No. 09-1403

IN THE

Supreme Court of the United States

ERICA P. JOHN FUND, INC.,

Petitioner,

v.

HALLIBURTON CO. ET AL.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF OF CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

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INTEREST OF *AMICUS CURIAE*[1]

The Chamber of Commerce of the United States of America ("Chamber") is the Nation's largest federation of business companies and associations. It directly represents 300,000 members and indirectly represents the interests of over 3 million business, trade, and professional organizations of every size, in every sector, and from every region of the country. Over 96% of the Chamber's members are small businesses with 100 or fewer employees. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae* briefs in cases that raise issues of concern to the nation's business community, such as those involving the federal securities laws, including *Stoneridge Investment Partners, LLC v. Scientific Atlanta, Inc.*, 552 U.S. 148 (2008), *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308 (2007), and *Dura Pharmaceuticals Inc. v. Broudo*, 544 U.S. 336 (2005).

Many of the Chamber's members are companies subject to the U.S. securities laws who would be directly and adversely affected if the Court were to hold that loss causation could not be considered at the class certification stage. Over

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[1] Pursuant to this Court's Rule 37.6, *amicus curiae* affirms that no counsel for any party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae*, its members or its counsel made a monetary contribution to its preparation or submission.

Pursuant to Rule 37.3, *amicus curiae* states that petitioner and respondent have consented to the filing of this brief, and copies of their letters of consent are on file with the Clerk's Office.

twenty years ago, in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), the Court created the fraud-on-the-market presumption expressly to allow 10b-5 plaintiffs to bring class action claims without having to prove individual reliance. Without that presumption, as *Basic* held, most 10b-5 class actions could not be certified as individual issues would predominate. *Basic* at 242. This significantly expanded both the Rule 10b-5 implied private right of action and Rule 10b-5 class actions. However, *Basic* did provide some limits to these expansions. At the class certification stage, *Basic* (i) required plaintiffs seeking the benefit of the presumption to "allege and prove" that, among other things, the alleged misrepresentations were "material" and the market in which the securities traded was "efficient," and (ii) permitted the presumption to be rebutted by "[*a*]*ny* showing that severs the link between a [defendant's] alleged misrepresentation and … the price received (or paid) by the plaintiff…." 485 U.S. at 248, n. 27 (emphasis added).

The result advocated by Petitioner would erase even the limits on the fraud-on-the-market presumption imposed by *Basic*. By prohibiting courts from considering loss causation evidence at the class certification stage, Petitioner's argument would render the fraud-on-the-market presumption virtually irrebuttable and thereby further expand the 10b-5 judicially-implied cause of action. This would open the door to a flood of Rule 10b-5 class action litigation to the detriment of our nation's businesses and the financial markets. Such a result cannot be reconciled with *Basic* or with *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 165-166 (2008), which held that the courts should not further expand the judicially-implied private right of action under Rule 10b-5.

INTRODUCTION AND SUMMARY OF ARGUMENT

In *Archdiocese of Milwaukee Supporting Fund, Inc. v. Halliburton Co.*, 597 F.3d 330, 341-42 (5th Cir. 2010), the Fifth Circuit Court of Appeals affirmed a lower court's decision denying class certification in a Rule 10b-5 case because the lack of any evidence of a market price impact disproved the fraud-on-the-market presumption. Specifically, the court stated that plaintiff could either prove that the price of the security was increased by the misrepresentation at the time it was made or, alternatively, prove that the price fell in response to a corrective disclosure through evidence akin to that used to show loss causation. The Court properly held that plaintiff could make neither showing. Petitioner seeks reversal of the Fifth Circuit's decision, arguing principally that because loss causation is a merits issue, it should not be considered as part of class certification. Petitioner is wrong because loss causation, like reliance, is *both* a class certification issue and a merits issue.

1. The result advocated by Petitioner – that courts are precluded from considering loss causation at the class certification stage – would expand class actions based on the Rule 10b-5 implied right of action in contravention of this Court's holdings in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988) and

Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc., 552 U.S. 148 (2008).

Basic Inc. v. Levinson,[2] significantly expanded the Rule 10b-5 implied right of action by creating a fraud-on-the-market presumption in order to permit securities fraud plaintiffs to meet class certification requirements under Fed. R. Civ. P. Rule 23. 485 U.S. at 242. *Basic* created the fraud-on-the-market presumption so that a class action might meet the predominance requirement of Fed. R. Civ. P. 23(b)(3). *Id*. ("Requiring proof of individualized reliance from each member of the proposed plaintiff class" would result in "individual issues . . . overwhelm[ing] the common ones"). To support its creation of a fraud-on-the-market presumption, the Court looked, not to the text of §10(b) and Rule 10b-5, but to an unexpressed "congressional policy" of "facilitating Rule 10b-5 litigation." *Id.* at 245.

Basic, however, expressly limited its expansion of the Rule 10b-5 private right of action by, *at the class certification stage*, (i) requiring plaintiffs seeking to benefit from the presumption to "allege and prove" that the alleged misrepresentations were material and that the securities traded in an efficient market, and (ii) permitting defendants to rebut the presumption by "[*a*]*ny* showing that severs the link between the alleged misrepresentation and . . . the price received (or paid) by the plaintiff. . . ." *Id.* at 248. Under *Basic*, establishing and rebutting the fraud-on-the-

[2] *Basic* was a 4-2 decision. Justices Rehnquist, Scalia, and Kennedy did not participate.

market presumption are class certification issues because, in the absence of the presumption, "individual [reliance] issues . . . overwhelm[] the common ones." *Id.* at 242.

