COMMENTARY

Supreme Court Rules Loss Causation Need Not Be Proven at Class Certification Stage

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Resolving a conflict among the Circuits, the Supreme Court held that securities fraud plaintiffs need not prove loss causation at the class certification stage. *Erica P. John Fund, Inc*. v. *Halliburton Co*., __ U.S. __ (June 6, 2011).

Plaintiffs in a securities fraud class action have the burden of proving both reliance upon an alleged material misrepresentation or omission and that the defendant's deceptive conduct caused their claimed economic loss. In *Basic* v. *Levinson,* 485 U.S. 224 (1988), the Supreme Court permitted plaintiffs to invoke a rebuttable presumption of reliance, and thus proceed with a class action absent proof of individual reliance, provided that the shares traded in an efficient market in which share prices reflect all publicly available information. In 2007, the Fifth Circuit held that this presumption would not be available unless plaintiffs also proved loss causation at the class certification stage. *Oscar Private Equity Investments* v. *Allegiance Telecom, Inc*., 487 F.3d 261 (5th Cir. 2007). Other Circuits, including the Second, Third and Seventh Circuits, did not require plaintiffs to prove loss causation at the class certification stage.

The Supreme Court reasoned in *Halliburton* that reliance and loss causation are separate requirements for a 10b-5 claim: Under *Basic*, an "investor presumptively relies on a defendant's misrepresentation if that 'information is reflected in [the] market price' of the stock at the time of the relevant transaction", whereas "[l]oss causation . . . requires a plaintiff to show that a misrepresentation that affected the integrity of the market price *also* caused a subsequent economic loss."

Because the Court of Appeals in *Halliburton* had rested its decision on loss causation, the Supreme Court felt constrained to vacate the decision. The Court, however, left open the possibil-

ity that a lower court could deny class certification on the ground that alleged misrepresentations did not affect the price of a company's stock in the first place. In such an event, the price would not "reflect the fraud," and thus arguably would not trigger the *Basic* presumption. The Supreme Court declined to address the question of which party would bear the burden of proof on the question of price impact or other questions "about *Basic*, its presumption, or how and when it may be rebutted."

In the wake of *Halliburton*, defendants may seek to terminate securities fraud class actions at the class certification stage by arguing that alleged misrepresentations had no effect on the market price, a question on which the allocation of the burden of proof may be important. Moreover, the Court's emphasis on the fact that loss causation is a separate requirement underscores that a failure to plead or prove loss causation may be fatal to a plaintiff's claim "even if the investor purchased the stock at a distorted price, and thereby presumptively relied on the misrepresentation reflected in that price."

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