No. 11-1085

IN THE
Supreme Court of the United States

AMGEN INC., ET AL.,
Petitioners,
v.
CONNECTICUT RETIREMENT PLANS AND TRUST FUNDS,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF *AMICUS CURIAE* OF SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF THE PETITIONERS

IRA D. HAMMERMAN
KEVIN M. CARROL
Securities Industry and Financial Markets Association
1101 New York Ave, N.W.
Washington, D.C. 20005
(202) 962-7382

WILLIAM F. SULLIVAN
(*counsel of record*)
HOWARD M. PRIVETTE
BARRY G. SHER
PETER M. STONE
STEPHEN B. KINNAIRD
JOHN S. DURRANT
Paul Hastings LLP
515 S. Flower Street, 25th Fl.
Los Angeles, California 90071
(213) 683-6000
williamsullivan@paulhastings.com

(Additional counsel are listed on the inside cover page)

75 East 55th Street
New York, NY 10022
(212) 318-6000

1117 S. California Avenue
Palo Alto, California 94304
(650) 320-1800

875 15th Street, N.W.
Washington, DC 20005
(202) 551-1700

Counsel for *Amicus Curiae*
Securities Industry and
Financial Markets Association

TABLE OF CONTENTS

Page

TABLE OF CONTENTS
(continued)

Page

TABLE OF AUTHORITIES

Page(s)

CASES

TABLE OF AUTHORITIES
(continued)

Page(s)

TABLE OF AUTHORITIES
(continued)

Page(s)

TABLE OF AUTHORITIES
(continued)

Page(s)

TABLE OF AUTHORITIES
(continued)

Page(s)

STATUTES

TABLE OF AUTHORITIES
(continued)

Page(s)

OTHER AUTHORITIES

TABLE OF AUTHORITIES
(continued)

Page(s)

STATEMENT OF INTEREST

The Securities Industry and Financial Markets Association ("SIFMA") is a securities industry trade association representing the interests of hundreds of securities firms, banks, and asset managers.[1] SIFMA's mission is to support a strong financial industry while promoting investor opportunity, capital formation, job creation, economic growth, and trust and confidence in the financial markets. SIFMA has offices in New York and Washington, D.C. and is the United States regional member of the Global Financial Markets Association. SIFMA regularly files *amicus curiae* briefs in cases that raise matters of vital concern to participants in the securities industry.

SIFMA has appeared before this Court as amicus curiae in many cases involving issues arising under the federal securities laws, most recently in *Credit Suisse Securities (USA) LLC v. Simmonds*, 132 S. Ct. 1414 (2012) (considering tolling under Section 16(b) of the Securities Exchange Act of 1934); *Erica P. John Fund, Inc. v. Halliburton Co.*, 131 S. Ct. 2179 (2011) (holding that plaintiffs need not prove loss causation to obtain class certification under the fraud-on-the-market theory of reliance); *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309 (2011)

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[1] Pursuant to Supreme Court Rule 37.6, counsel for *amicus* certifies that no counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus* made such a monetary contribution. Letters from the parties consenting to the filing of all *amicus* briefs have been filed with the Clerk of the Court.

(involving pleading standard for materiality in private securities fraud claim), *Morrison v. Nat'l Austl. Bank Ltd.*, 130 S. Ct. 2869 (2010) (extraterritorial application of anti-fraud provisions of federal securities laws), *Merck & Co. v. Reynolds*, 130 S. Ct. 1784 (2010) (statute of limitations for bringing private securities fraud claim), and *Jones v. Harris Associates L.P.*, 130 S. Ct. 1418 (2010) (breach of fiduciary duty under the Investment Company Act of 1940).

This case involves important issues regarding liability under the federal securities laws for misrepresentations in connection with public market transactions and the appropriate standards governing the adjudication of private securities claims under class action procedure. These issues are directly relevant to SIFMA's mission of promoting fair and efficient markets and a strong financial services industry. Resolution of these issues could have a significant effect on SIFMA's members.

SUMMARY OF ARGUMENT

Class certification requires that the class proponent demonstrate strict compliance with Rule 23 of the Federal Rules of Civil Procedure ("Rule 23"). The overwhelming majority of plaintiffs seeking class status under Rule 23(b)(3) in federal securities actions attempt to invoke the rebuttable presumption of reliance derived from the fraud-on-the-market theory. First adopted by this Court in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), the Court has articulated four prerequisites that must be established to invoke the fraud-on-the-market

presumption: (i) that the defendant made public misrepresentations; (ii) that the misrepresentations were material; (iii) that the securities traded on an efficient market; and (iv) that the plaintiff traded the shares between the time the misrepresentations were made and the time the truth was revealed. *See id.* at 248 n.27. This case concerns the second of these prerequisites – materiality.

Under the fraud-on-the-market doctrine, immaterial statements do not impact the market price of a security and, therefore, investors do not indirectly rely upon those immaterial statements through reliance on the market price. Given the Court's strong direction to apply a rigorous analysis for determining Rule 23 compliance, the clear language of *Basic*, and the substantial *in terrorem* effects of improvidently certifying a class, SIFMA respectfully submits that the Court should require a plaintiff to establish materiality at the class certification stage or, at a minimum, permit a defendant the opportunity to rebut the presumption of reliance.