Loss causation is directly relevant to both of these class certification inquiries in a way that other 10b-5 merits issues, such as scienter, are not. Specifically, the absence of loss causation is relevant to showing that either the alleged misrepresentation was not material or the market was not efficient – either of which independently undermines the presumption. For the same reason, evidence disproving loss causation is one showing that "severs the link between the alleged misrepresentation and . . . the price received (or paid) by the plaintiff . . . ." *Id.* at 248. It does this by proving that no event correcting that alleged misrepresentation ever moved the market price downward.

Unless the common-sense principle that what goes up must come down is repealed, the absence of loss causation disproves the presumption of reliance. When a plaintiff alleges that it paid an inflated stock price because a material misrepresentation was relied on by an efficient market – but the price never comes down due to a corrective event – this is a "showing" that rebuts the allegation of inflation in the first place.

An additional reason supports broadly interpreting *Basic*'s limitations so that the absence of loss causation disproves the presumption invented by *Basic*. This reason is that *Basic*'s presumption is inconsistent with the Court's more recent jurisprudence against expanding implied rights of action, including 10b-5 private civil claims. *See Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 166 (2008) (declining to expand Rule 10b-5 implied right of action). At a minimum, *Basic*'s presumption should be constrained, not further expanded, by construing loss causation to be relevant to disproving the presumption.

This Court already has rejected the canard that if an issue is a merits issue, it cannot also be a class certification issue. After all, *Basic* itself expressly treats establishing and rebutting the presumption of reliance as both a merits issue and a class certification issue. 485 U.S. at 230, 250. More generally, in *General Telephone Co. of the Southwest v. Falcon*, 457 U.S. 147 (1982), the Court held that the class certification decision requires a "rigorous analysis" of whether "the prerequisites of Rule 23(a) have been satisfied" which could entail "prob[ing] behind the pleadings" and deciding issues that are "*enmeshed in the factual and legal issues compromising the plaintiff's cause of action.*"' *Id.* at 160, 161. (internal citations and quotations omitted) (emphasis added); *see also Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 615 (1997) (noting that Rule 23(b)(3) "invites a close look at the case before it is accepted as a class action")(internal citation omitted); *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 845, n. 20 (1999), (noting that where there is a "likelihood that significant questions, not only of damages but *of liability and defenses of liability*, would be present, affecting the individuals in different ways," class certification may not be appropriate)(emphasis added)(citing Advisory Committee Notes to Rule 23(b)(3)). Loss causation is such an issue.

2. Independently, loss causation is also relevant to other class certification issues such as: (i) the proper end of the class period, and (ii) whether a broad Rule 10b-5 plaintiff class is impracticable or unmanageable.

Class Period. Pursuant to Rule 23(c)(1)(B), "[a]n order that certifies a class action must define the class" and include "a readily discernable, clear, and precise statement of the parameters defining the class or classes to be certified," including the class period. Fed. R. Civ. P. 23(c)(1)(B); *Wachtel v. Guardian Life Ins. Co. of Am.*, 453 F.3d 179, 187-88 (3d. Cir. 2006). In a Rule 10b-5 case, identifying the end of the class period requires courts to determine the last date when curative events caused a price drop. Identifying the last date when, if ever, a curative event reduced the stock price is a loss causation question. *See Dura Pharm. Inc. v. Broudo*, 544 U.S. 336, 344 (2005) ("a person who misrepresents the financial condition of a corporation in order to sell its stock *becomes liable to a relying purchaser 'for the loss' the purchaser sustains 'when the facts . . . become generally known' and 'as a result' share value 'depreciate[s]'*")(emphasis added)(internal citations omitted). Absent loss causation, no class period can be defined, because it would never end, and no class can be certified.

Manageability. Under Rule 23(b)(3)(D), "likely difficulties in managing a class action" may require that certification be denied. Although Rule 23(c)(5), allows, "[*w*]*hen appropriate*, a class [to] be divided into subclasses," a class with many subclasses may well be unmanageable. Fed. R. Civ. P. 23(c)(5) (emphasis added). Many putative 10b-5 class actions allege that curative events affected a stock's price over a long period of time. Before certifying a class action, a court would have to consider whether multiple subclasses are necessary for numerous different groups of plaintiffs who sold at various points in time before the curative events were complete, as well as for those who sold before any curative events, and those who never sold or sold after all curative events had been absorbed by the market. These subgroups and their contingency fee counsel might have conflicts, such as how fairly to divide among them any settlement proceeds, or court-ordered recovery, based on when loss causation occurred. Such a morass of subclasses could render a broad class action unmanageable. In addition to the other reasons, at the class certification stage, courts should consider loss causation on manageability issues.

