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Securities Law Alert

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Supreme Court: Grants Certiorari to Consider Whether the *American Pipe* Tolling Doctrine Permits an Unnamed Class Member to File a New Class Action After the Expiration of the Applicable Limitations Period

On December 8, 2017, the Supreme Court granted certiorari to decide whether the tolling rule established in *American Pipe & Construction Co. v. Utah*, 414 U.S. 538 (1974) allows an unnamed class member to file a new class action after the applicable limitations period has expired. *China Agritech v. Resh*, No. 17-432. The *American Pipe* Court held that "the commencement of a class action suspends the applicable statute of limitations as to all asserted members of the class who would have been parties had the suit been permitted to continue as a class action." The Supreme Court subsequently held, in *Crown, Cork & Seal Co. v. Parker*, 462 U.S. 345 (1983), that the *American Pipe* tolling doctrine applies not only to intervenors but also to class members who file individual actions.

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In *Resh v. China Agritech*, 857 F.3d 994 (9th Cir. 2017), the Ninth Circuit held that the *American Pipe* tolling doctrine permits plaintiffs to bring a new class action after the expiration of the statute of limitations if they were unnamed plaintiffs in a timely-filed putative class action, even if class certification was denied in the prior action on substantive grounds and the new action asserts similar class claims.

The Ninth Circuit found that "permitting future class action named plaintiffs, who were unnamed class members in previously uncertified classes, to avail themselves of *American Pipe* tolling would advance the policy objectives that led the Supreme Court to permit tolling in the first place." The Ninth Circuit reasoned that this "rule creates no unfair surprise to defendants because the pendency of a prior class suit has already alerted them 'not only [to] the substantive claims being brought against them, but also [to] the number and generic identities of the potential plaintiffs who may participate in the judgment.'" *Id.* (quoting *American Pipe*, 414 U.S. 538). As to the possibility that this rule might "lead to abusive filing of repetitive class actions," the Ninth Circuit stated that "ordinary principles of preclusion and comity will … reduce incentives to re-litigate frivolous or already dismissed class claims, and will provide a ready basis for successor federal district courts to deny class action certification."

The Ninth Circuit's decision is in line with the approach taken by the Sixth and Seventh Circuits.[1] However, in *Korwek v. Hunt*, 827 F.2d 874 (2d Cir. 1987), the Second Circuit expressly held that *American Pipe* "does not apply to permit a plaintiff to file a subsequent class action following a definitive determination of the inappropriateness of class certification." The First, Fifth, and Eleventh Circuits have held that *American Pipe* only tolls the *individual* claims of absent class members, and does not permit absent class members to bring a class action after the expiration of the statute of limitations.[2] The Third and Eighth Circuits have held that a class member may file a subsequent class action only if class certification was denied for reasons unrelated to the validity of the class itself.[3]

The Supreme Court granted defendant's petition for a writ of certiorari to review the Ninth Circuit's decision in *China Agritech* to address the question of whether *American Pipe* tolls the class claims of unnamed class members, in addition to their individual claims.

1. *Sawyer v. Atlas Heating & Sheet Metal Works*, 64 2 F.3d 560 (7th Cir. 2011) (holding that whether or not a class member can bring a subsequent class action does not depend on "the statute of limitations or the effects of tolling, but the preclusive effects of a judicial decision in the initial suit applying the criteria of Rule 23"); *Phipps v. Wal-Mart Stores*, 792 F.3d 637 (6th Cir. 2015) ("subsequent class actions timely filed under *American Pipe* are not barred").

2. *See Basch v. Ground Round*, 139 F.3d 6 (1st Cir. 1998) ("Plaintiffs may not stack one class action on top of another and continue to toll the statute of limitations indefinitely. … This simply cannot be what the *American Pipe* rule was intended to allow, and we decline to embrace such an extension of that rule."); *Salazar-Calderon v. Presidio Valley Farmers Ass'n*, 765 F.2d 1334 (5th Cir. 1985) ("Plaintiffs have no authority for their contention that putative class members may piggyback one class action onto another and thus toll the statute of limitations indefinitely, nor have we found any."); *Griffin v. Singletary*, 17 F.3d 356 (11th Cir. 1994) ("the pendency of a previously filed class action does *not* toll the limitations period for additional class actions by putative members of the original asserted class").

