

The Supreme Court's Recent Securities Litigation Cases

September 7, 2011

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Agenda

- Introduction
- Presentation
- Questions and Answers — (anonymous)
- Slides — now available on front page of Securities Docket
 - www.securitiesdocket.com
- Wrap-up

Webcast Series

- Approximately every other week
- September 8: “**Anti-Corruption Enforcement and Compliance Update**”

Panel



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Presented By Jordan Eth & Deanne Maynard

Presentation Overview

1. October 2010 Decisions: *Matrixx; Halliburton; Janus*
2. October 2011 Case: *Simmonds*
3. Themes
4. Observations
5. Questions & Answers

1. October 2010 Decisions

Matrixx Initiatives, Inc. v. Siracusano,
131 S. Ct. 1309 (2011)
Materiality & Scierter

Matrixx: Background

- **Claims:** Alleged failure to disclose that cold remedy product (Zicam) was linked to loss of smell.
- **Key Facts:**
 - Zicam constituted 70% of revenue
 - Doctors reported possible link
 - Doctors planned a presentation regarding the link
 - 9 plaintiffs filed 4 lawsuits
 - FDA looking into link
 - Matrixx stated its belief that “[link] completely unfounded and misleading”
 - Two weeks later, Matrixx 8-K stated that there was “insufficient scientific evidence ... to determine if [Zicam] affects a person’s ability to smell”

Matrixx: Background

- **History:** District court granted motion to dismiss; Ninth Circuit reversed.
- **Issue:** Can plaintiff state a claim based on failure to disclose reports of adverse events where adverse events are not statistically significant?
- **Result:** Affirmed.
- **Unanimous opinion by:** Justice Sotomayor

Matrixx: Materiality

- Per se approach would “necessarily be overinclusive or underinclusive.”
- Adverse event is material if it would “significantly alter the total mix of information.”
- “[A]ssessing the materiality of adverse events reports is a fact specific inquiry. . . [t]his is not to say that statistical significance (or lack thereof) is irrelevant – only that it is not dispositive over every case.”
- “[M]edical professionals and regulators act on the basis of evidence of causation that is not statistically significant.”

Matrixx: No Duty to Disclose

- Securities law is about speech – not silence.
- “Moreover it bears emphasis that § 10(b) and rule 10b-5(b) do not create an affirmative duty to disclose any and all material information Even with respect to information that a reasonable investor might consider material, companies can control what they have to disclose under these provisions by controlling what they say to the market.”

Matrixx: ScienTer Analysis

- Court “must review all allegations holistically” under *Tellabs*.
- Matrixx “sufficiently” concerned about product that it hired a consultant to review, asked expert to participate in animal studies, and convened a panel.
- Matrixx issued press release suggesting that studies confirmed product did not cause loss of smell when it had not conducted any studies.
- Matrixx prevented researcher from using product’s name in presentation.

Matrixx: Implications

- **Counseling**
 - *The Kindergarten Rule*
 - *Warren Buffett*
- **Litigation**
 - *Changes Scierter Analysis?*

Erica P. John Fund, Inc. v. Halliburton Co.,
131 S. Ct. 2179 (2011)
Class Certification

Halliburton: Background

- **Claims:** Halliburton shareholders alleged that the company deliberately made false statements about (1) asbestos litigation liability, (2) expected revenue, and (3) benefits of a merger.
- **History:** Plaintiffs survived a motion to dismiss, but failed to obtain class certification because they did not establish loss causation. The Fifth Circuit affirmed denial of class certification.
- **Issue:** Must a securities fraud plaintiff prove loss causation at the class certification stage?
- **Result:** Vacated and remanded.
- **Unanimous Opinion By:** Roberts, C.J.

Halliburton: Basic Revisited

- Class certification requires commonality as to the element of reliance
- *Basic's* presumption of reliance turns on market efficiency
- Loss causation requirement is “not justified by *Basic* or its logic” and in fact “contravenes *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 his transaction.”