ARGUMENT

I. LOSS CAUSATION IS ESSENTIAL TO KEEP CLASS CERTIFICATION OF IMPLIED SECTION 10(B) ACTIONS WITHIN REASONABLE BOUNDS.

Basic Inc. v. Levinson expanded class actions based on the Rule 10b-5 implied private right of action by permitting putative class action plaintiffs to benefit from a class-wide presumption of reliance, but only if they could "allege and prove" that: (i) the defendant made material public misrepresentations, (ii) the "shares were traded on an efficient market," and (iii) the plaintiff traded the shares "between the time the misrepresentations were made and the time the truth was revealed." *Basic*, 485 U.S. at 248, n. 27. *Basic* held that, "without the presumption [of reliance], it would be impractical to certify a class under Federal Rule of Civil Procedure 23(b)(3)" because "individual [reliance] issues then would have overwhelmed the common ones." *Id*. at 230, 242. To support its creation of the fraud-on-the-market presumption to expand the implied private civil action, the Court looked not to the text of §10(b) and Rule 10b-5. Instead, *Basic* explained that "facilitating Rule 10b-5 litigation . . . supports . . . the congressional policy embodied in the 1934 Act." *Id*. at 245.

Basic is inconsistent with the Court's recent jurisprudence against expanding implied rights of action based on policy notions. In *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008), the Court, recognizing that the private right of action under §10(b) is a "judicial construct that Congress did not enact in the text of the relevant statutes" held that "[t]he decision to extend the [implied] cause of action is for Congress," not for the courts. *Id.* at 164-165. This reflected the Court's current approach, unlike *Basic*, of neither creating nor expanding implied rights of action. *See Wilkie v. Robbins*, 551 U.S. 537, 562 (2007) (no private *Bivens* action against Bureau of Land Management employees alleged to have used harassment and intimidation in attempt to force owner to grant easement); *Gonzaga Univ. v. Doe*, 536 U.S. 273, 287-91 (2002) (no private right of action created by nondisclosure provisions in Family Educational Rights and Privacy Act); *Alexander v. Sandoval*, 532 U.S. 275, 293 (2001) (no private right of action to enforce disparate-impact regulations promulgated under Title VI of Civil Rights Act of 1964).

The result advocated by Petitioner would contravene both *Stoneridge* and *Basic*. It would erode two important limitations on *Basic*'s sweeping expansion of the implied right of action: (i) the requirement that a plaintiff seeking the benefit of a fraud-on-the-market presumption "allege and prove" that the alleged misrepresentations are material and that the market for the securities is efficient, and (ii) the defendant's ability to rebut the presumption with "[a]ny showing that severs the link between [a defendant's] alleged misrepresentation and … the price received (or paid) by the plaintiff …." 485 U.S. at 248, n. 27. Consistent with *Stoneridge*, the Court should reject this expansion by ruling that a plaintiff cannot benefit from the fraud-on-the-market presumption at the class certification stage where loss causation is absent.

A. Loss Causation Is Relevant To Whether the Fraud-on-the-Market Presumption Can Be Established And Rebutted At The Class Certification Stage.

In *Basic*, the Court held that a putative class-action plaintiff was entitled to a rebuttable presumption of class-wide reliance if plaintiff could "allege and prove," among other things, that (i) the alleged misrepresentations were material, (ii) "the misrepresentations would induce a reasonable, relying investor to misjudge the value of the shares" and (iii) the securities were traded in an efficient market. *Id*. at 248, n. 27. To reach this result, *Basic* embraced the "fraud-on-the-market" theory, which holds that "where materially misleading statements have been disseminated into an impersonal, well-developed market for securities, the reliance of individual plaintiffs on the integrity of the market price may be presumed" because "*most publicly available information is reflected in the market price*" and "*an investor who buys or sells stock at the price set by the market does so in reliance on the integrity of that price*." *Id.* at 247 (emphasis added). The Court held that, in the absence of a fraud-on-the-market presumption, the predominance requirement of Fed. R. Civ. P. Rule 23(b)(3) could not be met because "[r]equiring proof of individualized reliance from each member of the proposed plaintiff class" would result in "individual issues . . . overwhelm[ing] the common ones." *Id.* at 242.

In *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005), the Court held that loss causation required proof that plaintiff's loss in share price was caused by the alleged material misrepresentation and not by other factors such as "changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events, which taken separately or together account for some or all of that lower price." *Id.* at 342-43. Under *Dura*, "a person who misrepresents the financial condition of a corporation in order to sell its stock becomes liable to a relying purchaser *for the loss the purchaser sustains when the facts . . . become generally known and, as a result, share value depreciates*." *Id.* at 344. (citing Restatement of Torts, 548A, comment b (internal quotations omitted) (emphasis added)).