The requirement that a plaintiff establish materiality at class certification is not unduly burdensome. There are numerous practicable ways to demonstrate materiality. Although the Court has held that materiality is not suitable to a bright-line rule determination, materiality may be established through at least two practical and regularly used methods. A plaintiff may analyze the total mix of information available to market participants through review of publicly available information, including issuer disclosures, press reports, and/or reports of industry analysts. Alternatively, or in conjunction

with a review of the total mix of information, a plaintiff may submit evidence of an appropriate event study regarding the impact of an alleged misrepresentation on the market price of the security.

Moreover, there are compelling policy reasons to require the establishment of materiality at class certification. This Court and lower federal courts have acknowledged the "*in terrorem*" effects that certifying a class has on a defendant with supposed "deep pockets." *See, e.g.*, *Coopers & Lybrand v. Livesay*, 437 U.S. 463, 476 (1978). Such effects are particularly pronounced in securities cases, where amounts in controversy can be very large. A rigorous analysis of materiality at class certification allows district courts to efficiently and fairly manage cases that are not suitable for class treatment, which will ameliorate the problem of *in terrorem* settlements in the securities context.

Regardless of the method of proof used by a plaintiff, a defendant should be permitted the opportunity to rebut the materiality of alleged misstatements with evidence supported by an analysis of the total mix of information or an event study. Without consideration of such evidence a district court cannot establish a proper class period in a securities case.

Allowing a class to be certified notwithstanding the availability of dispositive evidence refuting a claim of materiality, would unnecessarily increase the costs of defending meritless litigation and exacerbate the problem of *in terrorem* settlements of securities cases.

ARGUMENT

I. SUMMARY OF THE FRAUD-ON-THE-MARKET THEORY

A. Class Certification Requirements

The Court has long recognized that the class action is "an exception to the usual rule that litigation is conducted by and on behalf of the individual named parties only." *Califano v. Yamasaki*, 442 U.S. 682, 700-702 (1979). To permit a class action to proceed, a court must determine that the class representative "possess[es] the same interest and suffer[s] the same injury . . ." as the putative class members. *E. Tex. Motor Freight Sys., Inc. v. Rodriguez*, 431 U.S. 395, 403 (1977) (internal quotations omitted).

The burden is on the class proponent to demonstrate that all of the requirements are met under Rule 23. *See Wal-Mart Stores, Inc. v. Dukes*, 131 S. Ct. 2541, 2548 (2011).[2] Rule 23 is not a pleading standard; rather, it requires the party seeking class certification to *prove* compliance with the rule. *Id.* at 2550. A class will only be certified if the trial court determines, after a "rigorous analysis," that all Rule 23 requirements are met. *Id.* Therefore, "'it may be necessary for the court to probe behind the pleadings before coming to rest on the

[2] To properly certify a class, the proponent must meet all the requirements of Rule 23(a) – numerosity, commonality, typicality, and adequacy of representation – as well as one of the requirements of Rule 23(b). *See Dukes*, 131 S. Ct. at 2548.

certification question[.]'" *Id.* at 2551 (quoting *Gen. Tel. Co. of the Sw. v. Falcon*, 457 U.S. 147, 160 (1982)).[3]

B. Class Certification Requirements in Putative Securities Class Actions

In *Basic*, the Court addressed whether plaintiffs seeking class certification for claims brought under Rule 10(b) of the Securities Exchange Act of 1934 can make a class-wide showing of reliance. *Basic*, 485 U.S. at 242 ("Requiring proof of individualized reliance from each member of the proposed plaintiff class effectively would have prevented respondents from proceeding with a class action."). Recognizing difficulties in establishing individual reliance, the Court adopted a presumption allowing a plaintiff to demonstrate indirect reliance through the "fraud-on-the-market" theory. *Basic*, 485 U.S. at 247. The fraud-on-the-market presumption holds that "the market price of shares traded on well-developed markets reflects all publicly available information,

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[3] The vast majority of securities class action proponents seek certification under Rule 23(b)(3), which requires that "the court finds that the questions of law or fact common to class members predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fairly and efficiently adjudicating of the controversy." Fed. R. Civ. P. 23(b)(3) (emphasis added). This Court has held that the inquiry into whether common questions predominate over individual claims is more demanding than determining the commonality prerequisite in Rule 23(a)(2). In *Dukes*, the majority opinion makes the distinction that Rule 23(b)(3) concerns whether common questions *predominate* over individual claims, whereas a Rule 23(a)(2) determination is satisfied if there is even a *single* common question. 131 S. Ct. at 2556.

and, hence, any material misrepresentations." *Id.* at 246.

In a putative securities class action involving allegations of misrepresentations, a court's rigorous analysis often turns upon the element of reliance. By extension, this usually means a focus on the fraud-on-the-market presumption. Although *Basic* did not establish a strict test to invoke the presumption of reliance, it did recognize a set of threshold requirements: (i) that the defendant made public misrepresentations; (ii) that the misrepresentations were material; (iii) that the securities traded on an efficient market; and (iv) that the plaintiff traded the shares between the time the misrepresentations were made and the time the truth was revealed. *See id.* at 248 n.27; *see also Halliburton*, 131 S. Ct. at 2185 ("It is undisputed that securities fraud plaintiffs must prove certain things in order to invoke *Basic's* rebuttable presumption of reliance.").

