CA No. 09-56965

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

CONNECTICUT RETIREMENT PLANS AND TRUST FUNDS,

Plaintiff/Appellee,

v.

AMGEN INC., KEVIN W. SHARER, RICHARD D. NANULA, ROGER M. PERLMUTTER, and GEORGE W. MORROW,

Defendants/Appellants.

On Appeal from the United States District Court
for the Central District of California
No. 07-2536 PSG (PLAx)
(Honorable Philip S. Gutierrez)

BRIEF OF WASHINGTON LEGAL FOUNDATION AND ALLIED EDUCATIONAL FOUNDATION AS *AMICI CURIAE* IN SUPPORT OF APPELLANTS' PETITION FOR REHEARING *EN BANC*

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December 2, 2011

CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1, the Washington Legal Foundation and the Allied Educational Foundation state that they are non-profit corporations; neither entity has a parent corporation, and no publicly-held company has a 10% or greater ownership interest.

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INTERESTS OF *AMICI CURIAE*

The interests of *amici curiae* Washington Legal Foundation (WLF) and Allied Educational Foundation (AEF) are set out more fully in the accompanying motion for leave to file this brief.[1]

In brief, is a public interest law and policy center headquartered in Washington, D.C., with supporters in all 50 States. WLF devotes a substantial portion of its resources to defending free-enterprise, individual rights, and a limited and accountable government. WLF has appeared before this and other federal courts in numerous cases raising issues related to the proper scope of the federal securities laws. WLF previously filed an *amicus* brief in support of Defendants/Appellants when this case was before the three-judge panel.

AEF is a non-profit charitable and educational foundation based in Englewood, New Jersey. Founded in 1964, AEF is dedicated to promoting education in diverse areas of study, and has appeared as *amicus curiae* in this Court on a number of occasions.

INTRODUCTION AND STATEMENT OF THE CASE

In affirming class certification, the panel adopted a distinctly minority view

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[1] Pursuant to Fed.R.App.P. 29(c)(5), *amici* state that no counsel for a party authored this brief in whole or in part; and that no person or entity, other than *amici* and their counsel, contributed monetarily to the preparation and submission of this brief.

among the federal appeals courts regarding what must be shown to meet FRCP 23(b)(3)'s predominance requirement in a securities law class action. The panel held that certification is mandated under a fraud-on-the-market theory whenever the plaintiff demonstrates that the securities market was efficient and that the defendant's purported falsehoods were public. If those showings are made, it is immaterial how much evidence there is that the alleged falsehoods were not deemed material by the market; the class must be certified. The shortcomings of that rule are obvious: since the market for the common stock of virtually every large corporation is likely to be efficient, all but the most dull plaintiffs' lawyer will *always* be able to win class certification– all he/she need do is point to some public statement of the corporate defendant and allege that the statement was misleading and caused stock prices to be artificially inflated. And once the shareholder class is certified, public corporations face overwhelming pressures to settle even the most insubstantial claims. Moreover, the panel's determination that invocation of the fraud-on-the-market theory (with its presumption of reliance) is appropriate even when the alleged misrepresentations are shown not to have affected the market price is inconsistent with Supreme Court case law and the decisions of all but one of the federal appeals courts that have addressed the issue. Rehearing *en banc* is warranted to correct the panel's decision.

Appellee alleges that Appellants (collectively, "Amgen") violated federal securities laws by issuing misleading information (and omitting material information) regarding two of Amgen's biologics. Appellee alleges that Amgen's violations caused it to purchase Amgen stock at an inflated price, and it thereby suffered losses.

Appellee sought certification of a plaintiff class consisting of all those who purchased Amgen stock between April 22, 2004 (the date of Amgen's first alleged misrepresentation) and May 10, 2007 (the date on which the truth allegedly was fully disclosed). Appellee relied upon the fraud-on-the-market theory when seeking class certification. It argued that the court could presume that members of the proposed class relied on Amgen's misrepresentations – regardless whether they ever heard the misrepresentations – because the stock traded in an open and developed securities market, such that the price they paid for their stock would likely include a premium reflecting the market's awareness of and reliance on the misrepresentations.