Loss causation is directly linked to whether a plaintiff can establish the fraud-on-the-market presumption. If loss causation cannot be proven because no corrective event has had a negative impact on the stock price, this tends to prove at least one of two things: (i) the alleged misrepresentation was not material in the first place, or (ii) the market was not efficient with respect to the alleged misrepresentation. Either one is sufficient to find that the fraud-on-the-market presumption does not apply. *See Basic* at 248, n. 27 (quoting with approval and adopting the Sixth Circuit's holding that "in order to invoke the presumption, a plaintiff *must allege and prove*: (1) that the defendant made public misrepresentations; (2) that the misrepresentations were material; (3) that the shares were traded on an efficient market; (4) that the misrepresentations would induce a reasonable, relying investor to misjudge the value of the shares, and (5) that the plaintiff traded the shares between the time the misrepresentations were made and the time the truth was revealed") (emphasis added). *See also Ray v. Citigroup Global Markets, Inc.*, 482 F.3d 991, 995 (7th Cir. 2007) (affirming summary judgment because plaintiffs "have not introduced enough evidence to go forward on a fraud-on-the-market theory" where the "record affirmatively contradicts the assertion that the value of the SSOL's stock declined just when the alleged misrepresentations were revealed");[3] *Greenberg v. Crossroad Systems, Inc.*, 364 F.3d 657, 665 (5th Cir. 2004) ("to trigger the presumption plaintiffs must demonstrate that there is a *reasonable likelihood that the cause of the decline in price is due to the revelation of the truth* and not the release of unrelated negative information"); *see also* Daniel R. Fischel, *Use of Modern Finance Theory In Securities Fraud Cases Involving Actively Traded Securities*, 38 BUS. L. 1, 11 (1982) ("if there has been no such effect [on market price], it is more accurate to say that the plaintiff has not shown that there has been a fraud on the market and therefore is not entitled to recovery"); Jeffrey Oldham, *Comment, Taking "Efficient Markets" Out of the Fraud-on-the-Market Doctrine After the Private Securities*

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[3] Petitioner argues that the Seventh Circuit's decision in *Schleicher v. Wendt*, 618 F.3d 679 (7th Cir. 2010) is contrary to the Fifth Circuit's decision below. *Schleicher* cited with approval the Seventh Circuit's prior decision in *Ray v. Citigroup Global Markets*, which held that a plaintiff's inability to prove that a curative disclosure affected market price precluded recovery under a fraud-on-the-market theory. *Id.* at 683.

Litigation Reform Act, 97 NW. U. L. REV. 995, 1034 (2003) ("whether the alleged misstatement actually affected the market [price], i.e., loss causation" is a "question at the center of the presumption of reliance").

Even assuming the presumption applies, evidence that disproves loss causation also rebuts the fraud-on-the-market presumption. Under *Basic,* the fraud-on-the-market presumption is rebuttable by, among other things, a "show[ing] that the misrepresentation in fact did not lead to a distortion of price." 485 U.S. at 248 (discussing the Sixth Circuit's decision below). Indeed, "[*a*]*ny showing that severs the link between the alleged misrepresentation and … the price received (or paid) by the plaintiff* . . .will be sufficient to rebut the presumption of reliance." *Id.* (emphasis added).

The Second Circuit, the Circuit with the largest securities docket,[4] has recognized that the absence of loss causation rebuts the presumption of reliance. In *In re Salomon Analyst Metromedia Litigation*, for example, the Second Circuit vacated a trial court decision certifying a class where the trial court had refused to permit defendants to point to the absence of loss causation in order to rebut the presumption. Rejecting arguments similar to those advanced by Petitioner here, the Second Circuit remanded the case "to allow the district court to

[4] *See Morrison v. Nat'l Australia Bank Ltd.*, __ U.S. __ , 130 S. Ct. 2869, 2880 (2010) (referring to a decision of the D.C. Circuit Court of Appeals that deferred to the Second Circuit "because of its preeminence in the field of securities law.")(internal citations omitted).

permit defendants the opportunity to rebut the *Basic* presumption prior to class certification" by "*arguing for example, that market price was not affected by the alleged misstatements*" or that "other statements in the 'sea of voices' of market commentary were responsible for price discrepancies." 544 F.3d 474, 485-86 (2d Cir. 2008); s*ee also In re Flag Telecom Holdings, Ltd. Sec. Litig.*, 574 F.3d 29, 38 (2d Cir 2009) (noting with approval that "the lower court clearly considered the in-and-out traders' ability to prove loss causation as relevant to Plaintiffs' class certification motion" and that "lower courts have an 'obligation' to resolve factual disputes relevant to the Rule 23 requirements" which is "not lessened by overlap between a Rule 23 requirement and a merits issue")(internal citations omitted).

Similarly, the Third Circuit has recognized that the absence of a price reaction when information is disclosed shows that the information was not material in the first place, thus rebutting the presumption of reliance. In *In re Burlington Coat Factory Securities Litigation*, 114 F.3d 1410, 1419, n. 8 (3d Cir. 1997), for example, then-Circuit Judge Alito explained that "the presumption of reliance [*is*] *based on the theory that in an efficient market the misinformation directly affects the stock prices at which the investor trades and thus, through the inflated or deflated price, causes injury* even in the absence of direct reliance." Although class certification was not at issue, *Burlington* held that materiality under a fraud-on-the-market theory fails where corrective disclosures had no effect on price:

> *In the context of an 'efficient' market, the concept of materiality translates into information that alters the price of the firm's stock* . . . This is so because efficient markets are those in which information important to reasonable investors (in effect, the market) is immediately incorporated into stock prices . . . *Therefore, to the extent that information is not important to reasonable investors, it follows that its release will have a negligible effect on the stock price*. In this case, plaintiffs have represented to us that the July 29 release of information had no effect on BCF's stock price. This is, in effect, a representation that the information was not material.
>
> *Id.* at 1425(emphasis added) (internal citations and quotations omitted).

