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US SUPREME COURT REFUSES TO OVERTURN FRAUD-ON-THE-MARKET PRESUMPTION

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The United States Supreme Court, on the morning of Monday, June 23, 2014, issued its highly-anticipated decision in *Halliburton Co. v. Erica P. John Fund*, No. 13-317. Contrary to the hopes of many business interests, the Court did not overrule the "fraud-on-the-market" presumption established more than 25 years ago in *Basic v. Levinson*, 485 U.S. 224 (1988), which provides securities fraud plaintiffs with a rebuttable presumption that they relied on the purported misrepresentations made by the defendant. This presumption has allowed the certification of classes in the absence of proof of actual, individual reliance and is based on the premise that market efficiencies build all relevant information into a security's price.

But, in what is quickly being characterized as a blow to securities class actions, the Court also held that defendants may, at the early class certification stage, defeat *Basic's* fraud-on-the-market presumption by introducing direct evidence that the purported misrepresentations did not affect the company's stock price – that is, the misrepresentations had no actual "price impact." Challenging whether alleged misrepresentations had price impact at the class certification stage can defeat a class action far earlier than at the merits stage, after expensive discovery has been completed. Of course, the certification of a class, and the attendant risk created for defendants, often drives settlement of even weak claims.

The Decision

Chief Justice Roberts wrote the majority opinion on behalf of himself and five other Justices (Justices Kennedy, Ginsburg, Breyer, Sotomayor and Kagan). The Court first held that securities fraud plaintiffs may continue to rely on the fraud-on-the-market presumption, which relieves plaintiffs of the burden of proving actual reliance on the purported misrepresentations at issue where the securities in question trade on an efficient market. In so holding, the Court declined Halliburton's invitation to overrule *Basic* in its entirety. But the Court went on to hold that securities fraud defendants may attack the presumption at the class certification stage by showing that the specific misrepresentations at issue had no "price impact" on the security in question. Such evidence would be sufficient to rebut the fraud-on-the-market presumption, the Court wrote:

> Under *Basic's* fraud-on-the-market theory, market efficiency and the other prerequisites for invoking the presumption constitute an indirect way of showing price impact. As explained, it is appropriate to allow plaintiffs to rely on this indirect proxy for price impact, rather than requiring them to prove price impact directly, given *Basic's* rationales for recognizing a presumption of reliance . . . . While *Basic* allows plaintiffs to establish that precondition indirectly, it does not require courts to ignore a defendant's direct, more salient evidence showing that the alleged misrepresentation did not actually affect the stock price and, consequently, that the *Basic* presumption did not apply.

Conclusion

Halliburton is not the "death knell" for securities fraud lawsuits that some had expected. By refusing to overturn *Basic* and its fraud-on-the-market presumption, the Supreme Court has ensured that private securities fraud lawsuits will continue. But, by recognizing the ability to attack the presumption at the class certification stage (and thereby potentially defeat certification and avoid the exposure that attaches to defending against a class action), *Halliburton* should provide an important and useful tool for defending against and defeating securities fraud lawsuits.

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