Why The Halliburton Court Cared About Procedures

Law360, New York (March 11, 2014, 6:36 PM ET) -- By now, most of us have heard about argument in Halliburton v. Erica P. John Fund, No. 13 317, which took place before the U.S. Supreme Court last week. Of course, it is impossible to know how the court will rule when it issues its opinion later this year — likely in June. However, analysts generally have agreed upon two takeaways from the argument.

First, despite some recognition by the justices that the efficient market theory underlying Basic Inc. v. Levinson, 485 U.S. 224 (1988), is not perfect, there did not appear to be sufficient support for overruling Basic outright and doing away with a presumption of classwide reliance derived from the fraud-on-the-market theory.

Second, it appears that at least some of the justices are considering a middle ground that would leave Basic substantially intact but require something more at the class certification stage. In particular, numerous questions were asked of both parties and the United States regarding the "midway position" — as Justice Anthony Kennedy described it — articulated in an amicus brief submitted in support of Halliburton by two law professors. The professors' brief advocates replacing Basic's focus on market efficiency with an event study that would look for market distortion due to an alleged misrepresentation.

So, although many expected the argument to focus on the economic theory underlying Basic and traditional principles of stare decisis (a term that was mentioned just once during the argument), much of the discussion instead focused on the practical realities of securities litigation, including the procedures available to defendants to rebut Basic's presumption of reliance and the percentage of cases that make it to summary judgment and trial.

Below is a summary of some of the key points raised by counsel and the court, which strongly suggest that, if Basic's presumption of classwide reliance survives, something needs to be done to ensure that its equally strong mandate regarding the presumption's rebuttability is given effect.

Is the presumption of reliance rebuttable? Without a doubt. Basic plainly states (among other things): "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." 485 U.S. at 248. As Justice Ruth Bader Ginsburg recognized at argument: "[I]t's not a question of is it rebuttable .... It's a question of when." (03/05/2014 Hearing Tr. ("Tr.") at 9:11-13.)

Is the presumption rebutted in practice? Frequently not. As Halliburton's counsel explained, "[i]t's very unusual outside of the context of the Second Circuit, which allows rebuttal with respect to price impact." (Tr. at 8:22-24.) If a defendant is not entitled to rebut the presumption at the class certification stage, the upshot is that "it is virtually impossible" for a defendant to rebut the presumption following class

certification. (Tr. at 8:21-22.) Quoting an amicus brief, Halliburton's counsel elaborated: "Outside of [the Second Circuit] ... they're as rare as hen's teeth." (Tr. at 8:24-9:1.)

Why is this? Because, as Justice Antonin Scalia asked rhetorically, "[o]nce you get the class certified, the case is over, right?" (Tr. at 23:6-7.) In fact, as Halliburton's counsel noted, "only 7 percent" of securities fraud class actions make it to the summary judgment stage, "because once the case gets past class certification ... there is an in terrorem effect that requires defendants to settle even meritless claims." (Tr. at 51:5-9.) The rate is even lower with respect to trial: "less than one-third of 1 percent actually go to a verdict." (Tr. at 23:8-9.)

What percentage of class certification motions are granted? According to Halliburton's counsel, "[t]he most recent studies by NERA and Stanford show that 75 percent of class certification motions are granted in securities cases; and that number is much, much higher with respect to New York Stock Exchange companies that essentially have no way to dispute market efficiency." (Tr. at 50:17-22.)

When is class certification typically decided? The chief justice asked this question, and the fund's counsel correctly responded that "[g]enerally, you have summary judgment after class certification." (Tr. at 37:3-7.) In fact, class certification frequently is decided long before summary judgment — in some cases even before merits discovery has begun. This is consistent with the Federal Rule of Civil Procedure 23(c)(1)(A), which states that "[a]t an *early* practicable time after a person sues or is sued as a class representative, the court must determine by order whether to certify the action as a class action." (Emphasis added.)