Since *Basic,* a circuit split has emerged regarding whether for class certification purposes materiality is an essential element to the fraud-on-the-market presumption, which is more fully discussed in Petitioners' merits brief. *Basic*, however, set the guidepost for how lower courts should interpret the fraud-on-the-market doctrine: "An investor who buys or sells stock at the price set by the market does so in reliance on the integrity of that price. Because most publicly available information is reflected in market price, an investor's reliance on any public *material misrepresentations*, therefore, may be presumed." *Basic*, 485 U.S. at 247 (emphasis added); *see also Halliburton*, 131 S. Ct. at 2185 (same). To invoke the

fraud-on-the-market presumption, then, the alleged public misstatement must be material in order to distort the market price.

II. POLICY PROBLEMS WITH CLASS CERTIFICATION BASED SOLELY ON ALLEGATIONS OF MATERIALITY

Requiring only *allegations* of materiality at class certification would substantially hinder a defendant's ability to dispute non-meritorious claims before being subjected to overwhelming settlement pressure. This Court and lower federal courts have acknowledged the "*in terrorem*" effects of certifying a class on a defendant with supposed "deep pockets." *See, e.g.*, *Coopers & Lybrand*, 437 U.S. at 476 ("Certification of a large class may so increase the defendant's potential damages liability and litigation costs that he may find it economically prudent to settle and to abandon a meritorious defense.").[4]

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[4] *See also AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1752 (2011) (recognizing the *in terrorem* effects of class actions); *Bell Atl. Corp. v. Twombly,* 550 U.S. 544, 546 (2007) (same); *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 347 (2005) (same); *Regents of the Univ. of Cal. V. Credit Suisse First Bos. (USA), Inc.*, 482 F.3d 372, 379 (5th Cir. 2007) (certification is often "the backbreaking decision that places insurmountable pressure on a defendant to settle, even where the defendant has a good chance of succeeding on the merits"); *Kohen v. Pac. Inv. Mgmt. Co. LLC & PIMCO Funds*, 571 F.3d 672, 677-78 (7th Cir. 2009) (noting *in terrorem* effects on securities class action defendant); *In re Vantive Corp. Sec. Litig.*, 283 F.3d 1079, 1092 (9th Cir. 2002) (noting that lengthening the class period to 63 weeks permitted plaintiffs to "sweep as many stock sales into their [damages] totals as possible . . ."), *overruled on other grounds by S. Ferry LP v. Killinger*, 542 F.3d 776, 784 (9th Cir. 2008); *In re Silicon Graphics Inc. Sec. Litig.*, 183 F.3d 970, 978 (9th Cir. 1999)

A rigorous analysis of materiality – an antecedent of the judicially created fraud-on-the-market doctrine – at class certification allows district courts to efficiently and fairly manage cases that are not suitable for class treatment. It also ameliorates the problem of *in terrorem* settlements prevalent in the securities context.

A. Improvident Class Certification in Securities Cases Imposes Significant Costs on SIFMA Members and All Participants in the Public Securities Markets

As this Court and the circuit courts have held, a defendant in a class action can face the prospect of financial ruin in the face of a certified class of plaintiffs who may not have legally meritorious claims. The benefits of class-wide relief must be balanced against the enormity of pressure a defendant encounters to settle class claims. *See In re Rhone-Poulenc Rorer, Inc.*, 51 F.3d 1293, 1297-99 (7th Cir. 1995) (discussion by Judge Posner of *in terrorem* effects of class actions in mass torts). These "*in terrorem*" effects are particularly prevalent in securities class action lawsuits. *In re Silicon Graphics Inc. Sec. Litig.*, 183 F.3d at 978 (examining the history of the Private Securities Litigation

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(noting that Congress enacted the PSLRA in part to prevent abusive securities fraud class actions designed "'to impose costs so burdensome that it [was] often economical for the victimized party to settle'" (alteration in original) (quoting H.R. Rep. No. 104-369, at 41 (1995) (Conf. Rep.), reprinted in 1995 U.S.C.C.A.N. 730, 730)).

Reform Act of 1995 ("PSLRA") and the reasons for enacting heightened pleading requirements); *see also Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 740 (1975) (noting securities class actions have a settlement value to plaintiffs out of proportion to success on the merits). In *Regents of the Univ. of Cal.*, for example, the Fifth Circuit closely analyzed the district court's certification of a class that alleged damages of nearly $40 billion related to the collapse of Enron and reversed and remanded the case. 482 F.3d at 379, 394. The court noted that class certification is often the "backbreaking decision that places insurmountable pressure on a defendant to settle[.]" *Id.* at 379. The court in that case found that plaintiff failed to properly invoke the rebuttable presumption of reliance. *Id.* at 382-83.