The district court granted the certification motion in August 2009, finding that Appellee met the prerequisites of FRCP 23(a) and 23(b)(3). In particular, the court determined that Appellee met Rule 23(b)(3)'s "predominance" requirement because – based on the fraud-on-the-market theory – Appellee was entitled to a

presumption that all class members relied on Amgen's alleged misrepresentations. Class Certification Order at 11-17.

On November 8, 2011, a panel of this Court affirmed. Slip Op. 20101-20114. The panel held that the only elements of the fraud-on-the-market presumption are "whether the securities market was efficient and whether the defendant's purported falsehoods were public." *Id.* at 20110. The panel rejected arguments that the availability of the presumption was dependent on proving that the alleged misstatements were material, *i.e.*, that the market was actually misled by and relied on the misstatements. *Id.* at 20112. The panel reasoned that materiality is a "merits" question that can be determined on a class-wide basis and thus is inappropriate for consideration at the class certification. *Id.* at 20111-12. It further held that any effort by defendants to rebut materiality is premature at the class certification stage but instead may only be made at trial or in support of a summary judgment motion. *Id.* at 20114.

SUMMARY OF ARGUMENT

Rehearing *en banc* is warranted. As the panel acknowledged, its decision exacerbated a circuit split on an issue of extreme importance in securities fraud litigation. It recognized that its decision places the Ninth Circuit in conflict with decisions from the First, Second, Fifth Circuits. Moreover, as Amgen pointed out

in its petition, the panel misread the Third Circuit's recent decision on this issue and counted the Third Circuit as being in its camp, when in fact the Third Circuit expressly held that it agreed with the Second Circuit's approach and deems materiality relevant to the class certification issue. *In re: DVI, Inc. Securities Litigation*, 639 F.3d 623, 638 (3d Cir. 2011) ("[W]e agree with the Second Circuit that a defendant's successful rebuttal demonstrating that misleading material statements or corrective disclosures did not affect the market price of the security defeats the presumption of reliance for the entire class, thereby defeating the Rule 23(b) predominance requirement."). The panel's only ally is the Seventh Circuit.

The panel is correct that materiality is a merits issue; a shareholder class will lose at trial if the finder of fact determines that the alleged misstatements were not material and thus had no effect on market price. But as the Supreme Court has repeatedly held, if an issue is relevant to whether plaintiffs meet the Rule 23 class certification requirements, federal courts are not authorized to overlook the issue merely because examining the issue will entail some overlap with the merits of the plaintiffs' underlying claims. The Supreme Court has made clear that class certification pursuant to the fraud-on-the-market theory is inappropriate if "the market" did not actually rely on the alleged misstatements. The panel decision – by denying defendants any opportunity to oppose class certification by

demonstrating that the market did not rely on the misstatements because it did not deem them material – cannot be squared with Supreme Court precedent. An *en banc* rehearing is warranted to resolve that conflict.

ARGUMENT

I. BY DECLINING TO PROVIDE AMGEN AN OPPORTUNITY TO REBUT THE PRESUMPTION OF RELIANCE, THE PANEL PLACED THE NINTH CIRCUIT IN CONFLICT WITH FOUR FEDERAL APPEALS COURTS AND THE SUPREME COURT

A. Certification of a Class Is Improper Unless the Movant Demonstrates By a Preponderance of the Evidence That He Has Met All the Requirements of Rule 23, Including Predominance

Appellee assert the right to sue Amgen not only on its own behalf but also as a representative of the thousands of others who purchased Amgen stock during a three-year period beginning in April 2004. FRCP 23 imposes numerous requirements on those seeking to maintain such a representative action, including (under the circumstances of this case) a judicial finding "that the questions of law or fact common to class members predominate over any questions affecting only individual members." FRCP 23(b)(3). Certification of a class is appropriate only if "the trial court is satisfied, after a rigorous analysis, that the prerequisites of Rule 23(a) have been satisfied." *Wal-Mart Stores, Inc. v. Dukes*, 131 S. Ct. 2541, 2551 (2011) (quoting *General Tel. Co. Southwest v. Falcon,* 457 U.S. 147, 161 (1982)).