Halliburton: Implications

It Could Have Been A Blockbuster

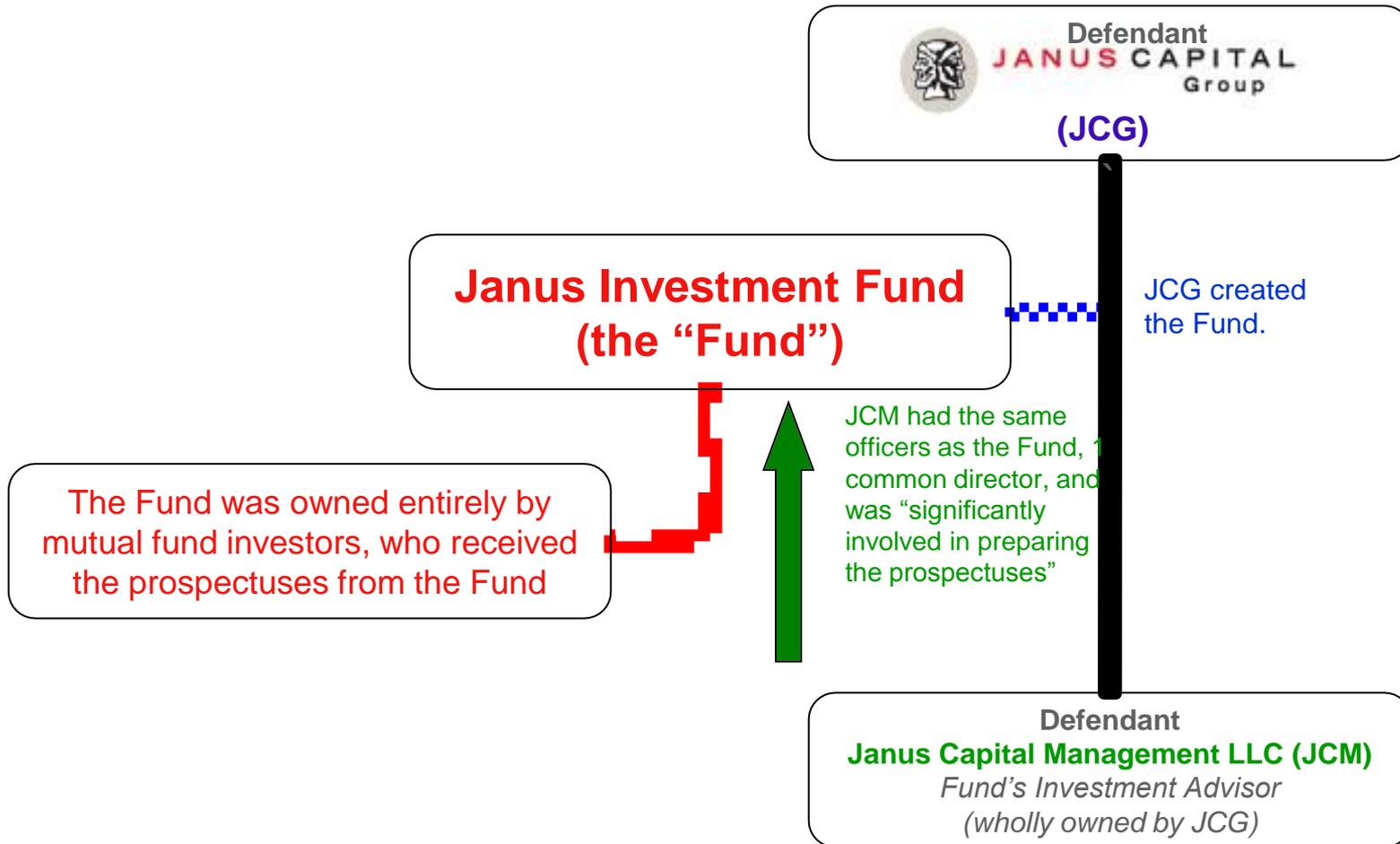
- Loss causation is a key part of cases
 - Often never squarely addressed
 - Strong statement of requirement, though (decline “because of the correction to a prior misleading statement”)
- *Basic* itself could have been challenged
 - 4-2 decision (Blackmun, Brennan, Marshall & Stevens; Rehnquist, Scalia, and Kennedy did not participate)
 - Rebuttable or conclusive presumption? When/how challenged?

Halliburton: Implications

- **Minor impact:** Decision does not change the law in any circuit but the Fifth.
- **Status Quo:** “Fraud-on-the market” presumption remains intact and unchanged.

Janus Capital Group Inc. v. First Deriv. Traders,
131 S. Ct. 2296 (2011)
Primary Liability for Making Statements

Janus: Background



Janus: Background

- **History:** District Court dismissed complaint; Fourth Circuit reversed.
- **Issue:** Whether mutual fund investment adviser can be held liable under Rule 10b-5 for statements in its client's mutual funds' prospectuses.
- **Result:** Reversed.
- **5-4 Decision:** Thomas for the court; Breyer dissent.

Janus: Rationale

- Section 10(b) is an “implied private right of action”
- “concerns with the judicial creation of a private cause of action caution against its expansion”
- “Congress did not authorize . . . and did not expand when it revisited the law,” so “narrow dimension.”