B. The "*In Terrorem*" Impact of Class Certification Nearly Always Leads to Settlement

Class certification increases the likelihood of *in terrorem* settlements.[5] Since the enactment of the PSLRA, only 29 securities class action cases have been adjudicated after a jury trial as compared to over 3,800 filings.[6] Indeed, less than one-half of one

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[5] Thomas E. Willging & Shannon R. Weathman, *An Empirical Examination of Attorneys' Choice of Forum in Class Action Litigation*, Federal Judicial Center, at 50 (2005) (in one study, the *in terrorem* effects led to nearly 90% of all *certified class actions* in the study sample to settlement).

[6] Dr. Jordan Milev, Dr. John Montgomery, Robert Patton and Svetlana Starykh, *Recent Trends In Securities Class Action Litigation: 2011 Year-End Review*, NERA Economic Consulting, Dec. 21, 2011, at 12 (statistics are through December 21, 2011).

percent of all securities class actions proceed to trial on the merits.[7] In 2011, only one case, *In re Homestore.com, Inc.*, went to trial, and only against one of many defendants where all other defendants had previously settled.[8] Despite so few securities cases reaching trial, the mean settlement for securities actions was $31 million in 2011.[9]

Faced with staggering potential losses, securities class action defendants settle even non-meritorious claims rather than risk financial disaster. *See Eisen v. Carlisle & Jacquelin*, 479 F.2d 1005, 1019 (2d Cir. 1973), *vacated*, 417 U.S. 156 (1974) (noting that defendants in large class actions settle in the face of large damages "as the alternative to complete ruin and disaster, irrespective of the merits of the claim").

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[7] *See id.*

[8] *Id.* at p. 14.

[9] *Id.* at p. 17.

III. IT IS REASONABLE, PRACTICABLE, AND NOT UNDULY BURDENSOME TO REQUIRE A PLAINTIFF TO ESTABLISH MATERIALITY AT CLASS CERTIFICATION

A. Materiality Is Necessary To Determine Predominance Under Rule 23 And To Define the Class Period Properly

Rule 23(b)(3) requires that common questions of law or fact predominate over questions subject to individual determination. *Basic* recognized a rebuttable presumption permitting a plaintiff to indirectly rely on integrity in the market price, incorporating all public material information in an efficient market. *See Basic*, 485 U.S. at 242. First adopted by this Court in *Basic*, and then most recently addressed in *Halliburton*, the fraud-on-the-market hypothesis is founded on the premise that in an "open and developed securities market, the price of a company's stock is determined by the *available material information* regarding the company and its business . . . ." *Basic*, 485 U.S. at 242 (emphasis added). The Court has therefore made clear that the necessary antecedents of the fraud-on-the-market theory include: (1) materiality of the alleged misstatement and (2) an efficient market. *See id.* at 242 (internal quotations omitted); *see also Halliburton*, 131 S. Ct. at 2186 ("investor presumptively relies on a misrepresentation so long as it was reflected in the market price").

A statement is "material" if there is a substantial likelihood that an accurate disclosure would have

been viewed by the reasonable investor as having significantly altered the total mix of information made available. *See Matrixx*, 131 S. Ct. at 1318.

Proof of materiality is also necessary in many cases to establish a proper class period. *See, e.g.*, *In re Federal Nat'l Mortg. Ass'n Secs., Derivatives, & "ERISA" Litig.*, 247 F.R.D. 32, 38 (D.D.C. 2008) ("whether the fraud-on-the-market presumption applies as a matter of law is essential for determining the duration of the class period"). In considering what period of time a misrepresentation defrauded the market, courts must consider whether and when the material facts (the truth on the market) emerged. *See Basic* 485 U.S. at 248 n.27 (requirements for the invocation of the fraud-on-the-market theory include "that the plaintiff traded the shares between the time the misrepresentations were made and the time the truth was revealed"). Absent proof that a material misstatement entered the market and then the truth was revealed, a court simply cannot determine (1) the proper class period or (2) the typicality of class members' claims as required under Rule 23(a)(3).[10]

[10] *See, e.g.*, *Maiman v. Talbott,* No. SACV 09-00012 AG (AN), 2011 U.S. Dist. LEXIS 98243, at *20 (C.D. Cal. Aug. 29, 2011) ("Because it would be impossible for the Court to determine whether Plaintiffs satisfy Rule 23(a)(3) without examining the parties' arguments concerning the appropriate end date of the class period, the court turns to those arguments now.").

B. Materiality May Be Determined Through an Analysis of How a Reasonable Investor Would Have Viewed a Misrepresentation In the Context of the "Total Mix" of Publicly Available Information.

