CLASS ACTIONS & DERIVATIVE SUITS
AMERICAN BAR ASSOCIATION SECTION OF LITIGATION

CASE NOTES

The Death Knell of the Class Certification Minitrial

Amgen, Inc. v. Connecticut Retirement Plans and Trust Funds (No. 11-1085) (Feb. 27, 2013)

Striking a blow to the securities class-action defense bar, the U.S. Supreme Court issued its opinion in Amgen, Inc. v. Connecticut Retirement Plans and Trust Funds (No. 11-1085) (Feb. 27, 2013), holding 6-3 that plaintiffs need not establish the materiality of an alleged misstatement at the class-certification stage in order to invoke the "fraud-on-the-market" theory. The Court also held that in such cases, federal district courts are not required to allow defendants to present evidence rebutting the applicability of the fraud-on-the-market theory before certifying a plaintiff class, where such evidence solely rebuts materiality.

Before a class can be certified in Section 10(b) securities fraud cases, Federal Rule of Civil Procedure 23 requires the plaintiff to convince the district court that the element of reliance is common to the entire class. Recognizing that the large class sizes typical to securities fraud class actions would normally make such a showing impossible, the Supreme Court, in Basic, Inc. v. Levinson, 485 U.S. 224 (1988), held that plaintiffs can establish a presumption of class-wide reliance (in appropriate cases) by invoking the "fraud-on-the-market" presumption—i.e., that the market price of a security traded in an efficient market incorporates all public and material information available, and therefore that all buyers of that security are presumed to have relied (albeit indirectly) on the truthfulness of that information in deciding whether to purchase. That is, if the fraud-on-the-market presumption applies, the element of common reliance is presumed to have been satisfied because it is assumed that buyers and sellers who rely on the integrity of the market price also necessarily rely on any material misrepresentations reflected in that price.

As recently as two terms ago, the Court affirmed that plaintiffs seeking to invoke the fraud-on-the-market theory are required to show (1) that the alleged misrepresentations were publicly known; (2) that the stock in question had traded in an efficient market; and (3) that the plaintiffs had bought or sold the stock "between the time the misrepresentations were made and the time the truth was revealed." Erica P. John Fund, Inc. v. Halliburton Co., 131 S. Ct. 2179, 2185 (2011). Perhaps forecasting the result in Amgen, the Court in Halliburton held that securities fraud plaintiffs also did not need to prove loss causation at the class certification stage when invoking the fraud-on-the-market doctrine, because requiring them to do so would "contravene[] Basic's fundamental premise—that an investor presumptively relies on a misrepresentation so long as it was reflected in the market price at the time of [the] transaction." 131 S. Ct. at 2186. But until its decision in Amgen, the Court had not resolved (and the federal appellate courts had divided on) the question of whether in addition to these requirements, a plaintiff was also

required at the class-certification stage to prove that the alleged misrepresentations were material—an element of the claim that is reserved normally for consideration on the merits.

In Amgen, Connecticut Retirement Plans and Trust Funds (Connecticut) brought claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 against Amgen, Inc., a biotechnology company, alleging that Amgen had misstated and failed to disclose safety information about two of its products used to treat anemia, and that these actions artificially altered Amgen's stock price The district court granted Connecticut's motion for class certification based on the fraud-on-the-market theory, finding that Amgen's stock traded in an efficient market, and that the alleged misstatements were public. The district court further held, over Amgen's objection, that Connecticut need only allege—rather than prove—that Amgen's purported misstatements were material, and that Amgen could not rebut application of the fraud-on-the-market theory with evidence of immateriality at the class-certification stage. Amgen filed an interlocutory appeal with the Ninth Circuit, which affirmed. In so doing, the court of appeals noted that proof of materiality is not necessary to ensure the commonality of reliance among prospective class members, and thus had no place in class-certification proceedings premised on the fraud-on-the-market doctrine. Moreover, the court pointed out that because materiality is a necessary element of a securities fraud claim, requiring plaintiffs to prove it during class certification would effectively transform such proceedings into mini-trials on the merits, and functionally telegraph the outcome of plaintiff's individual case if class certification was denied.

A six-justice majority affirmed that decision. (Justice Alito concurred with the opinion of the Court, but only on the assumption that Amgen had not asked the Court to revisit the soundness of Basic's fraud-on-the-market theory, which he felt might be appropriate in light of "more recent evidence" indicating that it rests on a "faulty economic premise." Slip Op. 16.) Writing for the Court, Justice Ginsburg drew a hard line between what is required to invoke the fraud-on-the-market theory under Basic, and what Rule 23(b)(3) demands in order to certify a class. This case, she wrote, rested entirely on the latter question. And thus while the Court affirmed that materiality is an indispensable element of the fraud-on-the-market theory, it noted that that conclusion alone did not answer whether proof of materiality at the class certification stage was necessary to ensure, under Rule 23(b)(3), that questions common to the class "predominate over any questions affecting only individual members." Slip Op. 10.

Rule 23(b)(3), the Court held, does not require such proof, and is instead concerned only with whether common questions regarding those elements predominate over those affecting individual class members. The Court also clarified its statement in Wal-Mart Stores, Inc. v. Dukes, 131 S. Ct. 2541, 2551 (2011), that district courts must engage in a "rigorous" analysis of the issues at the class certification stage, and that such analyses may "entail some overlap with the merits of the plaintiff's underlying claim." Noting that this generally remained true, the Court nevertheless clarified that "Rule 23 grants courts no license to engage in free-ranging merits inquiries at the certification stage," and that "[m]erits questions may be considered to the extent—but only to the extent—that they are relevant in determining whether the Rule 23 prerequisites for class certification are satisfied." Slip. Op. 9.

Thus, the Court first noted that because materiality is determined under an objective standard that does not take individual class members into account, it was by its nature a "common question" under Rule 23 that could be established through common evidence. Perhaps more important, though, the Court held that because materiality is a necessary element of a Section 10(b) claim, there was absolutely no risk that a failure to prove materiality on the merits would unravel the district court's determination that class certification was appropriate. That is, because the class would be required to prove materiality in order to succeed at trial, a failure to do so necessarily meant that the entire class would either stand or fall together—there could never be a situation in which a failure to prove materiality was fatal to some claims but not others.

The Court therefore concluded that there was no need to require proof of materiality at class certification because even if conclusively established, it would have no bearing on whether the class had been properly certified. Similarly, the Court rejected Amgen's argument that it should have been allowed to introduce evidence to rebut materiality because, even if it had done so, the rebuttal evidence would not affect whether the class could be certified under Rule 23.

Putative securities class-action plaintiffs can therefore breathe a little easier after Amgen, safe in the knowledge that, for the time at least, they need not prepare themselves for a full "minitrial" on the merits of their case before class certification can be granted. Rule 23 remains on the horizon, with a soon-to-be-decided Comcast v. Behrend (No. 11-864), which presents the question of whether a district court faced with expert testimony on the existence of class-wide damages can certify a class without first determining that the expert's opinions are admissible under Daubert v. Merrell Dow Pharmaceuticals, Inc., 509 U.S. 579 (1993). And while the case itself arises under the Sherman Act, there is no reason to believe that the Court's decision will be cabined to that particular area of the law.

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