ALERTS

Supreme Court Rules Securities Class Action Plaintiffs Need Not Prove Materiality at Class Certification Stage

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On Feb. 27, 2013, the U.S. Supreme Court ruled that securities fraud class action plaintiffs are not required to prove the materiality of alleged misstatements as a prerequisite to class certification. The decision, in *Amgen Inc. v. Connecticut Retirement Plans and Trust Funds*, No. 11-1085, 568 U.S. ___ (2013), resolves a conflict among several Courts of Appeals over whether district courts must require plaintiffs to prove, and permit defendants to rebut, the materiality element before certifying a Rule 10b-5 claim.

In *Amgen*, Connecticut Retirement Plans and Trust Funds ("Connecticut Retirement") brought a securities fraud class action against Amgen Inc. and several of its officers ("Amgen"), alleging that the market price for Amgen stock was artificially inflated due to alleged misrepresentations and omissions regarding two of Amgen's flagship products. Connecticut Retirement moved to certify the action as a class under Federal Rules of Civil Procedure 23(a) and 23(b)(3) on behalf of certain purchasers of Amgen stock. Connecticut Retirement invoked the fraud-on-the-market presumption, endorsed by the Supreme Court in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), to establish the reliance element of its Rule 10b-5 claim.

The fraud-on-the-market presumption allows courts to presume that the price of a security traded in an efficient market will reflect all publicly available information about a company and that, accordingly, a buyer of the security may be presumed to have relied on that information in

purchasing the security. Absent the fraud-on-the-market theory, individual reliance issues will typically preclude class certification, making it impossible for plaintiffs to show that common questions predominate over questions affecting only individual members.

In *Amgen*, Amgen conceded that its stock was traded in an efficient market and that the alleged misstatements were public. It argued, however, that the plaintiffs could not rely on the fraud-on-the-market doctrine in seeking class certification because the alleged misstatements were immaterial. The theory underpinning Amgen's argument was that because immaterial information, by definition, does not affect market price, it cannot be relied upon by investors whose reliance on public information under the fraud-on-the-market theory is presumed because of the integrity of the market price.

The Supreme Court viewed the "pivotal inquiry" as "whether proof of materiality is needed to ensure that the *questions* of law or fact common to the class will predominate over any questions affecting only individual members as the litigation continues." *Amgen Inc. v. Connecticut Retirement Plans and Trust Funds*, No. 11-1085, slip op. at 10, 568 U.S. ___ (2013) (emphasis in original; quotation marks and citation omitted). In a 6-to-3 decision, the Court held that the answer to that question was "clearly no." *Id.* (quotations omitted).

The Court provided two reasons for its holding. First, materiality is an objective question involving the significance of an omitted or misrepresented fact to a reasonable investor which can be proved by evidence common to the class. Accordingly, the answer, whatever it ultimately is, will be a common one. *Id.* at 11. Second, the Court reasoned there is no risk that failing to prove materiality by classwide evidence would result in "individual questions predominating" because it would "end the case for one and for all." *Id.* The Court explained, therefore, that "the potential immateriality of Amgen's alleged misrepresentations and omissions is no barrier to finding that common questions predominate," and, accordingly, "proof of that sort is a matter for trial." *Id.* at 25, 26.

The Supreme Court's ruling in *Amgen* will likely make it easier for securities class action plaintiffs to pass the certification stage, which, as Amgen argued, puts substantial pressure on defendants to settle a case rather than continue litigation. But the Court rejected this "policy consideration," acknowledging that Congress has already enacted legislation geared to address the settlement pressure associated with

securities fraud class actions "through means other than requiring proof of materiality at the class certification stage" and "rejected calls to undo the fraud-on-the-market presumption of classwide reliance." *Id.* at 19, 20.

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