3. *Yang v. Odom*, 392 F.3d 97 (3d Cir. 2004) ("where class certification has been denied solely on the basis of the lead plaintiffs' deficiencies as class representatives, and not because of the suitability of the claims for class treatment, *American Pipe* tolling applies to subsequent class actions"); *Great Plains Trust Co. v. Union Pac. R.R. Co.*, 492 F.3d 986 (8th Cir. 2007) (following *Yang* and explaining that "[w]hether the *American Pipe* rule applies to subsequent class actions … depends on the reasons for the denial of certification of the predecessor action").

Supreme Court: Hears Oral Arguments on (1) Whether State Courts Have Jurisdiction Over Class Actions Alleging Only '33 Act Claims; and (2) Who Qualifies as a "Whistleblower" Under the Dodd-Frank Act's Anti-Retaliation Provisions

On November 28, 2017, the Supreme Court heard oral arguments in two significant securities law cases: *Cyan v. Beaver County Employees Retirement Fund*, No. 15-1439, in which the Court will decide whether a class action alleging only violations of the Securities Act of 1933 ("the '33 Act") may be brought in state court; and *Digital Realty Trust v. Somers*, No. 16-1276, in which the Court will determine whether the Dodd-Frank Wall Street Reform and Consumer Protection Act's ("Dodd-Frank Act") anti-retaliation protections apply to an employee who makes internal disclosures of allegedly wrongful activity, but does not report the activity to the SEC.

Justices Question Whether SLUSA Divested State Courts of Jurisdiction Over Class Actions Alleging Only '33 Act Claims

After the Private Securities Litigation Reform Act of 1995 ("PSLRA") imposed heightened pleading requirements for federal securities fraud class actions, plaintiffs began filing securities fraud class actions in state courts asserting violations of state law. Congress responded by enacting the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"), which provides that "[n]o covered class action based upon the statutory or common law of any state … may be maintained in any State or Federal court by any private party alleging" securities fraud. 15 U.S.C. § 77p(b). SLUSA further provides that "[a]ny covered class action brought in any State court involving a covered security, as set forth in subsection (b), shall be removable to Federal district court." 15 U.S.C. § 77p(c).

Prior to SLUSA's enactment, federal and state courts had concurrent jurisdiction over actions asserting '33 Act claims pursuant to 15 U.S.C. § 77v(a). SLUSA amended Section 77v(a) to add the italicized language: "The district courts of the United States … shall have jurisdiction … concurrent with State and Territorial courts, *except as provided in [S]ection 77p of this title with respect to covered class actions*." SLUSA also amended § 77v(a)'s removal bar as follows: "*Except as provided in [S]ection 77p(c) of this title*, no case arising under" the Securities Act of 1933 "shall be removed to any court of the United States."

At issue in *Cyan* is whether Congress intended to divest state courts of jurisdiction over all class actions brought under the '33 Act. Lower courts are deeply divided on the issue. Some fifty-five federal court decisions have taken divergent positions on whether state courts have subject matter jurisdiction over '33 Act claims in the aftermath of SLUSA. In general, federal district courts in California have held that state courts retain jurisdiction over '33 Act claims, while many courts outside of California have held that SLUSA eliminated state court jurisdiction over such actions.

The oral argument focused heavily on the proper reading of § 77v(a). Cyan argued that the text, structure, and purpose of SLUSA reveal Congress's intent to divest state courts of jurisdiction over class action cases alleging '33 Act claims. Under this reading, SLUSA should be read to provide exclusive jurisdiction to federal courts over '33 Act class actions, bringing it into line with the treatment of claims asserted under the Securities and Exchange Act of 1934 ("the '34 Act"). To Cyan, the natural reading of the statute demonstrates that Congress intended to amend the '33 Act in order to curtail the efforts to evade the dictates of the PSLRA. Cyan also argued that SLUSA's legislative history reflected Congress's intent to make federal court the "exclusive" and "only" venue for hearing federal securities class actions.

