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In *Amgen Inc. v. Connecticut Retirement Plans*, the Supreme Court handed a victory to plaintiffs pursuing Rule 10b-5 securities fraud cases by making it easier to obtain class certification. By a 6-3 margin, the Court declined to require plaintiffs to prove that the alleged misstatements were "material" to obtain class certification, deferring that issue to a motion for summary judgment or trial on the merits. The Court was not persuaded by defense concerns that certification of a class imposes immense settlement pressure on defendants.

Since *Basic Inc. v. Levinson*, 485 U.S. 224 (1988) ("*Basic*"), the Court has permitted class certification in securities cases based on a "rebuttable presumption" that all investors relied on the price of the stock set by an efficient securities market, and that stock price is influenced by material statements by the defendant. Thus, plaintiffs are unquestionably required to prove materiality in order to win the case. However, the Court ruled that because materiality is judged by an "objective" standard, the issue should await trial (or summary judgment) because all investors are impacted identically by a finding of materiality (*i.e.*, if it is found at trial that the alleged misrepresentations were not material, the entire class would lose).

Significantly, four justices questioned the viability of the "fraud on the market" theory adopted in *Basic*, while the majority simply noted that Amgen had not challenged the viability of that presumption.

The *Amgen* decision is significant for several reasons. First, it ends a trend of Supreme Court decisions making it harder to use class actions against corporate defendants. Also, as noted above, the Court rejected the argument that making class certification more readily available would encourage the settlement of frivolous cases, saying Congress had addressed this concern when it enacted the Private Securities Litigation Reform Act of 1995 ("PSLRA").

"Fraud-on-the-market" theory

Under Federal Rule of Civil Procedure 23, to obtain class certification in a securities fraud case under Rule 10b-5, the plaintiff must demonstrate, among other requirements, that common questions "predominate" over individual issues. Because one of the important elements of a Rule 10b-5 cause of action is "reliance" on the alleged misrepresentation, individual reliance issues would appear to preclude class certification. Indeed, in *Basic*, the Supreme Court recognized that requiring each class member to prove reliance on the alleged misrepresentation would cause individual questions to "overwhelm" common questions, and thereby preclude class certification. However, over a strong dissent, a four-justice majority in *Basic* adopted the "fraud-on-the-market" theory, which permits a "rebuttable presumption" of reliance on alleged misrepresentations to the public if the stock trades in an efficient securities market. The Court held that an efficient market incorporates all material information and that all investors presumptively rely on the resulting price of the stock.

To invoke the fraud-on-the-market theory, a plaintiff must demonstrate three predicates: (1) the market for the security was efficient; (2) the alleged misrepresentation was public; and (3) the plaintiff traded shares between the time of the alleged misrepresentation and the time when the truth was revealed. See *Basic*, 485 U.S. at 248 n.27.

The *Amgen* decision

In *Amgen*, the plaintiff sued Amgen alleging misrepresentations about the safety, efficacy and marketing of two flagship drugs.

Plaintiff claimed these misrepresentations artificially inflated the stock price, which declined when the truth was revealed. Plaintiff sought to certify a class of investors who purchased Amgen stock between the time of the first alleged misrepresentation and the time the truth was revealed.

In seeking class certification, the plaintiff invoked the fraud-on-the-market presumption to support its assertion that common issues predominated, but did not prove the statements at issue were material. Amgen argued that a class should not be certified because the plaintiff had failed to demonstrate the alleged misrepresentations were material. Amgen also sought to introduce evidence showing that the market was well-aware of the truth, so the statements could not have been material to investors. Because immaterial misstatements by definition do not affect a stock's price, Amgen claimed there was no basis to presume reliance.

The plaintiff countered that demonstrating materiality was not required to obtain class certification because materiality should be decided on a class-wide basis at trial. The district court rejected Amgen's arguments and granted class certification. The United States Court of Appeals for the Ninth Circuit agreed with the district court, allowing class certification to stand. Other Courts of Appeals, however, had disagreed and had required plaintiffs to prove materiality to obtain class certification. The Supreme Court heard the case to resolve this dispute and to determine (1) whether district courts must require plaintiffs to prove materiality to obtain class certification, and (2) whether district courts must allow defendants to present evidence rebutting materiality before granting class certification.

On February 27, 2013, the Supreme Court affirmed the lower courts, holding that plaintiffs need not prove materiality to invoke the fraud-on-the-market theory and its presumption of class-wide reliance. In doing so, the Court reasoned that materiality is common to all class members because it is based on an "objective standard" (*i.e.*, would a reasonable investor have considered the information important in making an investment decision). Indeed, if a securities case goes to trial and the judge or jury find the statement was not material, all class members lose the case. Thus, to obtain class certification under FRCP 23(b)(3), a Rule 10b-5 plaintiff need not prove materiality and the defendant may not rebut the materiality of the alleged misrepresentations.

Significantly, the Court rejected Amgen's argument that policy considerations, including the pressure to settle meritless litigation, should require proof of materiality at the certification stage. The Court ruled that Congress had already addressed these policy issues through enactment of the PSLRA, and the Court declined to adopt additional limiting measures.

Practical considerations

Because of the Court's ruling, defendants may not attack the materiality of the alleged misrepresentations in opposing class certification. This issue can arise in motions to dismiss and later in the litigation, such as a motion for summary judgment or at trial. A clear lack of materiality can be persuasive at these stages of the case. That said, the *Amgen* decision favors Rule 10b-5 plaintiffs by making class certification more easy to obtain.

It is also important to note that the *Amgen* decision does not affect the majority of cases, where the main defense is that the statements were not false and were not made with scienter. Allegations of falsity and scienter by plaintiffs must still meet the heightened pleading standards of the PSLRA.

If you have questions about this *Alert*, please contact a member of your Cooley team or one of the attorneys listed above from the Securities Litigation group.

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