To prevail in a securities fraud action, a plaintiff must demonstrate, among other things, that he *relied* on the defendant's misrepresentation. *Dura Pharms. v. Broudo* , 544 U.S. 336, 341-42 (2005). Thus, to meet Rule 23(b)(3)'s predominance requirement, a plaintiff needs to demonstrate that reliance can be established on a class-wide basis, because if reliance can only be established on a plaintiff-by-plaintiff basis, questions of law or fact common to class members could never be deemed to "predominate" over questions affecting only individual members. *See Basic, Inc. v. Levinson*, 485 U.S. 224, 242 (1988). In sum, whether Appellee is entitled to a presumption of reliance is very much a Rule 23(b)(3) class certification issue, because Appellee cannot meet the "predominance" requirement (and thus is not entitled to certification) unless it is afforded that presumption.

B. That Reliance Is Also a Merits Issue Does Not Diminish the Importance of Examining That Issue Closely in Connection with Determining Whether Appellee Can Demonstrate Predominance

As noted above, reliance is also a "merits" issue: Appellee cannot prevail on its securities fraud claim unless it can establish that it purchased Amgen securities at an inflated price in reliance on Amgen's misrepresentations. The panel stated that whether the reliance effects of the misrepresentations "were large enough to be called material" is a "question[ ] on the merits." Slip op. at 20111 (quoting *Schleicher v. Wendt*, 618 F.3d 679, 685 (7th Cir. 2010)). The panel agreed with

the Seventh Circuit that also examining materiality at the class certification stage is inappropriate because materiality "affect[s] investors alike" and thus that class certification is appropriate "even though all statements turn out to have only trivial effects on stock price." *Id.*

The panel's determination that reliance/materiality's status as a merits issue precluded consideration of the issue at the certification stage conflicts with Supreme Court precedent. While the Court has cautioned against evaluating the merits of a plaintiff's claims as a basis for granting or denying class certification, it has stated unequivocally that a district court should not shy away from considering evidence that goes to the merits in determining whether the plaintiff has met each of the Rule 23 requirements. *Falcon*, 457 U.S. at 160 ("the class determination generally involves considerations that are enmeshed in the factual and legal issues comprising the plaintiff's cause of action"); *Wal-Mart*, 131 S. Ct. at 2551.

C. *Basic* and *Erica P. John Fund* Make Clear That Evidence Rebutting the Presumption of Reliance Is Not Premature at the Class Certification Stage

The Supreme Court's 1988 decision in *Basic* endorsed the "general validity" of the fraud-on-the-market theory and held that, under appropriate circumstances, the theory supports recognition of a presumption of reliance in securities fraud cases. 485 U.S. at 242. The Court described the theory as follows:

> The fraud on the market theory is based on the hypothesis that, in an open and developed market, the price of a company's stock is determined by the available information regarding the company and its business. . . Misleading statements will therefore defraud purchasers of stock even if the purchasers do not directly rely on the misstatements. . . The causal connection between the defendants' fraud and the plaintiffs' purchase of stock in such a case is no less significant than in a case of direct reliance on misrepresentations.

Id. at 241-42 (quoting *Peil v. Speiser*, 806 F.2d 1154, 1160-61 (3d Cir. 1986)).

The Court determined that: (1) "it is not inappropriate to apply a presumption of reliance supported by the fraud-on-the-market theory"; (2) that presumption is "rebuttable"; and (3) the district court's initial certification of the class "was appropriate when made but is subject on remand to such adjustment, if any, as developing circumstances demand." *Id.* at 250. Although the Court upheld the trial court's class certification decision, nothing in the Court's summation of its holdings suggested that a defendant's efforts to rebut the presumption of reliance are premature at the class certification stage.

