 that requires overt fraud to prove illegal market manipulation is lacking in nature and allows many harmful acts to fall through the cracks. The SEC and the courts must categorize collective purchasing of securities without the intent to invest as fraud and move swiftly to impose penalties. Otherwise, investors will only be incentivized to conduct similar open-market schemes in the future and create a stock market that is unstable and inefficient for the public.