SUPREME COURT FURTHER CLARIFIES CLASS CERTIFICATION STANDARDS FOR SECURITIES FRAUD ACTIONS

Yesterday, the Supreme Court ruled, in *Amgen v. Connecticut Retirement Plans & Trust Funds*, that investors seeking to certify a class in a securities fraud action need not prove materiality at the class certification stage. The 6-3 decision overturned precedent (particularly in the Second Circuit) that had held that, *before* a class can be certified, an investor must prove materiality to invoke the *Basic v. Levinson*[1] rebuttable presumption of reliance on public misrepresentations regarding securities traded on an efficient market.

Background of the *Amgen* Case

In *Amgen*, the Plaintiff alleged that Amgen, Inc. and several of its officers (collectively, the "Defendants") made a series of materially false and misleading statements and omissions relating to two of Amgen's pharmaceutical products.[2] The complaint asserted claims pursuant to sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b–5 thereunder. To recover damages in a section 10(b) case, a plaintiff must prove, among other things, reliance on a material misstatement made by defendants. Plaintiffs typically seek to satisfy the reliance element for the putative investor class by utilizing the *Basic* presumption.

The district court in *Amgen* certified the investor class, holding that, to trigger the *Basic* presumption, "Plaintiff need only establish that an efficient market exists [and that] [o]ther inquiries into issues such as materiality . . . are properly taken up at a later stage in the proceeding."[3] The Ninth Circuit affirmed. It held that, at the class certification stage, investors must merely "plausibly allege" (but need not prove) that the claimed misrepresentations were material.[4] The Ninth Circuit also rejected the argument that Defendants should have had an opportunity at the class certification stage to rebut the fraud-on-the-market presumption by showing immateriality, noting that such merits question should be adjudicated at summary judgment or trial.[5]

The Ninth Circuit's decision conflicted with other circuit court decisions, including the Second Circuit's decision in *In re Salomon Analyst Metromedia Litigation*,[6] which held that a plaintiff must prove, and a defendant may present evidence rebutting, materiality *before* class certification. Defendants petitioned the Supreme Court for a writ of certiorari, which the Court granted to "to resolve a conflict among the Courts of Appeals over whether district courts must

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1 485 U.S. 224 (1988).
2 *See Conn. Ret. Plans & Trust Funds v. Amgen, Inc.*, No. 07-CV-2536, 2009 WL 2633743, at *1 (C.D. Cal. Aug. 12, 2009).
3 *Id.* at *12.
4 *See Conn. Ret. Plans & Trust Funds v. Amgen, Inc.*, 660 F.3d 1170, 1171 (9th Cir. 2011).
5 *See id.* at 1177.
6 544 F.3d 474 (2d Cir. 2008).

require plaintiffs to prove, and must allow defendants to present evidence rebutting, the element of materiality before certifying a class action under § 10(b) and Rule 10b–5."[7]

The Supreme Court's Decision

In an opinion authored by Justice Ginsburg,[8] the Supreme Court held that proof of materiality is not necessary at the class certification stage. The Court reasoned that, because the test of whether a misrepresentation is material is "an objective one, involving the significance of an omitted or misrepresented fact to a reasonable investor," materiality is a "common question" for the entire class.[9] The Court rejected Defendants' argument that materiality should be treated no differently than the other fraud-on-the-market predicates, which must be proven prior to class certification – namely, that the statements were publicly made, the stock was traded on an efficient market, and the transaction occurred after the alleged misrepresentation and before the corrective disclosure. The Court explained that the timing of the transaction relates to the Rule 23(a) requirements of typicality and adequacy of representation of the lead plaintiff while the public nature and efficiency of the market are not (unlike materiality) essential elements of a section 10(b) claim.[10] The Court next rejected Defendants' argument that certification without proof of materiality will result in undue pressure on defendants to settle cases. In that regard, the Court commented that materiality was no different from other elements of a securities fraud claim – none of which must be proven prior to class certification.[11] The Court also pointed to the enactment of the Private Securities Litigation Reform Act of 1995, which addressed "perceived abuses" in securities fraud cases. Given that Congress had already addressed the policy concerns raised by Defendants, the Court concluded that it was not the role of the judiciary to "make its own further adjustments by reinterpreting Rule 23."[12]