Indeed, numerous passages in the decision point in the opposite direction. For example, *Basic* on several occasions (and in connection with its ruling that the presumption of reliance was rebuttable) emphasized that a class certification order is subject to revision at all times prior to final judgment. *See, e.g.*, *id.*. at 250 (class certification is subject on remand to adjustments "as developing circumstances demand"). Those passages indicate that the Court contemplated that

defendants should *not* be required to wait for trial before attempting to rebut the presumption of reliance.

In particular, Amgen's truth-on-the-market defense is an appropriate basis for rebutting the presumption of reliance and thereby defeating class certification. While conceding that a truth-on-the-market defense negates a stock fraud claim by demonstrating that the market was fully aware of Amgen's financial condition and thus that market price was unaffected by any misrepresen-tation, the panel concluded that such evidence is merely "a method of refuting an alleged misrepresentation's materiality" and may not be introduced to defeat class certification. Slip Op. at 20114. But properly understood, the truth-on-the-market theory is both a defense on the merits *and* an appropriate basis for rebutting the presumption of reliance (and thus relevant in determining whether the Rule 23 requirements have been met). The theory postulates that a misrepresentation cannot have a fraudulent effect on a stock's value after information contrary to the misrepresentation becomes known to an efficient market. It posits that the market will not rely on a defendant's allegedly misleading information if the "truth" is widely disseminated during the class period and is thus known to the market. *See, e.g., Ganino v. Citizens Utility Co.*, 228 F.3d 154, 167 (2d Cir. 2000).

Indeed, *Basic* listed truth-on-the-market as one of the theories a securities

law defendant may employ to rebut the presumption of reliance in a fraud-on-the-market case:

> Any showing that severs the link between the alleged misrepresentation and either the price received (or paid) by the plaintiff, or his decision to trade at a fair market price, will be sufficient to rebut the presumption of reliance. For example, if petitioners could show that the "market makers" were privy to the truth about [the alleged misrepresentations] and thus that the market price would not have been affected by their misrepresentations, the causal connection could be broken: the basis for finding that the fraud had been transmitted through market price would be gone.

Basic, 485 U.S. at 248.

It would have made little sense for the Court to discuss truth-on-the-market in connection with efforts "to rebut the presumption of reliance" if it really contemplated (as the panel held) that any such rebuttal must be delayed until trial. If a securities law defendant must await trial for a rebuttal opportunity, any trial victory would be of limited value – because a holding that rejects the presumption of reliance would result in decertification of the class for failure to meet Rule 23(b)(3)'s predominance requirement, not in a class-wide victory on the merits.

In concluding that materiality is not proper considered at class certification proceedings, the panel relied in substantial part on its conclusion that a "no materiality" finding would defeat the claims of *every* shareholder. Slip Op at 20111. That conclusion is demonstrably mistaken. Even if the market as a whole

did not rely on the alleged misrepresentations, it is entirely conceivable that individual shareholders did so; for example, they might have been unwilling to purchase shares at the market but for their belief in the truth of misrepresentations. If such shareholders can establish loss, there is no reason why they should not be permitted to proceed with their securities fraud claims on an individual basis. Indeed, in its most recent decision regarding fraud-on-the-market claims, the Court explicitly contemplated the propriety of such individual suits:

> Reliance by the plaintiff upon the defendant's deceptive acts is an essential element of the § 10(b) cause of action. . . . The traditional (and most direct) way a plaintiff can demonstrate reliance is by showing that he was aware of a company's statement and engaged in a relevant transaction, *e.g.*, purchasing common stock – based on that specific representation. In that situation, the plaintiff plainly would have relied on the company's deceptive conduct.

Erica P. John Fund, Inc. v. Halliburton Co., 131 S. Ct. 2179, 2184-85 (2011).

It would be unfair to shareholders who actually relied on the alleged misrepresentation to force them to be bound by a fraud-on-the-market class action, if there is serious doubt that "the market" also relied on the misrepresen-tation. By allowing rebuttal evidence regarding materiality to be introduced at the class certification stage, courts can protect individual shareholders who might otherwise have their rights cut off if a class were certified in a fraud-on-the-market case in which "the market" did not deem the misrepresentations to be material (and which

is thus headed to eventual defeat).