See also Oran v. Stafford, 226 F.3d 275, 282 (3d Cir. 2000) ("when a stock is traded in an efficient market, *the materiality of disclosed information may be measured post hoc by looking to the movement, in the period immediately following disclosure, of the price of the firm's stock*") (Alito, C.J.).

In *In re DVI, Inc. Sec. Litig.*, Nos. 08-8033 & 08-8045, 2011 WL 1125926 (3d Cir. Mar. 29, 2011), the Third Circuit, following Judge Alito's reasoning in *Burlington* and *Oran*, joined the Second Circuit in permitting the fraud-on-the-market presumption to be rebutted at the class certification stage by evidence that a corrective disclosure did not affect the market price of a security. *Id. at *8.* According to the Third Circuit, there were "several reasons" for this: (i) "a demonstration the market did not assimilate information about the security into the market price . . . when an alleged corrective disclosure occurred . . . may undercut the general claim of market efficiency or demonstrate market inefficiency relating to the securities in issue" and (ii) "[i]n an otherwise efficient market, the failure of a corrective disclosure to affect market price may . . . serve as a rebuttal to the presumption of reliance because it renders the misstatement immaterial as a matter of law." *Id.*

As the Third Circuit held in *In re DVI, Inc. Securities Litigation*, the same facts that show that information was immaterial on the merits also demonstrate that the materiality required for the presumption of reliance – and thus necessary for class certification – has not been shown. *See id.* And like the Third Circuit, the Fifth Circuit has simply applied the logic of *Burlington* to the fraud-on-the-market issue both on the merits and at the class certification stage. *See Nathenson v. Zonagen, Inc.*, 267 F.3d 400, 415 (5th Cir. 2001) (agreeing with *Burlington* and noting that "although there is generally a presumption that potentially significant publicly disseminated information is reflected in the price of stock traded on an efficient market, the presumption is rebuttable, and *where the facts properly considered by the district court reflect that the information in question did not affect the price of the stock then the district court may properly deny fraud-on-the-market based recovery*")(emphasis added); *see also Oscar Private Equity Investments v.*

Allegiance Telecom, Inc., 487 F.3d 261, 265 (5th Cir. 2007) (vacating class certification order and holding that the presumption may be rebutted by "a showing that the market price would not have been affected by the alleged misrepresentations" because "in such a case the basis for finding that the fraud had been transmitted through the market price would be gone").[5]

This could be improper only if merits issues and class certification issues always must fall in different categories. As we next show, that assertion is demonstrably wrong.

B. Loss Causation is Both a Merits Issue and a Class Certification Issue.

Petitioner argues that because loss causation is a merits issue, it should not be considered at the class certification stage of a 10b-5 case. (Pet. Br. at 46). But this Court has repeatedly rejected that argument, holding that merits issues and class certification issues can overlap. Indeed, *Basic* itself addressed the application of the fraud-on-the-market rebuttable presumption of reliance as both a merits issue and a class certification issue. *See* 485 U.S. at

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[5] To be clear, the Fifth Circuit does not require a plaintiff to establish, at the class certification stage, the "full quantification of damages" or show the exact "percentage of the [price] drop [that] was attributable to the corrective disclosure." *Oscar*, 487 F.3d at 271. Rather, the Fifth Circuit requires that plaintiffs make "some empirically-based showing that the corrective disclosure was more than just present at the scene." *Id.*

250 ("the District Court's certification of the class here was appropriate when made but is subject on remand to such adjustment, if any, as developing circumstances demand"); *see also id.* at 230 ("We granted certiorari . . . to determine whether the courts below *properly applied* a presumption of reliance in certifying the class, rather than requiring each class member to show direct reliance on Basic's statements") (emphasis added).

More generally, in *General Telephone Co. of the Southwest v. Falcon*, 457 U.S. 147 (1982), the Court held that the class certification decision requires a "rigorous analysis" of whether "the prerequisites of Rule 23(a) have been satisfied" which could entail "prob[ing] behind the pleadings" and considering issues that are "*enmeshed in the factual and legal issues compromising the plaintiff's cause of action*"' *Id.* at 160-161. (internal citations and quotations omitted)(emphasis added). *See also Amchem Prods.,* 521 U.S. 591, 615 (noting that Rule 23(b)(3) "invites a close look at the case before it is accepted as a class action")(internal citations omitted); *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 845, n. 20 (1999), (noting that where there is a "likelihood that significant questions, not only of damages but *of liability and defenses of liability*, would be present, affecting the individuals in different ways," class certification may not be appropriate)(emphasis added)(internal citations omitted).

Similarly, the comments to the 2003 Amendments to Rule 23 reflect that merits issues "relevant to making the certification decision on an informed basis" will be considered at the class certification stage:

> [D]iscovery in aid of the certification decision often includes information required to indentify the nature of the issues that actually will be presented at trial. In this sense it is appropriate to conduct controlled discovery into the "merits," limited to those aspects relevant to making the certification decision on an informed basis.
>
> Comments to 2003 Amendments to Rule 23.

See also In re Initial Pub. Offerings Sec. Litig. 471 F.3d 24, 42 (2d Cir. 2006) (rejecting the argument that a "district judge may not weigh conflicting evidence and determine the existence of a Rule 23 requirement just because that requirement is identical to an issue on the merits" and noting that "[a] district judge is to assess all of the relevant evidence admitted at the class certification stage and determine whether each Rule 23 requirement has been met, just as a judge would resolve a dispute about any other threshold prerequisite for continuing a lawsuit")(emphasis added).