Although predominantly a case-by-case determination not well suited for a bright-line rule, a plaintiff could attempt to ascertain materiality through (1) an analysis of the total mix of information available to the market; and/or (2) an empirical analysis of stock price movements in relation to publicly known facts known as an event study.[11]

In *Matrixx*, the Court refused to adopt a bright-line rule that pharmaceutical product risks should be

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[11] "An event study is a statistical analysis that isolates the effects of an event on a security's price and measures the likelihood that the effect could have been due to the normal random fluctuations of the security's price as opposed to being due to a particular event." Frederick C. Dunbar & Dana Heller, *Fraud on the Market Meets Behavioral Finance,* 31 DEL. J. CORP. L. 455, 468 (2005); Glenn V. Henderson, Jr., *Problems and Solutions in Conducting Event Studies*, 57 J. RISK & INS. 282 (1990). "[T]he primary interest of investors is economic. After all, the principal, if not the only reason why people invest their money in securities is to obtain a return. A variety of other motives are probably present in the investment decisions of numerous investors but the only common thread is the hope for a satisfactory return, and it is to this that a disclosure scheme intended to be useful to all must be primarily addressed." Richard C. Sauer, *The Erosion of the Materiality Standard in the Enforcement of the Federal Securities Laws*, 62 BUS. LAW. 317, 331-32 (2007) (citing SEC Release, Proposed Environmental Disclosures, 40 Fed. Reg. 51656, 51664 (Nov. 6, 1975) (alteration in original).

required to be disclosed as "material" only if such risks were "statistically significant." 131 S. Ct. at 1318-20. *Matrixx* reaffirmed *Basic*, holding that materiality is a test of "whether a reasonable investor would have viewed the nondisclosed information as having significantly altered the total mix of information made available." *Matrixx*, 131 S. Ct. at 1318, 1321 (quoting *Basic*, 485 U.S. at 232) (internal quotation marks omitted) (finding that "something more" is required to show that an omitted statement would have significantly altered the total mix of information).

For example, plaintiffs could seek to establish materiality at class certification by assessing an alleged misstatement in the context of the "total mix" of public information present at the time of the alleged misstatement. In this way, a plaintiff could attempt to show that a reasonable investor would have viewed the nondisclosed information as having significantly altered the "total mix" of information made available.

Materiality hinges upon the information that is publicly available to a reasonable investor. *See Basic*, 485 U.S. at 232; *Matrixx*, 131 S. Ct. at 1321. The plaintiff has access to this information – it is public by definition – and may readily assess the total mix of public information to present facts that establish the materiality of a particular statement within a particular timeframe. *See In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1425 (3d Cir. 1997) ("In the context of an 'efficient' market, the concept of materiality translates into information that alters the price of the firm's stock."); *Shaw v. Digital Equipment*

Corp., 82 F.3d 1194, 1218 (1st Cir. 1996) (in cases involving the fraud-on-the-market theory of liability, statements identified as actionably misleading are alleged to have caused injury, "not through the plaintiffs' direct reliance upon them, but by dint of the statements' inflating *effect on the market price of the security purchased*.") (emphasis added), *superseded on other grounds by statute as recognized in Greebel v. FTP Software, Inc.*, 194 F.3d 185, 197 (1st Cir. 1999).

There are numerous ways that a plaintiff could seek to assess and analyze the total mix of information. Depending on the circumstances of the case, for example, review of press reports, company disclosures, or other publicly available information can be effective. Such methods are commonly used by plaintiffs. *In re Sadia, S.A. Sec. Litig.,* 269 F.R.D. 298, 317 (S.D.N.Y. 2010) (analysis of SEC filings and company conference calls); *Durgin v. Mon*, 659 F. Supp. 2d 1240, 1245 (S.D. Fla. 2009) (analysis of SEC filings and press release), *aff'd,* 415 F. App'x 161 (11th Cir. 2011); *Miller v. Lazard*, *Ltd.*, 473 F. Supp. 2d 571, 578 (S.D.N.Y. 2007) (analysis of news articles, press releases, and analyst reports); *see also In re Amgen Sec. Litig.*, 07-cv-02536-PSG-PLA, Dkt. No. 137, Order Regarding Motion to Dismiss (filed Feb. 1, 2008) (analysis of company conference calls); *DeMarco v. Lehman Bros.*, *Inc.*, 222 F.R.D. 243, 246 (S.D.N.Y. 2004) (the "role of research analysts and other market professionals is, indeed, critical to the pricing mechanism of the securities market, for ordinary investors frequently lack sufficient expertise to interpret the wealth of information, much of it

highly technical, emanating from most public companies.").

Analyst reports can also provide useful insight into the total mix. *See, e.g.*, *Cal. Pub. Employees' Ret. Sys. v. Chubb Corp.*, 394 F.3d 126, 169 (3d Cir. 2004) (considering analysts' reports as part of the "total mix" of information available to a reasonable shareholder deciding how to vote). As reflected in the record in this case, analyst reports are often a useful reflection of public information and are readily available to the parties in securities cases.

It is reasonable to require securities fraud class action plaintiffs – who are typically represented by highly sophisticated counsel – to analyze information that is publicly available. To the extent a party may seek non-public information, a court can readily permit narrow precertification discovery. *See Oppenheimer Fund, Inc. v. Sanders*, 437 U.S. 340, 351 n.13 (1978) ("discovery often has been used to illuminate issues upon which a district court must pass in deciding whether a suit should proceed as a class action under Rule 23 . . ."); *Stewart v. Winter*, 669 F.2d. 328, 331 (5th Cir. 1982) (quoting *Pittman v. E.I. duPont de Nemours & Co.*, 552 F.2d 149, 150 (5th Cir. 1977)) ("in most cases, 'a certain amount of discovery is essential in order to determine the class action issue and the proper scope of the class action.'").