The panel cited *Erica P. John Fund* in support of its contention that a plaintiff need make only two showings (an efficient market and public misrepresentations) to be entitled to class certification. Slip Op. at 20113. The panel has mis-cited that decision, which actually cuts in favor of Amgen's position. The Court stated that securities fraud plaintiffs must make *at least three showings* in order to obtain class certification:

> It is undisputed that securities fraud plaintiffs must prove certain things in order to invoke *Basic*'s rebuttable presumption. It is common ground, for example, that plaintiffs must demonstrate that the alleged misrepresentations were publicly known (else how would the market take them into account?), that the stock traded in an efficient market, and that the relevant transaction took place "between the time the misrepresentations were made and the time the truth was revealed."

Erica P. John Fund, 131 S. Ct. at 2185 (quoting *Basic*, 485 U.S. at 248 n.27).[2] Accordingly, the case establishes that a key factor in determining whether the plaintiff is entitled to a presumption of reliance is "the time the truth was

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[2] Footnote 27 of *Basic* sets forth the requirements that a plaintiff must meet in order to invoke the presumption of reliance and does so in a manner that is highly favorable to defendants opposing class certification. In an effort to explain away Footnote 27, the panel argued that the *Basic* footnote was merely reciting the appeals court's list of requirements. Slip Op. at 20112. But by citing directly to Footnote 27 in support of the proposition that there are at least three well-established requirements that must be met to invoke the presumption of reliance, *Erica P. John Fund* undercuts the panel's contention that Footnote 27 sets forth the position of the appeals court, not that of the Supreme Court.

revealed." That is the precise issue on which Amgen has sought to be permitted to introduce rebuttal evidence; its consistent position has been that "the time that the truth was revealed" was on or before the dates on which it made its alleged misrepresentations. The panel's determination that Amgen was not permitted to introduce its rebuttal evidence at the class certification stage directly conflicts with *Erica P. John Fund*. Rehearing *en banc* is warranted to resolve that conflict, as well as the conflict between the panel's decision and decisions from the First, Second, Third, and Fifth Circuits – all four of which have held explicitly that a securities fraud defendant is entitled to contest class certification by introducing evidence that any misrepresentations were immaterial and did not affect the market price.

D. A Trial Court Cannot Accurately Determine the Starting and End Dates for the Class Period Without Considering All Rebuttal Evidence Regarding Truth on the Market

Truth-on-the-market rebuttal evidence is particularly relevant in determining appropriate starting and end dates for the class period. The trial court included within the certified class all those who purchased Amgen stock between April 2004 and May 2007. Amgen asserts that the "truth" regarding its two biologics had entered the market by April 2004 and continued to enter the market throughout the extraordinarily lengthy three-year class period certified in this case. By denying

Amgen an opportunity to submit its rebuttal evidence, both the panel and the district court deprived themselves of crucial evidence regarding the dates, if any, on which the misleading information was affecting share prices and the dates when the "truth" effectively counterbalanced the misleading information. *See, e.g.*, *In re Federal Nat. Mortg. Ass'n Securities, Derivatives, and "ERISA" Litigation*, 247 F.R.D. 32, 38 (D.D.C. 2008) ("whether the fraud-on-the-market presumption applies as a matter of law is essential for determining the duration of the class period").

The panel held that the only evidence relevant to the class certification issue is whether the market for the stock was efficient and whether the alleged misrepresentations were public. But unless a trial court agrees to hear all evidence regarding when and if the "truth" reached the market, it cannot possibly make an informed decisions regarding when the class period ought to begin and end. For example, if Amgen's excluded evidence would have shown that truth-on-the-market had eliminated the misrepresentation's effects on market price by May 2004, there can be no justification for certifying a class that runs until May 2007 simply because the plaintiff has *alleged* (but has not been asked to prove) that not until the latter date was the market fully aware of the truth. Similarly, if Amgen's evidence would have shown that the truth was revealed by April 2004 (*i.e.*, the

same date on which Appellee alleges that the misrepresentations were first made), then there can be no justification for establishing any class period – that is, class certification should be denied. By mandating exclusion of all rebuttal evidence regarding when the truth entered the market, the panel decision deprives district courts of all meaningful guidance for determining an appropriate class period. *En banc* review is warranted in order to supply that guidance.