The United States, participating as amicus curiae, argued for a more limited reading than Cyan, but one that would nonetheless allow state court suits asserting exclusively '33 Act claims to be removed to federal court. According to the Solicitor General, nothing in SLUSA prevents state courts from maintaining concurrent jurisdiction over covered class actions that only allege '33 Act claims. The Solicitor General argued, however, that § 77p(c) permits the removal of "[a]ny covered class action brought in any State court involving a covered security, as set forth in subsection(b)." Therefore, the government took the position that though state courts retain concurrent jurisdiction to hear covered class actions that allege only violations of the '33 Act, such cases may nevertheless be removed to federal court if the defendant so chooses.

Respondent investors argued that SLUSA was intended to prohibit the filing of certain securities class actions under state securities laws, not to prohibit the litigation of '33 Act claims in state court. Respondent further argued that the provisions of SLUSA limiting state court jurisdiction and allowing removal apply only to cases asserting both state law claims and '33 Act claims, not to those asserting exclusively '33 Act claims. In other words, Respondent argued that SLUSA was written to root out the most abusive practices of securities class actions, not to prevent state courts from hearing these cases at all. Respondent pointed out that Congress could have clearly and easily eliminated concurrent jurisdiction for '33 Act claims had it wished to do so. Because the language of SLUSA does not contain such clear language and instead is far more limited, Respondent argued, SLUSA clearly provided that state courts should retain concurrent jurisdiction for class actions brought exclusively under the '33 Act.

The one conclusion that the Justices appeared to reach was that the relevant language in SLUSA was far from clear. Indeed, Justices described Congress's language as "obtuse" and "gibberish."

Other than agreeing that SLUSA's language was unclear, the Court appeared to offer divergent views on how to construe the language in question. Within the first several minutes of Cyan's argument, Justice Sotomayor questioned whether SLUSA's purpose was to divest state courts of jurisdiction over all '33 Act claims, as opposed to only removing its jurisdiction over claims asserting both '33 Act and state law claims. Justice Sotomayor also appeared to reject the contention that it was necessary to keep all '33 Act claims in federal court in order to apply a uniform set of standards for those cases. Justices Kagan and Ginsberg appeared to agree with Justice Sotomayor's position.

By contrast, Justice Gorsuch pressed Respondent to explain why, if the language was so carefully drawn, Respondent's position would treat one of the "except" clauses in § 77v(a) as superfluous.

Justice Alito began his questioning by referring to the statute as "gibberish." However, he then appeared to take issue with the interpretations being proposed by all sides.

Finally, Justice Breyer appeared intrigued by the Solicitor General's position that Congress did not deprive state courts of concurrent jurisdiction over suits asserting only '33 Act claims, but provided for the removal of those claims to federal court.

Justices Consider Whether the SEC's Definition of "Whistleblower" Should Govern the Reach of the Dodd-Frank Act's Anti-Retaliation Provisions

Section 922 of Dodd-Frank, codified as Section 21F of the Securities Exchange Act of 1934, created new rewards and employment protections for individuals who report alleged violations of the securities laws. Section 21F(a) defines a whistleblower as "any individual who provides ... information relating to a violation of the securities laws to *the Commission*, in a manner established, by rule or regulation, by the Commission." 15 U.S.C. 78u-6(a)(6) (emphasis added). Section 21F's anti-retaliation provision goes on to prohibit employers from firing or penalizing employees who, among other things, "mak[e] disclosures that are required or protected under the Sarbanes-Oxley Act of 2002." In certain situations, Sarbanes-Oxley requires internal reporting before external reporting (e.g., auditors must inform management of any potentially illegal acts and may only bring their concerns to the SEC after this internal reporting has occurred). In 2011, the SEC promulgated a rule construing Section 21F, which interpreted the term "whistleblower" to include employees who make only internal disclosures of potentially wrongful activity.