Janus: Rationale

LINGUISTIC:

- “One makes a statement by stating it.”
- “Even when a speechwriter drafts a speech, the content is entirely within the control of the person who delivers it. And it is the speaker who takes the credit – or the blame – for what is ultimately said.”
- “For the purposes of Rule 10b-5, the maker of the statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it.”

Janus: Rationale

FOLLOWS PRECEDENT:

- *Central Bank* eliminated aiding and abetting liability.
- A broad reading of “make” would hold aiders and abettors primarily liable.
- *Stoneridge* restricts primary liability unless disclosure of deception is “necessary or inevitable.”

Janus: Breyer Dissent

- **“Ultimate Authority” is the wrong test.** “[D]epending on the circumstances, a management company, a board of trustees, individual company officers, or other others, separately or together, might ‘make’ statements” contained in a firm’s prospectus”
- **Majority misreads *Central Bank*.** *Central Bank* was about secondary liability, but *Janus* is about “individuals who allegedly themselves ‘make’ materially false statements, not about those who help others do so.”
- **New loophole?** “What is to happen when the guilty management writes a prospectus containing materially false statements and fools both the board and public into believing they are true?”

Janus: Implications

- Reduction in the number of defendants
 - Entities
 - Individuals
- Elimination of theories
 - Adoption
 - Conduit
 - Imprimatur
- Whose scienster?

2. October 2011 Case

Credit Suisse Securities v. Simmonds,
No. 10-1261
Limitations Period for Rule 16(b) Actions

Credit Suisse: Background

- **Claims:** Alleges that supposed arrangement whereby underwriters had arranged for post-IPO stock purchases of the issuers' securities at progressively higher prices ("laddering") constituted prohibited short-swing profits.
- **Key Allegations:**
 - Simmonds owns stock in 55 companies that conducted IPOs in 1999 or 2000
 - Filed 55 virtually identical actions under Section 16(b) of the Exchange Act
 - Alleged that petitioners – investment bank or banks that underwrote the IPO at issue in each action – "created the opportunity for themselves to directly and indirectly profit or share in any profits derived from transactions" in the IPO allocation and aftermarket
 - Claimed that petitioners qualified as "beneficial owners" of 10% or more of the issuers' stock (and hence were covered by Section 16(b)) by virtue of their relationships with the issuers' officers and directors and their own customers
 - Claimed petitioners had profited from short-swing transactions
 - Alleged that petitioners failed to report the short-swing transactions under Section 16(a), thus tolling the statute of limitations set forth in Section 16(b)

Credit Suisse: Background

- **History:** As relevant here, district court granted motion to dismiss as barred by two-year statute of limitations
- Ninth Circuit reversed, holding that the limitations period was tolled until the filing of reports under Section 16(a), regardless of whether the plaintiff knew or should have known of the conduct at issue
- **Issue:** Whether the two-year time limit for bringing an action under Section 16(b) of the Securities Exchange Act of 1934 is subject to tolling, and, if so, whether tolling continues even after the receipt of actual notice of the facts giving rise to the claim?

Credit Suisse: Pending

- **Cert granted June 27, 2011**
- **Petitioners' brief filed August 18, 2011:**
 - Primary argument: Section 16(b) establishes a two-year repose period that cannot be extended
 - Supported by amicus U.S. Chamber of Commerce
- **Solicitor General Filed Brief Supporting Neither Party**
 - Takes the position that Section 16(b)'s two-year period is equitably tolled until a reasonably diligent security holder knows or should know the facts underlying his claim
- **Respondent's brief due September 26, 2011**
- **Oral argument likely November or December 2011**

3. Themes

1. Scope Cases – Bright Lines

- *Central Bank* (1995)
- *Stoneridge* (2008)
- *Morrison* (2010)
- *Janus* (2011)

2. *Pleading Cases – Holistic & Factual*

- *Tellabs* (2007)
- *Merck* (2010)
- *Matrixx* (2011)

3. *No Creativity*

Courts Should Not Be Creative - For Either Side

Plaintiffs	Defendants
<i>Morrison</i> (2010)	<i>Merck</i> (2010)
<i>Janus</i> (2011)	<i>Halliburton</i> (2011)
<i>Stoneridge</i> (2008)	<i>Matrixx</i> (2011)

4. *Chipping Away*

What the Court Giveth, It Can Taketh Away

- *Morrison* (2010)
- *Stoneridge* (2008)
- *Janus* (2011)

