Class Is Back In Session:
Loss Causation and Class Certification After Halliburton

by Matthew D. Baker

Clarifying a circuit split, the Supreme Court in *Erica P. John Fund v. Halliburton,* No. 09-1403 (2011) held that securities fraud plaintiffs need not affirmatively prove loss causation in order to obtain class certification. Although the Court's unanimous decision represents a victory for plaintiffs, the Court declined to preclude defendants from using loss causation evidence to block class certification.

The petitioner, a Halliburton stockholder, alleged that various misrepresentations were made by Halliburton in order to inflate its stock price that subsequently dropped in the wake of corrective disclosures. The Court faced the question of whether the plaintiffs had demonstrated a sufficient basis for class certification. Specifically, plaintiffs seeking class certification must show that questions of law or fact common to class members predominate over any questions affecting only individual members." Fed. Rule Civ. Proc. 23(b)(3). In securities fraud claims predicated on § 10(b) of the Securities Exchange Act and Rule 10b-5, plaintiffs must prove, among other elements, reliance by the purchasers of the securities on the alleged misrepresentations. If the plaintiffs can only establish reliance by looking at individual investors on a case-by-case basis, class certification will fail under the balancing test of Fed. Rule Civ. Proc. 23(b)(3). Consequently, class certification frequently hinges on the plaintiffs' ability to establish a rebuttable presumption of reliance by all investors based on the "fraud-on-the-market" theory announced in *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988). The generally accepted requirements of the *Basic* presumption include: i) publically known misrepresentations, ii) efficient markets, and iii) a transaction that occurred between the misrepresentation and the revelation of the truth. However, the Fifth Circuit also required the demonstration of loss causation (*i.e.* that the misrepresentation that distorted the market price also caused the economic loss). The Court rejected this framework as not grounded in *Basic* or its logic. Although, loss causation is a necessary element of the potential claim, it is conceptually distinct from reliance. Consequently, the Court held that the plaintiffs were not required to demonstrate loss causation in order to trigger the *Basic* presumption.

The Court's decision was hardly surprising. In fact, even Halliburton abandoned the Fifth Circuit's position during oral arguments. Instead, Halliburton attempted to reinterpret the lower court's opinion to hold that a defendant could rebut the *Basic* presumption after it had been triggered and defeat class certification with loss causation evidence. Various circuit court cases including *In re Salomon Analyst Metromedia Litigation*, 544 F.3d 474, 483 (2d Cir. 2008) indicate that such price impact rebuttal evidence may defeat the *Basic* presumption. The Court refused to construe the Fifth Circuit's analysis in this light. In fact, the Court declared that, "we need not, and do not, address any other question about *Basic*, its presumption, or how and when it may be rebutted." Consequently, although plaintiffs must not prove loss causation to trigger the *Basic* presumption for purposes of class certification, the Court failed to preclude defendants from using loss causation or price impact evidence to rebut the *Basic* presumption and defeat class certification.