The circuits are divided on whether an individual who reports alleged misconduct internally but does not report that misconduct to the SEC qualifies for the Dodd-Frank Act's anti-retaliation protections. *Compare Asadi v. G.E. Energy (USA),* 720 F.3d 620 (5th Cir. 2013) (holding that the Dodd-Frank Act's definition of "whistleblower" "expressly and unambiguously requires that an individual provide information to the SEC") *with Berman v. Neo@Ogilvy*, 801 F.3d 145 (2d Cir. 2015) (finding that the tension between the two relevant provisions of the Dodd-Frank Act "creates sufficient ambiguity" to require the court's deference to the definition of 'whistleblower' in the SEC's implementing regulations) *and Somers v. Digital Realty Trust*, 850 F.3d 1045 (9th Cir. 2017) (holding that the Dodd-Frank Act "necessarily bars retaliation against an employee of a public company who reports violations to the boss" but not to the SEC.)

Oral argument focused primarily on two issues. First, the Court considered whether to apply Dodd-Frank's definition to both the Act's rewards and anti-retaliation provisions, as opposed to just the Act's rewards provisions. Second, the Court evaluated the extent to which it ought to defer to the SEC's promulgated regulation if the statutory language is indeed determined to be ambiguous.

Which Definition of "Whistleblower" Applies?

Digital Realty contended that the statutory definition applied, "by its plain terms," to the entirety of Dodd-Frank's whistleblower provisions. This reading, counsel for the company claimed, is "entirely consistent" with Congress's intent to increase the incentives for reporting violations of securities laws to the SEC. Moreover, the legislative history supports this view, as an earlier version of the anti-retaliation provisions "reached all employees," but was revised to apply just to "whistleblowers." Digital Realty noted that the Sarbanes-Oxley regime offers protections to employees who only make internal disclosures of potentially wrongful activity, and that Congress did not intend to render these protections superfluous with the enactment of Dodd-Frank. Citing the "elephant-in-a-mousehole" doctrine, Digital Realty argued that Congress would not have intended to create an "all-purpose anti-retaliation" regime through the use of ancillary provisions.

The United States, participating as amicus curiae to defend the SEC's regulatory definition, disagreed with Digital Realty, asserting that the statutory definition applied to Dodd-Frank's rewards provisions, while the ordinary meaning of "whistleblower" applied to the retaliation provisions. Further, there is a "unity of interest" among employees, employers, and the SEC in protecting and strengthening internal reporting and compliance.

Counsel for Somers emphasized that Dodd-Frank must be read as being consistent with the entire securities law framework, which is designed to respond to the conduct of employers rather than the mechanism through which an employee discloses potentially wrongful conduct. Finally, Somers' counsel noted that Dodd-Frank was designed to strengthen, not contradict, the Sarbanes-Oxley regime, and that adopting Petitioner's reading of the statute would frustrate this purpose.

The Justices evaluated the circumstances under which the Court should or could depart from Dodd-Frank's definition of "whistleblower." Justice Sotomayor noted she was "not sure there's a natural reading [or ordinary meaning]" of the word "whistleblower." Justice Gorsuch exclaimed that he was "just stuck on the plain language" of the text, wondering "how much clearer could Congress have been?" Chief Justice Roberts noted that, even if Congress inadvertently created an anomalous situation, the Court could not move beyond a clearly defined term unless a failure to do so would "make[] a mess of the whole thing." Justice Breyer questioned if Dodd-Frank creates an anomaly at all, noting that internal whistleblowers still get Sarbanes-Oxley protections. Based on the questions posed, many of the Justices appeared wary of setting aside the Dodd-Frank definition based on the supposedly anomalous situations Somers and the government described.

How Much Deference Should the SEC's Opinion Receive?

The Justices also questioned the parties about why the SEC's promulgated rule defining "whistleblower" should be accorded *Chevron* deference. Justice Gorsuch, agreeing with Digital Realty, noted that when seeking public comment on its proposed rule, the SEC suggested it would be issuing a rule-making "with respect to whistleblowers who report to the Commission." However, the agency's final rule suggested, without any explanation, that reporting to the Commission would not be required for Dodd-Frank's anti-retaliation provisions to apply.