Justices Scalia, Kennedy, and Thomas dissented. In his dissent, Justice Thomas concluded that plaintiffs who have not demonstrated materiality are not entitled to the fraud-on-the-market presumption and, without that presumption, a class action should not proceed because plaintiffs cannot establish that common questions of reliance will predominate over individual questions.[13] Justice Scalia, writing separately, voiced his displeasure with the majority's holding that not only

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7 *Amgen v. Conn. Ret. Plans & Trust Funds*, No. 11-1085, 568 U.S. __, slip op. at 8 (Feb. 27, 2013). In the Second and Fifth Circuits, a plaintiff had to prove materiality in order to invoke the *Basic* presumption. *See In re Salomon*, 544 F.3d at 481-84, 486 n.9; *Oscar Private Equity Invs. v. Allegiance Telecom, Inc.*, 487 F.3d 261, 265 (5th Cir. 2005), *abrogated on other grounds by Erica P. John Fund v. Halliburton Co.*, 131 S. Ct. 2179 (2011). In the Third and Seventh Circuits, as well as in the Ninth Circuit, plaintiffs need not establish materiality at the class certification stage. *See In re DVI, Inc. Sec. Litig.*, 639 F.3d 623, 631 (3d Cir. 2011); *Schleicher v. Wendt*, 618 F.3d 679, 685 (7th Cir. 2010).

8 Justice Ginsburg was joined by Chief Justice Roberts and Justices Breyer, Alito, Sotomayor, and Kagan. Justice Alito also filed a concurring opinion. Justice Thomas filed a dissenting opinion, in which Justice Kennedy joined, and in which Justice Scalia joined, except for Part I–B. Justice Scalia also filed a separate dissenting opinion.

9 *Id.* at 11 (internal quotations omitted).

10 *See id*.

11 *See id*. at 18-19.

12 *Id*. at 20 (quoting *Schleicher*, 618 F.3d at 686).

13 *See id.* at 1 (Thomas, J., dissenting).

"accept[ed] what some consider the regrettable consequences of the four-Justice opinion in *Basic*; it expand[ed] those consequences from the arguably regrettable to the unquestionably disastrous."[14] The three dissenters agreed that the *Basic* decision was "questionable" and appeared open to revisiting *Basic's* fraud-on-the-market presumption.[15] A fourth justice, Justice Alito, joined the majority opinion, but filed a concurrence that questioned the "economic premise" of the fraud-on-the-market theory and suggested that "reconsideration of the *Basic* presumption may be appropriate."[16]

Implications of *Amgen*

After *Amgen*, instead of requiring plaintiffs to establish materiality by a preponderance of the evidence at the class certification stage (as was the standard in the Second Circuit), plaintiffs will only have to "must[er] sufficient evidence [regarding materiality] to satisfy the relatively lenient standard for avoiding summary judgment."[17] While securities plaintiffs no longer need to prove materiality at the class certification stage, *Amgen* does not alter the requirement that they establish by a preponderance of the evidence that the alleged misrepresentations were publicly known, that the stock traded on an efficient market, and that the relevant transaction took place between the time of the alleged misrepresentation and when the truth was revealed. However, those prerequisites are often easier for plaintiffs to establish at class certification than materiality. Finally, but perhaps most significantly, four justices appear ready to reconsider *Basic's* fraud-on-the-market presumption, the overturning of which could drastically alter securities fraud class actions by making it significantly more difficult for plaintiffs to certify a class.

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14 *Id.* at 4 (Scalia, J., dissenting).
15 *Id.* at 4 n.4 (Thomas, J., dissenting).
16 *Id.* at 1 (Alito, J., concurring).
17 *Id.* at 23-24.