The relationship between merits issues and class certification issues may be pictured as a Venn diagram, with merits and class certification issues forming two intersecting circles. Loss causation, like reliance, occupies the space where Rule 10b-5 merits issues and class certification issues intersect. This is because, as demonstrated above, evidence disproving loss causation is relevant to whether the fraud-on-the-market presumption can be established and/or rebutted and, in the absence of the presumption, a Rule 10b-5 claim cannot meet the predominance requirement of Rule 23(b)(3). *See Basic*, 485 U.S. at 242.

Nor does this open the door to all merits issues being considered as part of class certification in a securities or other class action. A merits issue such as scienter, unlike loss causation, has no connection to proving or rebutting the fraud-on-the-market presumption. To return to the Venn diagram illustration, scienter falls only in the circle of merits issues.

Petitioner is also incorrect that consideration of loss causation at the class certification stage would deprive class action plaintiffs of the right to a jury trial. This Court has held that nothing in the Seventh Amendment "inhibits" Congress or the Federal Rules from establishing heightened pleading requirements for raising individual issues in 10b-5 actions. *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 327-28 n. 9 (2007). This is because either Congress or the Federal Rules may "prescribe[] the means of making an issue, and [only] when the issue [is] made as prescribed, the right to trial by jury accrues." *Id.* at 328 (first two sets of brackets added) (quoting *Fidelity & Deposit Co. of Md. v. United States*, 187 U.S. 315, 320 (1902)). Likewise, Rule 23(b)(3) requires the trial court to make "findings" that class issues predominate over individual issues. Fed. R. Civ. P. 23(b)(3). Only if and when plaintiff satisfies this means prescribed by Rule 23(b)(3) for making class issues predominate, could any right to jury trial attach to any class issues.[6]

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[6] Petitioner also claims that *Basic* held that rebuttal of the presumption is a matter for trial, not class certification. Pet. Brf. at 24. *Basic's* full comment, which appears as *dicta* in a footnote, suggests the opposite:

> We note there may be a certain incongruity between the assumption that Basic shares are traded on a well-developed, efficient, and information-hungry market, and the allegation that such a market could remain misinformed, and its valuation of Basic shares depressed, for 14 months, on the basis of three public statements. *Proof of that sort is a matter for trial, throughout which the District Court retains the authority to amend the certification order as may be appropriate.*
>
> *Basic*, 485 U.S. at 249, n. 29 (emphasis added).

Thus, even when a district court has certified a class action, and a jury trial is underway, the court should decertify when the proof at trial rebuts the presumption of reliance. *See also id.* at 250 ("[t]he District Court's certification of the class . . . is subject on remand to such adjustment, if any, as developing circumstances demand"). Moreover, *Basic*, *id.* at 248, cited with approval the very footnote of the Sixth Circuit's decision below that made clear that a defendant has the opportunity to rebut the presumption at the class certification stage. *See Levinson v. Basic, Inc.*, 786 F.2d 741, 750, n.6 (6th Cir. 1986) ("*A defendant can defend against this presumption of reliance in two ways* . . . First,… a defendant can rebut proof of the five elements that give rise to the presumption") (emphasis added).

The United States, in its *amicus* brief, argues that plaintiff's inability to establish loss causation has no bearing on whether reliance may be presumed because *Basic*'s focus is on "the initial transaction, not on subsequent events that might (or might not) cause the plaintiff to suffer an economic loss." (U.S. Br. at 20). To support this argument, the United States posits hypothetical scenarios in which a purchaser buys a security at a falsely inflated price and then either sells it before the truth is made public or sells it after at a lower price that results from factors other than the material misrepresentation. In both scenarios, the United States argues, the purchaser may have relied on an initial purchase price that was inflated by a misrepresentation – thereby satisfying the *Basic* presumption – and yet loss causation cannot be proven. (U.S. Br. at 22).

The United States' hypotheticals oversimplify because they assume the unusual situation where the putative class plaintiff sells before any event corrected the alleged misrepresentation. In reality, such a plaintiff could not be certified as a class representative because it would both suffer no injury and therefore lack standing and be an inadequate and atypical representative. *See* Fed. R. Civ. P. 23(a). *Dura* holds that a plaintiff who sells before a corrective event tied to the challenged misrepresentation has not been injured. *Dura Pharm. Inc. v. Broudo*, 544 U.S. 336, 342 (2005). An uninjured plaintiff has neither standing nor satisfies adequacy and typicality. *Blum v. Yaretsky*, 457 U.S.

991, 999-1000 (1982); *Amchem Prods.*, 521 U.S. at 626. The typical putative class plaintiff has never sold, or sold only after what it claims was the corrective event.