Counsel for Somers contended that the SEC "specifically asked for comments about whether to broaden or change the definition of whistleblower for the purposes of the anti-retaliation [provisions]." Respondent further noted that, in a public comment in response to the proposed rule, the Association of Corporate Counsel noted their assumption that Dodd-Frank would also cover internal whistleblowers. The government added that under the "logical outgrowth test" adopted by the Supreme Court, an agency "proposing 'X' and getting 'not-X' is enough to satisfy" the requirements of the test.

However, some of the Justices seemed unconvinced by these arguments. Justice Breyer suggested that receiving notice that the SEC will be defining what counts as having provided information to the Commission "does not put people on notice that [the SEC is] … going to apply [the definition] to people who don't provide information to the Commission," adding "I mean, that's English, I would think." After the government's logical outgrowth assertion, Justice Sotomayor asked, "Bottom line…how much are you relying on just *Chevron* deference here?" Given the skepticism the Justices expressed, it is unclear whether a majority of the Court believes that the SEC's definition of "whistleblower" should be accorded deference in this case.

Second Circuit: (1) *Affiliated Ute* Presumption of Reliance Does Not Apply If Plaintiffs' Claims Are "Primarily Based on Misstatements," and (2) Plaintiffs May Be Able to Establish Market Efficiency Without Direct Evidence of Price Impact

On November 6, 2017, the Second Circuit held that the presumption of reliance established in *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128 (1972) for omission-based Section 10(b) claims "does not apply" if plaintiffs' claims "are primarily based on misstatements." [*Waggoner v. Barclays*, 2017 WL 5077355 (2d Cir. 2017) (Droney, J.)](). The court further held that "direct evidence of price impact is not always necessary to demonstrate market efficiency." In addition, the Second Circuit ruled that "defendants seeking to rebut" the presumption of reliance established in *Basic v. Levinson*, 485 U.S. 224 (1988) "must do so by a preponderance of the evidence."

Affiliated Ute Presumption of Reliance Applies Only in Cases That Primarily Involve Omissions

The Second Circuit explained that *Affiliated Ute* "allows the element of reliance to be presumed in cases involving primarily omissions, rather than affirmative misstatements, because proving reliance in such cases is, in many situations, virtually impossible." The Second Circuit noted that it has twice found the *Affiliated Ute* presumption inapplicable where "the claims of fraud at issue were not based primarily on omissions."

In *Wilson v. Comtech Telecommunications Corp.*, 648 F.2d 88 (2d Cir. 1981), plaintiff alleged that sales and earnings projections "became misleading when subsequent corrective information was not timely disclosed." *Waggoner*, 2017 WL 5077355 (discussing *Wilson*, 648 F.2d 88). The court found the *Affiliated Ute* presumption inapplicable because "the omissions alone were not the actionable events and proving reliance on them was therefore not 'impossible.'" *Id.* (discussing *Wilson*, 648 F.2d 88). The *Wilson* court reasoned that in "many instances, an omission to state a material fact relates back to an earlier statement, and … the omission may also be termed a misrepresentation."

Similarly, in *Starr ex rel. Estate of Sampson v. Georgeson Shareholder*, 412 F.3d 103 (2d Cir. 2005), the court found the *Affiliated Ute* presumption did not apply to claims concerning defendants' alleged failure to correct misstatements. Plaintiffs contended that defendants' alleged omissions "exacerbated the misleading nature of the affirmative misstatements," but did not base their claims "primarily" on omissions.

Relying on its prior holdings in *Wilson* and *Starr*, the Second Circuit in *Waggoner* found the *Affiliated Ute* presumption inapplicable because plaintiffs alleged "numerous affirmative misstatements" and the claimed omissions were "directly related" to those misstatements. The Second Circuit underscored that "[t]he *Affiliated Ute* presumption does not apply to earlier misrepresentations made more misleading by subsequent omissions, or to what has been described as 'half-truths,' nor does it apply to misstatements whose only omission is the truth that the statement misrepresents."

