A “Plausible” Allegation of Materiality and Rebutting the Presumption of Reliance at Class Certification

*Connecticut Retirement Plans & Trust Funds v. Amgen Inc.*

Securities litigation is usually in the form of a class action because the class action aggregates otherwise de minimus claims. Federal Rule of Civil Procedure 23 states that to obtain class certification, the class must be so numerous that joinder of all members is impracticable, questions of law or fact are common to the class, the claims or defenses of the representative parties are typical of the class, and the representative parties will fairly and adequately protect the interests of the class. In securities litigation, one of the most contested issues is whether the plaintiff has adequately demonstrated that the element of reliance is common to the class.

Reliance can be shown on class certification by invoking the fraud-on-the-market presumption—the principle that the market price of a security traded in an efficient market reflects all public information and therefore that a buyer of the security is presumed to have relied on the truthfulness of that information in purchasing the security. See *Erica P. John Fund, Inc. v. Halliburton Co.*, 131 S. Ct. 856 (2011).

The Ninth Circuit in *Connecticut Retirement Plans & Trust Funds v. Amgen, Inc.*, No. 09-56965, 2011 WL 5341285 (9th Cir. Nov. 8, 2011), addressed what a plaintiff must do to invoke the fraud-on-the-market presumption in aid of class certification. The court made two holdings of note. First, the court held that plaintiff must (1) show that the security in question was traded in an efficient market, and (2) show that the alleged misrepresentations were public. As for the element of materiality, the plaintiff must plausibly allege—but need not *prove*—that the
claimed misrepresentations were material. The court said that “[p]roof of materiality, like all other elements of a 10b–5 claim, is a merits issue that abides the trial or motion for summary judgment.” Second, the court held that rebuttal of the fraud-on-the-market presumption, at least by showing that the alleged misrepresentations were not material, is a matter for trial or summary judgment, not a matter to be taken up in a class certification motion.

Connecticut Retirement Plans and Trust Funds sued Amgen Inc. and several of its officers, alleging that they violated the federal securities laws by misstating and failing to disclose safety information about two Amgen products used to treat anemia (a red blood cell deficiency). According to the complaint, Amgen downplayed the FDA’s safety concerns about its products in advance of an FDA meeting with a group of oncologists, concealed details about a clinical trial that was canceled over concerns that Amgen’s product exacerbated tumor growth in a small number of patients, exaggerated the FDA-approved uses of its products, and misrepresented its marketing practices by claiming that it promoted its products solely for onlabel uses. The plaintiffs alleged that those misstatements and omissions inflated the price of Amgen’s stock when Connecticut Retirement purchased it, and that later, corrective disclosures caused Amgen’s stock price to fall, injuring Connecticut Retirement.

Connecticut Retirement moved to certify a class. Amgen proposed rebuttal evidence purportedly negating reliance by showing that the truth behind each of the alleged misstatements had already entered the market. (This is known as the “truth-on-the-market” defense). The district court granted the motion. According to the district court, Connecticut Retirement successfully invoked the fraud-on-the-market presumption of reliance by showing that Amgen’s stock traded in an efficient market (which Amgen conceded) and that the alleged misstatements were public (which Amgen did not contest). The district court further held that at the class certification stage, Connecticut Retirement did not need to prove—but rather could merely allege—that Amgen’s supposed falsehoods were material to invoke the fraud-on-the-market presumption. Last, the district court declined to afford Amgen an opportunity to rebut the presumption of reliance at the class certification stage, holding that rebuttal was a matter for trial. On
appeal, the Ninth Circuit affirmed the district court’s decision.

I. Materiality

First, the court joined the Seventh and Third Circuits and held that materiality was a matter for trial, and that the plaintiffs only had to plausibly allege materiality on class certification. The court stated:

The problem with [the defendant’s] argument is that, because materiality is an element of the merits of their securities fraud claim, the plaintiffs cannot both fail to prove materiality yet still have a viable claim for which they would need to prove reliance individually. See Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 341 (2005). If the misrepresentations turn out to be material, then the fraud-on-the-market presumption makes the reliance issue common to the class, and class treatment is appropriate. But if the misrepresentations turn out to be immaterial, then every plaintiff’s claim fails on the merits (materiality being a standalone merits element), and there would be no need for a trial on each plaintiff’s individual reliance. Either way, the plaintiffs’ claims stand or fall together—the critical question in the Rule 23 inquiry.

The court noted that a footnote in Basic Inc. v. Levinson, 485 U.S. 224 (1988), simply states that the court of appeals deemed materiality essential, but the Supreme Court did not adopt it as a precondition to class certification. Moreover, the court continued, the Court in Erica P. John Fund and Dukes, required the plaintiff to show that the stock was traded in an efficient
market but did not mention materiality as a requirement.

Second, the court held that the district court correctly required the plaintiffs to prove that the market was efficient and that the statements were public. The court relied upon the Supreme Court’s recent decision in Wal-Mart Stores Inc. v. Dukes, 131 S. Ct. 2541, 2551 (2011), where the Court stated that “What matters to class certification ... is not the raising of common ‘questions’—even in droves—but, rather the capacity of a classwide proceeding to generate common answers apt to drive the resolution of the litigation. Dissimilarities within the proposed class are what have the potential to impede the generation of common answers.” The Ninth Circuit side-stepped the issue of what standard of proof is required, but explained that:

By contrast, the elements of the fraud-on-the-market presumption—whether the securities market was efficient and whether the defendant’s purported falsehoods were public—are not elements of the merits of a securities fraud claim. . . . Thus, if the plaintiffs failed to prove those elements, they could not use the fraud-on-the-market presumption, but their claims would not be dead on arrival; they could seek to prove reliance individually. That scenario, however, would be inappropriate for a class proceeding.

The court concluded that proof of materiality is not necessary to ensure that the question of reliance is common among all prospective class members’ securities fraud claims, and thus plaintiffs need not prove materiality to avail themselves of the fraud-on-the-market presumption of reliance at the class certification stage. The court reiterated that plaintiffs need only allege materiality with sufficient plausibility to withstand a 12(b)(6) motion.

II. Opportunity to Rebut the Presumption at Class Certification

The Ninth Circuit also held that the defendants could not rebut the fraud-on-the-market presumption until trial. Specifically, the court noted, Amgen tried to introduce the “truth-on-the-market defense. Under the truth-on-the-market defense, if, despite the defendants’ allegedly fraudulent attempt to manipulate market price, the truth credibly entered the market and dissipated the effects of the misstatements, then those who traded after the
corrective statements could not claim reliance.

But the Ninth Circuit, relying upon *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083 (1991), held that the truth-on-the-market defense is a method of refuting an alleged misrepresentation’s materiality, and as such, “is a merits issue to be reached at trial or by summary judgment motion if the facts are uncontested.”