At a minimum, a defendant should be permitted the opportunity to present evidence that might refute the claimed materiality of a particular statement

when analyzed in the total mix of information, as Petitioners sought to do in this case.

C. Materiality May Also be Established Through an Event Study of the Impact of an Alleged Misrepresentation on the Price of the Security

1. A Determination of the Impact of a Purported Misstatement on the Price of a Security Is Distinct From Loss Causation

In addition to an analysis of the total mix of information, a plaintiff can also use an economic analysis of "price impact" to establish the materiality.

It is important at the outset to distinguish *allowing* a showing of *price impact* at class certification to prove the materiality predicate from *requiring* a showing of *loss causation* at class certification. In *Halliburton*, this Court held that a plaintiff in a Section 10(b) case seeking class certification need not prove facts demonstrating *loss causation*. *Halliburton*, 131 S. Ct. at 2184. Loss causation tests the causation of any *damages* in securities cases. *See Dura Pharm., Inc.,* 544 U.S. at 342 (loss causation is "causal connection between the material misrepresentation and the loss"). Under *Dura*, a loss is actionable only if the revelation of the truth of a misrepresentation or omission results in a corresponding decline in stock price producing a quantifiable out-of-pocket loss. *Id.* at 346-47. That is, loss causation focuses on the movement of the stock price *after* revelation of the truth.

Price impact is a distinct concept from *loss causation*. In *Halliburton*, this Court articulated that reliance concerns "facts surrounding the investor's decision to engage in the transaction." 131 S. Ct. at 2186. Under *Basic*, "an investor presumptively relies on a defendant's misrepresentation if that 'information is reflected in [the] market price' of the stock at the time of the relevant transaction." *Halliburton*, 131 S. Ct. at 2186 (quoting *Basic*, 485 U.S. at 247). "Loss causation, by contrast, requires a plaintiff to show that a misrepresentation that affected the integrity of the market price *also* caused a subsequent economic loss." *Id.*

"'Price impact' simply refers to the effect of a misrepresentation on a stock price." *Id.* at 2187. Unlike loss causation, price impact is a means of establishing reliance, because it ultimately concerns analysis of the market price of stock at the time of the relevant transaction (*i.e.*, the purchase or sale relevant to a particular plaintiff's claim).[12] Several

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[12] As noted in Petitioners' brief, *see* Pet'rs Br. at 14, reliance or "but for" causation is wholly distinct from loss causation. "Reliance is an 'essential' component of a 10b-5 claim because it guarantees 'the "requisite causal connection between a defendant's misrepresentation and a plaintiff's injury."' *Id.* (quoting *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 159 (2008)). Market impact analysis similarly can address both price impact at purchase (*i.e.*, reliance) and loss causation (*i.e.*, damages). "Market-impact analysis takes two related forms: first, the showing that the market was distorted by the fraud; second, that the emergence of the truth, corrective disclosure, caused a loss to some or all investors. The former, as just noted, is what *Basic* focused on as a predicate for the presumption of reliance. The latter, loss causation, is conceptually distinct." Donald C. Langevoort,

circuits have found price impact to be an appropriate means of proving or disproving materiality at class certification. *In re Salomon Analyst Metromedia Litig.*, 544 F.3d 474, 485 (2d Cir. 2008); *In re DVI, Inc. Sec. Litig.*, 639 F.3d 623, 634 (3d Cir. 2011); *Oscar Private Equity Invs. v. Allegiance Telecom, Inc.*, 487 F.3d 261, 265 (5th Cir. 2007), *abrogated on other grounds by Halliburton*, 131 S. Ct. 2179.

Price impact exists when a misrepresentation has distorted the market price of a security, so that *at the time of the purchase or sale* a misrepresentation affected the price of a security by a statistically significant amount. Price impact can evince materiality because only material misrepresentations will have a distorting impact on the price of a security. If a misrepresentation does not distort the market price, then the *Basic* reliance presumption simply does not apply. *See Halliburton*, 131 S. Ct. at 2186.

2. An Empirical Analysis of Materiality at Class Certification Is Practical, Proper, and Not Unduly Burdensome

An event study is a commonly used means of empirically assessing the predominance requirement under Rule 23 and the materiality element to the fraud-on-the-market presumption.[13] A plaintiff

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Basic at Twenty: Rethinking Fraud on the Market, 2009 WIS. L. REV. 151, 180 (2009).

[13] *See Eckstein v. Balcor Film Investors*, 58 F.3d 1162, 1170 (7th Cir. 1995) ("Reliance is the confluence of materiality and

likewise has readily available means to establish price impact at class certification through an event study because it requires empirical analysis of the total mix of publicly available information. *See* William O. Fisher, *Does the Efficient Market Theory Help Us Do Justice in A Time of Madness?,* 54 EMORY L.J. 843, 872 (2005).