4. Observations

Cases & Results

Case	Issue	Result
<i>Dura Pharms., Inc. v. Broudo</i> , 544 U.S. 336 (2005)	Loss Causation	9-0
<i>Erica P. John Fund, Inc. v. Halliburton Co.</i> , 131 S. Ct. 2179 (2011)	Class Certification	9-0
<i>Kircher v. Putnam Funds Trust</i> , 547 U.S. 633 (2006)	SLUSA Remand	9-0
<i>Matrixx Initiatives, Inc. v. Siracusano</i> , 131 S. Ct. 1309 (2011)	Materiality	9-0
<i>Merck & Co., Inc. v. Reynolds</i> , 130 S. Ct. 1784 (2010)	Statute of Limitations	9-0
<i>Tellabs, Inc. v. Makor Issues & Rights, Ltd.</i> , 551 U.S. 308 (2007)	Scienter Inference	8-1
<i>Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit</i> , 547 U.S. 71 (2006)	SLUSA Coverage	8-0
<i>Morrison v. National Australia Bank Ltd.</i> , 130 S. Ct. 2869 (2010)	Foreign Purchasers	8-0
<i>Credit Suisse Securities LLC v. Billing</i> , 551 U.S. 264 (2007)	IPO Laddering	7-1
<i>Janus Capital Group Inc. v. First Derivative Traders</i> , 131 S. Ct. 2296 (2011)	Primary Liability	5-4
<i>Stoneridge Inv. Partners, LLC v. Scientific-Atlanta</i> , 552 U.S. 148 (2008)	Primary Liability	5-3

Opinions By Justice

Justice	Majority Op.	Concurring Op.	Dissenting Op.
Stevens*	<i>Dabit</i> (2005)	<i>Morrison</i> (2010) <i>Merck</i> (2009) <i>Credit Suisse</i> (2007)	<i>Stoneridge</i> (2008) <i>Tellabs</i> (2007)
Breyer	<i>Merck</i> (2009) <i>Credit Suisse</i> (2007) <i>Dura</i> (2005)		<i>Janus</i> (2011)
Scalia	<i>Morrison</i>	<i>Merck</i> (2010) <i>Tellabs</i> (2007) <i>Kircher</i> (2006)	
Thomas	<i>Janus</i> (2011)		<i>Credit Suisse</i> (2007)
Alito		<i>Tellabs</i> (2007)	
Ginsburg	<i>Tellabs</i> (2007)		
Kennedy	<i>Stoneridge</i> (2008)		
Roberts	<i>Halliburton</i> (2011)		
Sotomayor	<i>Matrixx</i> (2011)		
Souter*	<i>Kircher</i> (2005)		
<i>*Former Justices</i>			

Winners & Losers

Plaintiffs' 4 Wins		Defendants' 7 Wins	
Case	Issue(s)	Case	Issue(s)
<i>Matrixx</i> (2011)	materiality; scienter	<i>Dura</i> (2005)	loss causation
<i>Halliburton</i> (2011)	class cert.	<i>Dabit</i> (2006)	SLUSA
<i>Merck</i> (2010)	statute of limitations	<i>Credit Suisse</i> (2006)	IPO laddering
<i>Kircher</i> (2006)	SLUSA appeal	<i>Tellabs</i> (2007)	strong inference
		<i>Stoneridge</i> (2008)	reliance/scheme
		<i>Morrison</i> (2010)	foreign purchaser
		<i>Janus</i> (2011)	Speaker