Direct Evidence of Price Impact Is Not Always Required to Establish Market Efficiency at the Class Certification Stage

To demonstrate market efficiency, a prerequisite for the *Basic* presumption of reliance, plaintiffs' experts typically rely on some combination of the five factors set forth in *Cammer v. Bloom*, 711 F. Supp. 1264 (D.N.J. 1989) and the three factors enumerated in *Krogman v. Sterritt*, 202 F.R.D. 467 (N.D. Tex. 2001). Only one of these factors — *Cammer* 5 — is a direct measure of market efficiency.

The Second Circuit held that "direct evidence of price impact under *Cammer* 5 is not always necessary to establish market efficiency and invoke the *Basic* presumption." The court explained that "[t]he *Cammer* and *Krogman* factors are simply tools to help district courts analyze market efficiency in determining whether the *Basic* presumption of reliance applies in class certification decision-making." The court emphasized that these factors "are no more than tools," and stated that "certain factors will be more helpful than others in assessing particular securities and particular markets for efficiency."

The Second Circuit made it clear that its decision should not be read to "imply that direct evidence of price impact under *Cammer* 5 is never important." The court observed that "[d]irect evidence of an efficient market may be more critical, for example, in a situation in which the other four *Cammer* factors (and/or the *Krogman* factors) are less compelling in showing an efficient market." The court noted that in *Teamsters Local 445 Freight Division Pension Fund v. Bombardier*, 546 F.3d 196 (2d Cir. 2008), it placed great weight on *Cammer* 5 because "certain of the indirect factors did not demonstrate market efficiency." *Waggoner*, 2017 WL 5077355 (discussing *Bombardier*, 546 F.3d 196).

Here, however, the Second Circuit found the district court was not obligated to consider direct evidence of market efficiency under *Cammer* 5 because the remaining four *Cammer* factors and the *Krogman* factors "weighed so clearly in favor of concluding that the market … was efficient" that defendants had not even challenged the expert's analysis of those factors.

Defendants Seeking to Rebut the *Basic* Presumption Bear the Burden of Persuasion to Disprove Reliance

The Second Circuit also held the district court did not err "by shifting the burden of persuasion, rather than the burden of production, to rebut the *Basic* presumption."

The court explained that in *Halliburton Co. v. Erica P. John Fund*, 134 S. Ct. 2398 (2014) (*Halliburton II*), the Supreme Court stated that "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." The Second Circuit found "[t]his Supreme Court guidance indicates that defendants seeking to rebut the *Basic* presumption must demonstrate a lack of price impact by a preponderance of the evidence at the class certification stage."

The Second Circuit reasoned that "the phrase '[a]ny showing that severs the link' aligns more logically with imposing a burden of persuasion rather than a burden of production." The court found *Halliburton II* "requires defendants to do more than merely produce evidence that *might* result in a favorable outcome; they must demonstrate that the misrepresentations did not affect the stock's price by a preponderance of the evidence."[4]

In the case before it, the Second Circuit found the district court did not abuse its discretion in holding that defendants had not met their burden of persuasion. The Second Circuit explained that "the district court was well within its discretion in concluding that the lack of price movement on the dates of the alleged misrepresentations [did] not rebut the *Basic* presumption" because plaintiffs had "proceeded on a price maintenance theory." That theory "recognizes 'that statements that merely maintain inflation already extant in a company's stock price, but do not add to that inflation, nonetheless affect a company's stock price.'" *Id.* (quoting *In re Vivendi*, 838 F.3d 223 (2d Cir. 2016)).

The Second Circuit further held that defendants' burden was not met by demonstrating the existence of "a contributing factor to the decline" in the stock price. The court reasoned that "merely suggesting that another factor *also* contributed to an impact on a security's price does not establish that the fraudulent conduct complained of did not also impact the price of the security."

Fourth Circuit: Allegations Sufficient to Raise an Inference of the Speaker's Knowledge of a Statement's Falsity Do Not, Standing Alone, Satisfy the Scienter Pleading Requirement

On November 15, 2017, the Fourth Circuit held that allegations raising an inference of a CEO's knowledge of a statement's falsity were not "sufficient to show that [the CEO] acted intentionally or recklessly to deceive, manipulate, or defraud." *Maguire Financial v. PowerSecure Int'l*, No. 16-2163 (4th Cir. 2017) (Duncan, J.). The Fourth Circuit reasoned that "scienter and knowledge with respect to misrepresentation are distinct components of the requisite analytical framework." The court stated that "[t]o conflate the two … would read the scienter element out of the analysis in contravention of the … exacting pleading standard" established by the Private Securities Litigation Reform Act ("PSLRA").

