MAR 16 2009

No. 08-1021

In the
Supreme Court of the United States

GILEAD SCIENCES, INC., *et al.*,
Petitioners,

v.

TRENT ST. CLARE, *et al.*,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF THE CIVIL JUSTICE ASSOCIATION OF CALIFORNIA AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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INTEREST OF *AMICUS CURIAE*[1]

The Civil Justice Association of California ("CJAC" or "amicus")[2] is vitally interested in securing the Court's review of the important issue this case presents – *viz.*, whether a federal securities fraud complaint under Section 10(b) of the Securities Exchange Act must plead facts sufficiently specific to support a reasonable, non-speculative belief that the plaintiff can ultimately prove "loss causation".

CJAC is a more than thirty year old non-profit organization whose hundreds of members are businesses, professional associations and local government groups dedicated to educating the public about ways to make our civil liability laws more fair, efficient, uniform and economical. Our goal is not, to be sure, of purely academic interest or motive, but arises from the practical vicissitudes of legal and economic life too frequently visited upon our members, especially litigation over who gets how much, from whom, and under what circumstances when unlawful conduct is charged. Toward achievement of our purpose, CJAC regularly petitions co-equal and coordinate branches of the federal and California

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[1] Counsel of record for all parties consent to the filing of this amicus brief. All counsel received notice at least 10 days before the filing date of the intention to file said amicus brief.

No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person or entity other than amicus curiae, its members or its counsel made a monetary contribution to its preparation or submission.

[2] Formerly The Association for California Tort Reform ("ACTR").

governments to provide greater clarity and fairness to laws that intersect with and inform this objective.[3]

Amicus agrees with this Court's expressed concern in its recent reversal of another Ninth Circuit opinion that application of a "low" pleading threshold as to the "loss causation" element of a plaintiff's claim in a fraud class action like this one "tend[s] to transform a private securities action into a partial downside insurance policy." (*Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 347-48 (2005) ("*Dura*").) Despite the unfairness to defendants and the administration of justice of such a result, the Court in *Dura* nonetheless passed on addressing the issue of whether a higher pleading standard of specificity or particularity is required of future plaintiffs' loss causation pleadings because the plaintiffs there could not even meet the minimum threshold of "notice" pleading. Here, plaintiffs may have met the "bare-bones" pleading threshold but, as amicus contends and this case demonstrates, more should be required of them lest defendants continue to be deprived of a legitimate weapon to thwart securities fraud strike suits by plaintiffs and their counsel.

This case presents yet another opportunity for the Court to provide much needed certainty and clarity concerning the issue left unanswered by *Dura*: Does the Private Securities Litigation Reform Act of 1995

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[3] See, e.g., *Shell Oil Co. v. U.S.A.*, No. 07-1607; *Pacific Mut. Life Ins. Co. v. Haslip*, 499 U.S. 1 (1991); and *Browning-Ferris Industries of Vermont, Inc. v. Kelco Disposal, Inc.*, 492 U.S. 257 (1989).

(PSLRA)[4] require a more stringent pleading standard for "loss causation" than the low threshold found sufficient by the Ninth Circuit here – that the alleged facts "support a theory that is not facially implausible." (Petitioners' Appendix ("App.") 17a.) While the "plain language" of the PSLRA does not expressly answer this query, its statutory structure and intended purpose implicitly require that "loss causation" be pled with particularity just like scienter and misrepresentation. Guidance on this point now is precisely the type of gap-filling quasi-legislative roll the framers intended the Court provide.

BACKGROUND AND PROCEEDINGS BELOW

A. The Federal District Court's Decision Dismissing this Case

This case arises from dismissal by the federal district court of plaintiff investors' Fourth Amended class action complaint ("FAC") for "loss causation" resulting from alleged securities fraud by petitioner Gilead Sciences, Inc. The district court found that plaintiffs – persons who purchased or otherwise acquired Gilead stock between July 14, 2003 and October 28, 2003 (the "class period") – failed in their FAC allegations to satisfy the pleading requirements of the PSLRA and Federal Rules of Civil Procedure 12(b) and 9(b).

Specifically, allegations in the FAC focus on Gilead's announcements on July 14, and 31, 2003 of its financial results for the second quarter of 2003, and

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[4] Pub. L. No. 104-67, 109 Stat. 737.

the impact its premier product, Viread, had on those results. Viread is an antiretroviral drug used to treat HIV/AIDS, which Gilead introduced in 2001. In its announcements, Gilead gave an optimistic projection for its second quarter financial results, which it attributed to "strong sales growth" of Viread due to "broader prescribing patterns . . . as well as increases in U.S. wholesaler inventory . . .." (App. 22a.)

Gilead's July 31 announcement also contained warnings, reiterated in its Form 10-Q filed August 14, that its forward-looking statements were "subject to certain risks and uncertainties, which could cause actual results to differ materially." (*Id.* at 23a.) The Form 10-Q also disclosed a July 29, 2003 letter issued by the FDA, and made public by Gilead on August 7, warning Gilead about certain aspects of of its "off-label" promotional aspects for Viread. "Off-label marketing refers to the use for marketing purposes of information such as the result of clinical studies and other material on the uses of and the efficacy of an FDA-approved product that has not been approved by the FDA for inclusion in the product's package labeling." (*Id.* at 25a.)