Can a defendant move for summary judgment at an earlier point in the case? The fund's counsel asserted that "there's nothing that prevents a defendant from making a motion for summary judgment" at an earlier stage of the litigation; he also offered that "[y]ou could have summary judgment at the class certification stage." (Tr. at 37:9-15.)

While counsel's statements are technically correct, they ignore two procedural hurdles to obtaining summary judgment at an early stage. First, Federal Rule of Civil Procedure 56(d) allows a nonmoving party to seek denial or deferral of the motion for summary judgment "when facts are unavailable to" it.

So, if a defendant were to move for summary judgment at the class certification stage (which often happens before discovery has concluded), the plaintiff could (and likely would) argue that the motion is premature. The fund's counsel appeared to concede this very fact: "[B]ut the issue on the merits is that if you don't have discovery, you can't decide these issues obviously." (Tr. at 37:19-21.)

Second, litigants do not have an automatic right to file successive summary judgment motions, and, in most cases, it is within the district court's discretion whether to permit successive motions. See, e.g., Hoffman v. Tonnemacher, 593 F.3d 908, 911 (9th Cir. 2010) (holding that "district courts have discretion to entertain successive motions for summary judgment"); Local Civil Rule 56(C) (E.D. Va.) ("Unless permitted by leave of court, a party shall not file separate motions for summary judgment addressing separate grounds for summary judgment.").

Accordingly, if a defendant were to move for summary judgment in an effort to rebut the fraud-on-the-market presumption at the class certification stage, the defendant might be precluded from later filing a motion for summary judgment on other key elements of a securities fraud claim. For these reasons, absent judicial guidance sanctioning the use of summary judgment motions to rebut Basic's presumption, defendants may be reluctant to utilize this procedural tool.

To sum up:

1. A defendant has the right to rebut Basic's presumption of classwide reliance based on the fraud-on-the-market theory.

2. As a practical matter, if a class is certified, most cases settle, such that Basic's presumption is rarely, if ever, tested following class certification.

3. Basic's presumption could be tested through a summary judgment motion at the class certification stage, but the plaintiff likely would argue that any such motion is premature, and the defendant runs the risk (however remote) that it will be precluded from filing a successive summary judgment motion at a later stage of the case.

What does this mean? As a practical matter, if a defendant is not entitled to rebut the presumption at the class certification stage, Basic's directives regarding ways in which the presumption can be rebutted often remain untested.

Is there a solution? Kennedy correctly recognized that under the "Basic framework, at the merits stage there has to be something that looks very much like an event study" and aptly asked, "since you're going to have it anyway, why not have it at the class certification stage?" (Tr. at 18:8-11, 14-16.) The fund's counsel appeared to resist this approach, asserting that "the cost and expense at the class certification stage and the time delay would increase enormously, because now you would have to have these detailed event studies not just to prove efficiency of the market," but also "to show what the impact was of the particular allegedly culpable misrepresentation and disclosure." (Tr. at 37:21-38:4.)

The deputy solicitor general, however, appeared to have a different take. When asked for his views regarding adoption of the event study approach, he stated that "if anything, that would be a net gain to plaintiffs, because plaintiffs already have to prove price impact at the end of the day." (Tr. at 50:8-10.)

The procedures and percentages discussed during the Halliburton argument demonstrate that, if Basic survives, something should be done to ensure that defendants have a meaningful opportunity to rebut Basic's presumption of classwide reliance. This could be accomplished by requiring more of the plaintiff at the class certification stage or approving the defendant's use of an early summary judgment motion to test the presumption.

Although the law professors' event study approach would require a greater showing by the plaintiff at the class certification stage than is required in many courts today, practical questions remain about the approach — for instance, who would bear the burden of proof and whether a showing of market distortion could be rebutted at the class certification stage. The answers to these questions could go a long way to giving further meaning to Basic's clear directive that the presumption of reliance is rebuttable.

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