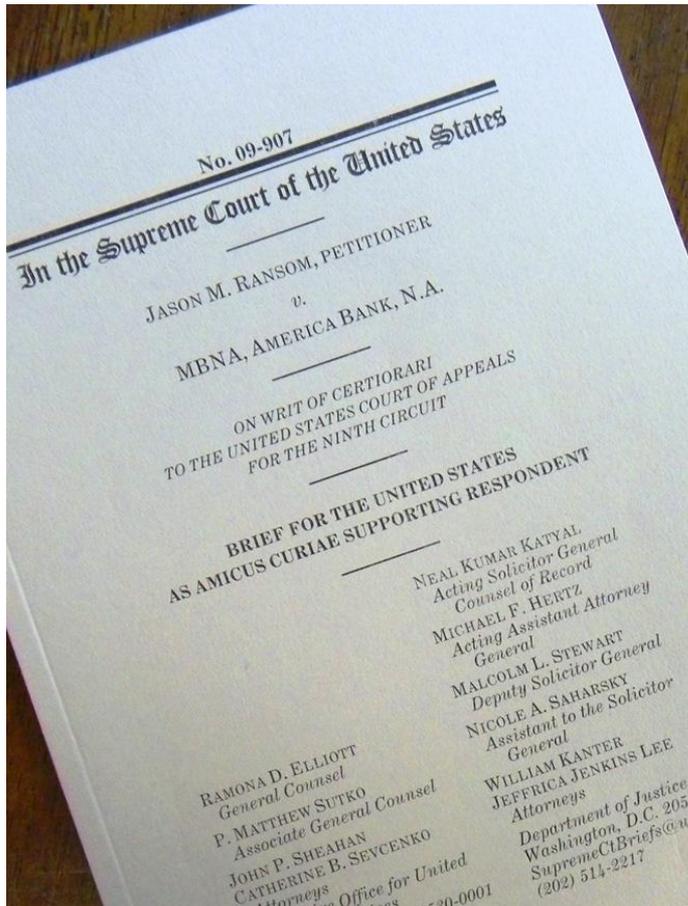
Types of Cases

Pleading/ Proof Cases		Scope Cases	
Case	Issue(s)	Case	Issue(s)
<i>Dura</i> (2005)	Loss Causation	<i>Dabit</i> (2006)	SLUSA
<i>Tellabs</i> (2007)	strong inference	<i>Credit Suisse</i> (2006)	IPO laddering
<i>Merck</i> (2010)	statute of limitations	<i>Stoneridge</i> (2008)	primary liability
<i>Matrixx</i> (2011)	materiality; scienter	<i>Morrison</i> (2010)	foreign purchaser
<i>Halliburton</i> (2011)	class cert.	<i>Janus</i> (2011)	primary liability

Circuit Scorecard

Circuit	Results	Affirmed	Reversed/ Vacated
Second	1-2	<i>Morrison (2010)</i>	<i>Credit Suisse (2007)</i> <i>Dabit (2006)</i>
Third	1-0	<i>Merck (2010)</i>	
Fourth	0-1		<i>Janus (2011)</i>
Fifth	1-0		<i>Halliburton (2011)</i>
Seventh	0-2		<i>Tellabs (2007)</i> <i>Kircher (2006)</i>
Eighth	1-0	<i>Stoneridge (2008)</i>	
Ninth	1-1 [1-3]	<i>Matrixx (2011)</i>	<i>Dura (2005)</i> [<i>Simpson (2008)</i>] [<i>Betz (2010)</i>]

Role of Solicitor General



- Call for Views of Solicitor General (CVSG)
- Determines Position of United States
- Participates in Approximately 2/3 of Merits Cases Each Term
- Behind the Scenes

Solicitor General Scorecard

Case	CVSG	Solicitor General Sides With		Result
		<i>Defendants</i>	<i>Plaintiffs</i>	
<i>Dabit</i> (2005)	X	●	X	Win
<i>Dura</i> (2005)	●	●	X	Win
<i>Kircher</i> (2005)	X	---	---	-
<i>Credit Suisse</i> (2006)	●	●	X	Win
<i>Tellabs</i> (2007)	X	●	X	Win
<i>Stoneridge</i> (2008)	X	●	X	Win
<i>Merck</i> (2010)	●	X	●	Win
<i>Morrison</i> (2010)	●	●	X	Win
<i>Halliburton</i> (2011)	●	X	●	Win
<i>Janus</i> (2011)	●	X	●	Lose
<i>Matrixx</i> (2011)	X	X	●	Win
Totals	6	6	4	9 Wins 1 Loss
			Bush	5-0
			Obama	4-1

Any Uptick?

- Roberts Court
- Circuit Splits Take Time
 - Reform Act in 1995
 - SLUSA in 1998
- Solicitor General Impact
- Going Forward

5. Q&A

About the Presenters



Jordan Eth is Co-Chair of the firm's Securities Litigation, Enforcement, and White-Collar Defense Group. He is a nationally recognized litigator, representing public companies and their officers and directors in securities class actions, SEC investigations, derivative suits, mergers and acquisitions litigation, and internal investigations. In 2008, Mr. Eth received a *California Lawyer* Attorney of the Year Award for co-leading the successful defense of JDS Uniphase Corp. and its former executives in a securities class action jury trial seeking \$20 billion in damages.



Deanne E. Maynard, Chair of the Appellate and Supreme Court Practice Group, is a partner in the Washington, D.C., office, and a former Assistant to the Solicitor General at the United States Department of Justice. She has argued 12 cases before the Supreme Court of the United States, and she has filed over 100 briefs in that Court. Notably, she worked on some of the most important business cases over the last several Terms, and was a principal author of the briefs for the United States in *Bell Atlantic Corp. v. Twombly*.

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