II. BECAUSE CLASS CERTIFICATION DECISIONS ARE OFTEN OUTCOME-DETERMINATIVE, IT IS PARTICULARLY IMPORTANT FOR THIS COURT TO ENFORCE STRICT ADHERENCE TO THE REQUIREMENTS OF RULE 23

Empirical research demonstrates the crucial role that class certification decisions play in the outcome of high-stakes class action lawsuits. Litigation costs make it very difficult for the party that loses the class certification decision to continue with the litigation – with the result that erroneous certification decisions are often effectively unreviewable. In light of that concern, *amici* respectfully urge the Court to grant rehearing *en banc* for the purpose of adopting clear rules that will encourage district judges to grant class certification motions only after they have determined that all the requirements of Rule 23 have been satisfied.

As numerous courts have recognized, companies that face a large certified class and hence enormous potential damages are "under intense pressure to settle"

In re Rhone-Poulenc Rorer, Inc., 51 F.3d 1293, 1298 (7th Cir.) (Posner, C.J.), *cert. denied*, 516 U.S. 867 (1995). If they do not want to "roll the dice," they settle, such that "the class certification – the ruling that will have forced them to settle – will never be reviewed." *Id.* Such settlements can in many instances legitimately be deemed "blackmail settlements." H. Friendly, *Federal Jurisdiction: A General View* 120 (1973).

Securities fraud class action litigation presents particular problems for defendants because they are especially prone to asymmetrical discovery costs: though they possess few relevant documents subject to discovery, plaintiffs can routinely demand that millions of pages of documents be produced by the defendants. J. Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497, 548-49, 571 (Feb. 1991). Moreover, because securities fraud cases often require the attention and participation of senior corporate executives, defendants in such actions can face costly and debilitating disruptions of their business activities. R. Bone & D. Evans, *Class Certification and the Substantive Merits*, 51 DUKE L.J. 1251, 1299 (Feb. 2002). Driven largely by litigation costs, "the vast majority of certified class actions settle, most soon after certification." *Id.* at 1291.

The tendency of securities fraud class actions to settle without any relation

to the underlying merits of the suits undermines the aim of the federal securities laws: to deter securities fraud or manipulation. But economists doubt that those laws can achieve their purpose given the consensus view that there is little correlation between being named in a securities fraud lawsuit and the incidence of fraud. *See, e.g.*, M. Johnson, *et al.*, In re Silicon Graphics Inc.: *Shareholders Wealth Effects Resulting from the Interpretation of the Private Securities Litigation Reform Act's Pleading Standard*, 73 S. CAL. L. REV. 773, 782 (May 2000).

Amici request that the Court grant rehearing *en banc* to emphasize the importance of strict adherence to the requirements of Rule 23, particularly Rule 23(b)(3)'s predominance requirement. Unless plaintiffs are denied class certification whenever the proffered evidence indicates that they are not entitled to a presumption of reliance, "blackmail settlements" of certified class actions will continue unabated.

CONCLUSION

Amici respectfully request that the Court grant the petition for rehearing *en banc*.

Respectfully submitted,

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Dated: December 2, 2011

CERTIFICATE OF COMPLIANCE

I am an attorney for *amicus curiae* Washington Legal Foundation. Pursuant to Fed.R.App.P. 32(a)(7)(C) and Ninth Circuit Rule 32-1, I hereby certify that the foregoing brief of *amicus curiae* is in 14-point, proportionately spaced Times New Roman type. According to the word processing system used to prepare this brief (WordPerfect X5), the word count of the brief is 4,158, not including the corporate disclosure statement, table of contents, table of authorities, certificate of service, and this certificate of compliance.

/s/ Richard A. Samp
Richard A. Samp

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 2nd day of December, 2010, I electronically filed the brief of *amicus curiae* Washington Legal Foundation with the Clerk of the Court for the U.S. Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

/s/ Richard A. Samp
Richard A. Samp