Event studies use economic analysis to determine whether a particular alleged misstatement had a statistically meaningful impact on stock price. "[A]n event study . . . [can] determine whether the alleged misrepresentations caused any statistically significant stock price movements when made or when a supposedly corrective disclosure was made, controlling for other possible causes of stock price movements (such as movements of the overall market) and random fluctuations."[14] They "are commonly used to isolate the effects on the stock price of the disclosure of the withheld information."[15]

When an event study shows that a misrepresentation had a statistically significant effect on the price of a stock then, absent contrary evidence, the market may be presumed to have

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causation. The fraud-on-the-market doctrine is the best example; a material misstatement affects the security's price, which injures investors who did not know of the misstatement.").

[14] Daniel R. Fischel, *Market Evidence in Corporate Law*, 69 U. CHI. L. REV. 941, 948 (2002).

[15] Janet Cooper Alexander, *The Value of Bad News in Securities Class Actions*, 41 UCLA L. REV. 1421, 1433 (1994).

indirectly relied on the misrepresentation.[16] "And, by the fraud-on-the-market theory, all of the investors who bought (or sold) the stock also 'relied' by buying or selling at a market price that included a component reflecting the falsity."[17]

Federal courts have lauded the use of empirical studies in securities class action cases because the studies provide a useful metric for measuring the effect a particular statement has on the price of the stock.[18] *See, e.g., In re Zonagen, Inc. Sec. Litig.*, 322 F. Supp. 2d 764, 780 (S.D. Tex. 2003) (finding defendant's event study sufficiently rebutted the fraud-on-the-market presumption of reliance); *In re N. Telecom Ltd. Sec. Litig.*, 116 F. Supp. 2d 446, 460-61 (S.D.N.Y. 2000) (supporting use of event studies in

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[16] In addition to showing inflation at the time of purchase, a plaintiff could also use an event study to show a reaction to disclosure of the truth to establish materiality. *See In re SLM Corp. Sec. Litig.*, No. 08 CIV. 1029 WHP, 2012 WL 209095, at *5 (S.D.N.Y. Jan. 24, 2012) ("While not required at the class certification stage, evidence of a stock price movement following corrective disclosures may be a relevant factor in the legal assessment of materiality.") (citing *Berks Cnty. Emp. Retirement Fund v. First Am. Corp.*, 734 F. Supp. 2d 533, 540 n. 40 (S.D.N.Y. 2010)). By *allowing* a plaintiff to make such a showing of price movement (or allowing a defendant to show a lack of price movement) the Court would not be *requiring* a plaintiff to make such a showing.

[17] *See* William O. Fisher, *Does the Efficient Market Theory Help Us Do Justice in A Time of Madness?*, 54 EMORY L.J. at 874.

[18] *See* Michael J. Kaufman & John M. Wunderlich, *Regressing: The Troubling Dispositive Role of Event Studies in Securities Fraud Litigation.,* 15 STAN. J.L. BUS. & FIN. 183, 219 (2009) (acknowledging that federal courts have widely accepted the use of event studies).

securities actions); *In re Oracle Sec. Litig.*, 829 F. Supp. 1176, 1181 (N.D. Cal. 1993) (same); *Teamsters Local 445 Freight Div. Pension Fund v. Bombardier Inc.*, 546 F.3d 196, 207-10 (2d Cir. 2008) (acknowledging importance of event studies in establishing market efficiency); *In re Xcelera.com Sec. Litig.*, 430 F.3d 503, 512-14 (1st Cir. 2005) (same); *In re Nature's Sunshine Prods. Inc. Sec. Litig.*, 251 F.R.D. 656, 664-65 (D. Utah 2008) (same); *see also* Frederick C. Dunbar, et al, *Fraud on the Market Meets Behavioral Finance*, 31 Del. J. CORP. L. at 468 (event studies are frequently determined by courts to be necessary tools to assess the price impact of a particular statement).

In fact, plaintiffs in this case conducted an event study related to the efficiency of the market to establish that particular *Basic* predicate for class certification.[19] Simply stated: an event study conducted to establish materiality in a securities fraud case can empirically assess whether a purported misstatement affected the market price of the security in order for the court to presume reliance under the fraud-on-the-market theory.[20]

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[19] *See* Mem. of Points and Authorities in Support of Lead Pl.'s Mot. for Class Cert. at 17, *Conn. Ret. Plans & Trust Fund v. Amgen Inc.* (C.D. Cal. Mar. 4, 2009), No. CV 07-2536 PSG (PLAx), ECF No. 129.

[20] William O. Fisher, *Does the Efficient Market Theory Help Us Do Justice in A Time of Madness?,* 54 EMORY L.J. at 871 (event studies are employed to determine, among other elements in a 10b-5 action, whether a purported misstatement was or was not material).

Absent a statistically significant impact on price at the time of the purported misstatement, one of two truths is revealed: (1) the alleged misstatement is not material; or (2) the statement is material, but the market is not efficient. The failing of either requires the trial court to deny certification because the plaintiff cannot establish the necessary foundation required to invoke the fraud-on-the-market presumption.[21]

In addition to an analysis of the total mix of information, then, a plaintiff could attempt to establish materiality through an event study at class certification. Such an empirical analysis of the purported misstatement and its impact upon the price of the security is therefore practical, not unduly burdensome, and usually effective in providing a metric to ascertain materiality. For example, in this matter, respondent presented the trial court with an empirical analysis of the efficiency of the market at class certification.