At issue in the case before the Fourth Circuit was a CEO's alleged misrepresentation that the company had obtained a contract "renewal and expansion" when the company had instead secured a new contract that allegedly turned out to be less profitable than the original contract. The Fourth Circuit recognized that "[a] reasonable investor might well expect a seasoned executive like [the company's CEO] to know the difference between a contract renewal" and a new contract, "and intend to make the distinction." However, the court explained that "the reasonable investor's view of a factual statement" is relevant to the "material

4. The Second Circuit distinguished the Eighth Circuit's decision in *IBEW Local 98 Pension Fund v. Best Buy Co.*, 818 F.3d 775 (8th Cir. 2016). There, the Eighth Circuit found defendants had successfully rebutted the *Basic* presumption by presenting "overwhelming evidence" that the alleged misstatements had no impact on Best Buy's share price. The Second Circuit explained that it did not "read the Eighth Circuit's decision as being in direct conflict with [its] holding" because "the Eighth Circuit's ruling did not depend on the standard of proof." Please click here to read our prior discussion of the Eighth Circuit's decision.

misrepresentation inquiry," rather than the scienter inquiry.

The Fourth Circuit determined that it could not "infer" scienter from allegations suggesting that the CEO "knew his statement was false." The court found plaintiffs were attempting to "fuse[ ] an inference that [the CEO] knew enough to realize that his characterization was technically incorrect with an inference that he intended to deceive." The court stated that "stacking inference upon inference in this manner violates the [PSLRA's] mandate that the strong inference of scienter be supported by facts, not other inferences."

Here, the Fourth Circuit declined "to find intent to deceive investors" based on the CEO's onetime use of the "possibly ambiguous" word "renewal" to describe "an agreement that had historically accounted for approximately 4.1% of the company's annual revenue." The court reasoned that "[i]f [the CEO] wanted to deceive investors, [one] would expect that he would discuss the new contract at length, in greater detail, or multiple times, not that he would briefly and ambiguously characterize it as a 'renewal and expansion' once."

Ninth Circuit: Plaintiffs Cannot Plead Loss Causation Based Solely on the Disclosure of Customer Complaints of Possible Fraud

On November 21, 2017, the Ninth Circuit held that a government agency's disclosure of consumer complaints of possible fraud "did not form a sufficient basis for a viable loss causation theory." [*Curry v. Yelp*, 2017 WL 5583889 (9th Cir. 2017) (Gould, J.)].[5] The Ninth Circuit explained that "[a]lthough a securities fraud plaintiff need not allege an outright admission of fraud to survive a motion to dismiss, 'the mere 'risk' or 'potential' for fraud is insufficient to establish loss causation.'" *Id.* (quoting *Loos v. Immersion, Corp.*, 762 F.3d 880 (9th Cir. 2014)).[6]

The Ninth Circuit noted that it previously held in *Loos* "that the mere announcement of an investigation was insufficient to establish loss causation because it does not 'reveal' fraudulent practices to the market." *Id.* (quoting *Loos.*, 762 F.3d 880). Here, plaintiffs attempted to "rely on even less" because they cited only to the disclosure of customer complaints "without a subsequent investigation." The Ninth Circuit held that "the element of loss causation cannot be adequately made out merely by resting on a number of customer complaints and asserting that where there is smoke, there must be fire."