Even assuming that the United States is correct in its atypical hypotheticals, this would simply mean that the absence of loss causation will not automatically destroy the fraud-on-the-market presumption in *all* cases. If, at the class certification stage, such unusual putative class plaintiffs can point to other facts demonstrating that they purchased the security at a falsely inflated price in an efficient market, even though no corrective event ever caused the price to decrease, plaintiffs may be able to establish the presumption of reliance despite the absence of loss causation. But, as a practical matter, a plaintiff who cannot show that any corrective event resulted in a price movement *at any time* will rarely, if ever, be able to show that, at the time of the purchase, the price of the stock was inflated by an alleged material misrepresentation in an efficient market. Rather, in the vast majority of cases, the absence of loss causation will constitute a "showing that severs the link between the alleged misrepresentation and . . . the price received (or paid) by the plaintiff . . . ." *Basic*, 485 U.S. at 248. Therefore, the fraud-in-the-market presumption will fail, and class certification will be denied because individual issues predominate.

Any other result would overburden the federal courts and the securities markets with improper class actions. A rule that prohibited courts from considering loss causation at the class certification stage would result in plaintiff classes being certified without the "rigorous analysis" required by *General Telephone Co.*, 457 U.S. 147, 161 (1982), and would shear the fraud-on-the-market presumption created by *Basic* of its own limits.

Such a result also would, contrary to *Stoneridge*, increase the "intense pressure to settle" that class actions create and permit "plaintiffs with weak claims to extort settlements from innocent companies" to the detriment of our economy. *Stoneridge*, 552 U.S. at 149; *In re Rhone-Poulenc Rorer, Inc.*, 51 F.3d 1293, 1298 (7th Cir. 1995) (Posner, J.) (noting that class action defendants are "under intense pressure to settle . . . Judge Friendly, who was not given to hyperbole, called settlements induced by a small probability of an immense judgment in a class action 'blackmail settlements'"). *See also* S. Rep. No. 109-14, at 20 (2005), reprinted in 2005 U.S.C.C.A.N. 11, 21 ("Hence, when plaintiffs seek hundreds of millions of dollars in damages, basic economics can force a corporation to settle the suit, even if it is meritless and has only a five percent chance of success. Not surprisingly, the ability to exercise unbounded leverage over a defendant corporation and the lure of huge attorneys' fees have led to the filing of many frivolous class actions."); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 740 (1975) (even a weak securities fraud complaint "has a settlement value to the plaintiff out of any proportion to its prospect of success at trial"). Thus, both *Basic* and *Stoneridge* support consideration of loss causation at the class certification stage.

II. LOSS CAUSATION IS ALSO PERTINENT TO THE CLASS CERTIFICATION ISSUES OF CLASS PERIOD AND MANAGEABILITY.

Loss causation is not only relevant at the class certification stage to the fraud-on-the-market presumption. Loss causation is also independently relevant to other class certification issues: (i) *class definition* -- whether the putative class period has an identifiable end; and (ii) *manageability* -- whether, where there are allegedly multiple successive corrective events and corresponding price drops, a broad plaintiff class would be unmanageable.

A. Loss Causation is Essential to Class Period Issues.

Loss causation is essential to deciding the class certification issues of class definition and class period. Fed. R. Civ. P. 23(c)(1)(B) provides that "an order that certifies a class action *must define the class*, and the class claims, issues, or defenses." Under Rule 23(c)(1)(B), the order certifying a class "must include (1) a *readily discernible, clear, and precise statement of the parameters defining the class or classes to be certified*, and (2) a readily discernible, clear, and complete list of the claims, issues or defenses to be treated on a class basis." *Wachtel v. Guardian Life Ins. Co. of Am.*, 453 F3d 179, 187-188 (3rd Cir. 2006)(emphasis added); *see also In Re Pharm. Indus. Average Wholesale Price Litig.*, 588 F.3d 24, 39 (1st Cir. 2009) ("Rule 23(c)(1)(B) explains the contents of a certification order: the order *must clarify and detail the identity of a class* and the class claims, issues, or defenses in a class action")(emphasis added). Indeed when a class is certified under 23(b)(3), the court must provide class members with "the best notice that is practicable under the circumstances" which must "clearly and concisely state," among other things, "(i) the nature of the action; (ii) *the definition of the class certified*; [and] (iii) the class claims, issues, or defenses." Fed. R. Civ. P. 23(c)(2)(B)(emphasis added).

A class cannot be defined without identifying the class period – when the plaintiff class begins and *ends*. *See In re Omnicom Group, Inc. Sec. Litig.*, No. 02 Civ. 4483, 2007 WL 1280640, *3 (S.D.N.Y. April 30, 2007) (class certification "concerns definition of the specific class, such as class claims, issues, defenses, and *the specific time period that the class covers*")(emphasis added). In a Rule 10b-5 class action, the class period begins with the first material misrepresentation or omission and ends when the market is "cured," – *i.e.*, "when the full truth has been disclosed to the market and the natural market forces have had a reasonable period of time to receive, digest and reflect the bad news in the market price of the security." *In re Oxford Health Plans, Inc. Sec. Litig.*, 191 F.R.D. 369, 378 (S.D.N.Y. 2000); *see also In re Fed. Nat'l Mortgage Ass'n Sec. Litig.*, 247 F.R.D. 32, 38-40 (D.D.C. 2008) (ending class period on date defendant disavowed financial statements causing a significant price drop); *In re Ribozyme Pharm., Inc. Sec. Litig.*, 205 F.R.D. 572, 579 (D. Colo. 2001) (class period ends when "curative information is publicly announced or otherwise effectively disseminated into the market"); *In re Sun Microsystems, Inc. Sec. Litig.*, No. C-89-20351-RPA, 1990 WL 169140, at *8 (N.D. Cal. Aug. 20, 1990) (the class period ends when "completely" "curative information is publicly announced or otherwise effectively disseminated").