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[21] *See In re DVI, Inc. Sec. Litig.*, 639 F.3d at 638 (finding that in an otherwise efficient market, the failure of a corrective disclosure to affect the market price may serve as a rebuttal to the presumption of reliance because it renders the misstatement immaterial as a matter of law); *In re Moody's Corp. Sec. Litig.*, 274 F.R.D. 480, 493 (S.D.N.Y. 2011) (finding "no period within the proposed class period where the alleged misrepresentation caused a statistically significant increase in the price or where a corrective disclosure caused a statistically significant decline in the price . . . . the reliance presumption for . . . the class cannot be certified"); *In re Am. Int'l Grp., Inc. Sec. Litig.*, 265 F.R.D. 157, 182, (S.D.N.Y. 2010); *In re Credit Suisse First Boston Corp. (Lantronix, Inc.) Analyst Sec. Litig.*, 250 F.R.D. 137, 143-49 (S.D.N.Y. 2008) (analyzing significance of market responses to statements and disclosures at the beginning, middle, and end of the class period).

IV. AT A MINIMUM, COURTS SHOULD ALLOW A DEFENDANT THE OPPORTUNITY TO REBUT THE FRAUD-ON-THE-MARKET PRESUMPTION BY REFUTING MATERIALITY AT CLASS CERTIFICATION

Under *Basic*, the fundamental premise in crafting a presumption of reliance to permit securities actions to be litigated as class actions was that a defendant be afforded the opportunity to rebut the presumption with "[a]ny showing that severs the link between the alleged misrepresentation and either the price received (or paid) by the plaintiff, or his decision to trade at a fair market price . . . ." 485 U.S. at 248; *see also In re DVI, Inc. Sec. Litig.*, 639 F.3d at 632 (finding defendants may rebut the presumption of reliance with any defense to actual reliance); *Semerenko v. Cendant Corp.*, 223 F.3d 165, 178-79 (3d Cir. 2000) (the fraud-on-the-market doctrine merely creates a presumption which a defendant may rebut by raising any defense to actual reliance); *In re Salomon*, 544 F.3d at 485 (court must permit defendants to present rebuttal arguments before certifying a class). *Basic* delineated a non-exhaustive list of potential defenses that would sever the link required to invoke the fraud-on-the-market presumption and specifically mentioned a showing that the alleged misstatement was immaterial.[22]

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[22] *See Basic*, 485 U.S. at 248-49 ("For example, if petitioners could show that the 'market makers' were privy to the truth about the merger discussion here with Combustion, and thus that the market price would not have been affected by their

Permitting a defendant to rebut the fraud-on-the-market presumption is also necessary so district courts can determine a proper class period (and typicality). As a simple hypothetical example, assume a plaintiff asserts a 2-year class period in a case in which a company on day one allegedly misrepresents its financial results (*e.g.* net income); announces an intent to restate on day 200; actually details its restatement and corrects its results on day 400; the stock drops ten percent on day 401; and the stock then drops (on no announcements) another ten percent on day 730 (the end of the two years). Without considering whether the restatement announcement or the actual restatement corrected the alleged material misrepresentation (*i.e.*, whether the material truth had been revealed so that any inference of reliance on market price has been severed), the court cannot determine when the class should properly end.[23]

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misrepresentations, the causal connection could be broken: the basis for finding that the fraud had been transmitted through market price would be gone. Similarly, if, despite petitioners' allegedly fraudulent attempt to manipulate market price, news of the merger discussions credibly entered the market and dissipated the effects of the misstatements, those who traded Basic shares after the corrective statements would have no direct or indirect connection with the fraud. Petitioners also could rebut the presumption of reliance as to plaintiffs who would have divested themselves of their Basic shares without relying on the integrity of the market.").

[23] In this example, the class period should obviously end before the second ten percent drop. Not allowing a defendant to rebut the presumption and allowing a two-year class period rather than a proper, shorter period almost *doubles* the amount of alleged class damages.

Requiring a case to proceed as a class action, notwithstanding the availability of dispositive evidence refuting a claim of materiality, would unnecessarily increase the costs of defending meritless litigation and the possibility of *in terrorem* settlements. For this reason, the Court should affirm a defendant's right to refute a claim of materiality at class certification.

CONCLUSION

For all the foregoing reasons, the Court should reverse the Ninth Circuit's opinion.

Respectfully submitted,

WILLIAM F. SULLIVAN (*counsel of record*)
HOWARD M. PRIVETTE
BARRY G. SHER
PETER M. STONE
STEPHEN B. KINNAIRD
JOHN S. DURRANT
Paul Hastings LLP

515 South Flower Street, 25th Floor
Los Angeles, California 90071
(213) 683-6000
williamsullivan@paulhastings.com

75 East 55th Street
New York, NY 10022
(212) 318-6000

1117 S. California Avenue
Palo Alto, California 94304
(650) 320-1800

875 15th Street, N.W.
Washington, DC 20005
(202) 551-1700

Counsel for *Amicus Curiae*
Securities Industry and Financial
Markets Association

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