Northern District of Texas: Predominance Requirement for Class Certification Is Not Satisfied Where Putative Class Members Relied on "Varying" Representations

On November 7, 2017, the Northern District of Texas denied plaintiffs' motion for class certification in an action related to R. Allen Stanford's Ponzi scheme. [*Rotstain v. Trustmark National Bank*, No. 3:09-CV-2384-N (N.D. Tex. 2017) (Godbey, J.)].[7] The court found the Rule 23(b)(3) predominance requirement was not satisfied because the "investors had different financial advisors who made varying oral representations in separate sales pitches for the" Stanford International Bank Limited ("SIBL") certificates of deposit ("CDs") at issue. The court reasoned that even if it

5. The Ninth Circuit stated that in order "to prove loss causation, the plaintiff must demonstrate a causal connection between the deceptive acts that form the basis for the claim of securities fraud and the injury suffered by the plaintiff" (quoting *Ambassador Hotel Co. v. Wei-Chuan Inv.*, 189 F.3d 1017 (9th Cir. 1999)).

6. Please click here to read our prior discussion of the Ninth Circuit's decision in *Loos*.

7. Simpson Thacher represents The Toronto-Dominion Bank in this matter.

assumed that "every class member's claim is predicated on the sole, common omission that SIBL was a Ponzi scheme, this omission was made in a variety of differing contexts."

The Northern District of Texas found instructive the Fifth Circuit's decision in *Simon v. Merrill Lynch, Pierce, Fenner & Smith*, 482 F.2d 880 (5th Cir. 1973). There, the Fifth Circuit affirmed the district court's denial of class certification based on plaintiff's "failure to prove any standardized representations" by the defendant. The Fifth Circuit reasoned that "[i]f there is any material variation in the representations made or in the degrees of reliance thereupon, a fraud case may be unsuited for treatment as a class action." The Fifth Circuit also found it significant that plaintiff "premised his reliance on the oral touting" of a security rather than a written statement. The Fifth Circuit explained that "courts usually hold that an action based substantially, as here, on oral rather than written misrepresentations cannot be maintained as a class action."

The Northern District of Texas also relied on its prior decision in *Gyarmathy & Associates v. TIG Insurance Co.*, 2003 WL 21339279 (N.D. Tex. June 3, 2003) (Godbey, J.). There, the court found the predominance requirement was not satisfied where "potential class members received varying [oral] representations from their brokers" in addition to written materials that "may have been identical."

In the instant action, plaintiffs sought to represent a class consisting of more than 17,000 investors in SIBL CDs. "Given the varying oral representations made to" the thousands of putative class members, the Northern District of Texas concluded that plaintiffs "failed to carry their burden of showing that common issues of fact would predominate, as required by Rule 23(b)(3)."

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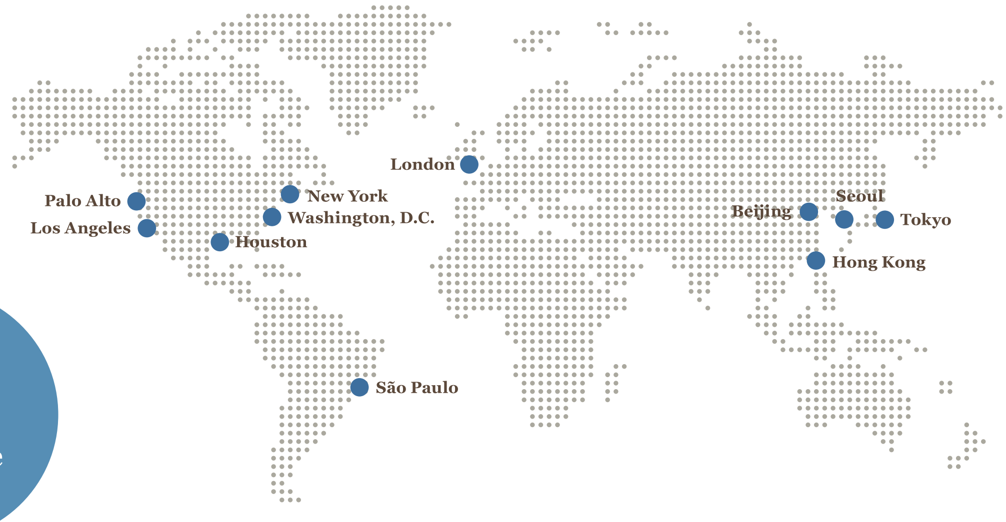

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