Identifying the end of the class period requires identifying the curative event that effected a complete cure of the market price. That is also a loss causation issue. *See Dura*, 544 U.S. at 344 ("a person who misrepresents the financial condition of a corporation in order to sell its stock *becomes liable to a relying purchaser 'for the loss' the purchaser sustains 'when the facts . . . become generally known' and 'as a result' share value 'depreciate[s]*'") (emphasis added); Steven Serajeddini, *Note, Loss Causation and Class Certification*, 108 MICH. L. REV. 255, 269 (2009) ("[b]ecause loss causation defines the class, and the plaintiff bears the burden of showing that a class satisfies Rule 23, the plaintiff must demonstrate loss causation at class certification"). Where there is never a price drop resulting from a curative event, an end point for the class period cannot be identified and class certification must be denied.

This is illustrated by *In re Credit Suisse First Boston Corp. (Lantronix, Inc.) Analyst Sec. Litig.*, 250 F.R.D 137, 148 (S.D.N.Y. 2008). In *Lantronix*, plaintiffs alleged that a stock analyst's reports violated Rule 10b-5 because they touted the company's stock as a buy even though the analyst held unexpressed reservations about the company. At the class certification stage, Plaintiffs argued that the class period ended on September 12, 2002, when the New York Times ran an article revealing that the analyst had "advised investors to buy shares of a company that he acknowledged in an email message were unworthy of purchase," and pointed to a significant drop in the company's stock price on the same day. 250 F.R.D. at 139. After analyzing the likely causes of the drop in the company's stock price on that day, the court declined to certify the class because other bad news about the company was released for the first time on September 12, 2002 that, the court determined, was the more likely cause of the decline in market price on that day. *Id.* 149. Consequently, the trial court found that there was "insufficient evidence of market impact at the close of the Class Period" to end the class period and denied class certification. *Id.* at 148. *Lantronix* illustrates that the need to define and end a class period provides an independent basis to consider loss causation when a 10b-5 plaintiff seeks class certification.

B. Loss Causation Is Also Pertinent To Determining Whether A Proposed Plaintiff Class Action is Manageable.

Fed. R. Civ. P. Rule 23(b)(3)(D) expressly requires courts to consider "the likely difficulties in managing a class action" as part of the class certification determination. *See Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 164 (1974) (noting that the manageability requirement "encompasses the whole range of practical problems that may render the class action format inappropriate for a particular suit"). A class should only be certified where "a class action would achieve economies of time, effort, and expense, and promote . . . uniformity of decision as to persons similarly situated, without sacrificing procedural fairness or bringing about other undesirable results." *Amchem Prods.*, 521 U.S. at 615 (quoting Advisory Committee Notes to the 1966 Rule 23 amendments). In a fraud-on-the-market case, courts may properly consider loss causation during the class certification stage in order to determine whether a broad plaintiff class is manageable, efficient, and fair.

For example, in a case where multiple curative events allegedly occurred over a period of time, the certification of a single broad plaintiff class may be unmanageable and inefficient. Purchasers and sellers of the stock at different times will have different reliance and loss causation issues, which is certainly pertinent to the predominance and manageability requirements. *See* John C. Coffee, Jr. *Securities Litigation: The Year Ahead*, 245 N.Y.L.J. 5 (Jan. 20, 2011) ("in a case where there was a multi-year class period and where multiple statements were alleged to be inaccurate and multiple corrective disclosures were made, the market's response to each such corrective disclosure represents a distinct issue for purposes of Rule 23(b)(3)'s predominance [requirement]").

Indeed, if a class were certified in such circumstances, conflicts may well emerge among subgroups who sold their stock at various points in time throughout the class period. Some will have sold before any curative events occurred, some before curative events were complete, some after all curative events had been absorbed by the market, and some will never have sold. Inter-class conflicts could exist, for example, as to how fairly to divide any settlement proceeds. Such potential conflicts are relevant to whether a broad plaintiff class is unmanageable or inefficient. *See Amchem Prods.*, 521 U.S. at 626 (affirming denial of class certification where, among other things, "the interests of those within the single class are not aligned").

Rule 23(c)(5) permits, "[*w*]*hen appropriate*, a class [to] be divided into subclasses that are each treated as a class under this Rule." Fed. R. Civ. P. 23(c)(5). *See e.g.*, *Ohman v. Kahn*, No. 87 Civ. 7117, 1990 U.S. Dist. LEXIS 7781, *4-5 (S.D.N.Y. June 27, 1990) (creating three subclasses based on when class members purchased their shares). But a proposed class action that might need multiple subclasses – and thus, multiple sets of attorney fees in the event of a settlement or judgment for plaintiff – would be less manageable and efficient than the typical class action that has no subclasses. A trial court should thus consider whether loss causation-related differences among subgroups within a broad class renders a proposed class unmanageable, inefficient, or unfair.

CONCLUSION

The decision of the court of appeals should be affirmed.

Respectfully submitted,

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