When Gilead issued its July 31 press release, the company also held a conference call with analysts and investors, and through a corporate officer, explained that "a substantial inventory build occurred in the U.S. distributor channel during the second quarter as wholesalers anticipated the Viread price increase announced on June 27th. (*Id.*) "Based on U.S. inventory build up seen in the second quarter," the Gilead officer reported, "we anticipate Viread sales for the third quarter will be at or below the sales level recognized this second quarter;" and that "[w]e expect

these inventories to be drawn down to more normal levels during this quarter." (*Id.*)

Then on October 28, 2003, Gilead issued a press release announcing its financial results for the third quarter of 2003, which included net revenues of $194.1 million, and sales of Viread of $115.4 million. Gilead also stated that "after reviewing . . . prescription trends, . . . inventory data and actual Viread sales, [it] estimates there was approximately $33 to $37 million of inventory reduction by U.S. pharmaceutical wholesalers during the third quarter of 2003 following an equivalent inventory build during second quarter of 2003." (*Id.* at 24a.) The following day, Gilead's stock dropped $7.46 per share from $59.46 to close at $52. About one month later, Gilead's stock price recovered the entire drop experienced on October 29 and closed at $59.83 per share. (*Id.*)

According to the FAC, investors did not attribute much significance to the FDA letter warning Gilead about its off-label use of Viread. (*Id.* at 24a, 27a.) Plaintiffs claim that 75% to 95% of Viread sales were attributable to off-label promotion of Viread, and that this accounted for between $86.7 million and $109.82 million of Gilead's second quarter 2003 domestic sales. (*Id.*) Plaintiffs charge that Gilead maintained this misleading image of Viread long enough for the stock price to become inflated and for defendants to sell their shares before the FDA made their letter to Gilead public. (*Id.*)

The district court was unpersuaded that these allegations in the FAC sufficiently pleaded "loss causation," finding that they are simply "too attenuated." (*Id.* at 34a.) "The fundamental problem

with Plaintiffs' allegations is that they require the Court to make the unreasonable inference that a public revelation on August 8 caused a price drop three months later on October 28." (*Id* at 35a.) Moreover, "Plaintiffs' assertion that the FDA Warning Letter was the cause of the lower demand for Viread still does not establish a causal connection. Even if the FDA Warning Letter caused practitioners to reduce their Viread supply, Plaintiffs still fail to connect that with the drop in stock price." (*Id.*)

The district court concluded that "Plaintiffs have not adequately connected the disclosure of Gilead's off-label marketing and the drop in stock price in the FAC. Indeed, the evidence Plaintiffs have presented . . . only supports an inference that the market gave little or no weight to the FDA Warning Letter." (*Id.* at 39a, fn. 14.) Accordingly, the Court dismissed the FAC finding that "Plaintiffs have not adequately pled, under *Dura*, that the alleged misrepresentation proximately caused their loss." (*Id.*)

B. The Ninth Circuit's Opinion of Reversal

The appellate court reversed, stating the district court's "incredulity" was what animated its dismissal of the action rather than a facially inadequate complaint. If the district court could not make "the unreasonable inference that a public revelation on August 8 caused a price drop three months later on October 28," or found "a slowing increase in demand, alone, too speculative to . . . demonstrate loss causation," this was because the court was improperly acting as "a trier of fact." (*Id.* at 17a.) It is enough, the appellate court stated, that plaintiffs allege "facts to support a theory that is not facially implausible." (*Id.*)

In justifying its reversal, the appellate opinion states that "[a] limited temporal gap between the time a misrepresentation is publicly revealed and the subsequent decline in stock value does not render a plaintiff's theory of loss causation per se implausible." (*Id.* at 19a.) Moreover, though obviously the market did not react immediately to Gilead's corrective disclosure about the FDA Warning Letter, it did react to Gilead's October 28, 2003 release of "less-than-expected revenues," which arguably resulted "from the reduction in wholesalers' Viread inventories," which analysts ascribed to "lower-end user demand" that, "in turn," was allegedly "caused by the Warning Letter." (*Id.*)

The appellate opinion characterizes as "erroneous" the district court's conclusion "that a slowing increase in demand is too speculative to establish loss causation." (*Id.*) Why? Because "[h]ad the investors alleged that the Warning Letter eliminated all sales resulting from off-label marketing, it would be very unlikely that demand would continue to increase, since the complaint asserts that 75% to 95% of sales were caused by off-label marketing." No matter that plaintiffs did not allege that, "we see no reason why the court cannot proceed to the evidentiary stages to determine the extent of the Warning Letter's impact on the growth of demand for Viread." (*Id.* at 20a.)

SUMMARY OF ARGUMENT

The Ninth Circuit's opinion in this case that "loss causation" in a securities fraud action is satisfied at the pleading stage so long as the complaint provides enough information to show that the theory upon which it is based is "not facially implausible" is at odds

with other circuits and the PSLRA. The result is that, in the Ninth Circuit now, plaintiffs claiming "loss causation" need not provide any factual basis to show that their loss occurred after the alleged fraud became generally known to the market or, even if it did, that they are capable of isolating the fraud from other confounding and contributing factors.

This disparity between the lax "not per se implausible" pleading standard of the Ninth Circuit for "loss causation" and the more heightened pleading standards of numerous other circuits, creates the very "confusion worse confounded" situation that the PSLRA was enacted to avoid. Unless and until the Court acts to provide uniformity and clarity as to the proper pleading standard applicable to "loss causation" claims in securities fraud, plaintiffs will understandably forum shop to file in the least restrictive jurisdictions, increasing the volume of groundless lawsuits filed there and the attendant expense and discovery abuse which the PSLRA intended to prevent.

This case provides a unique opportunity for the Court to provide the clarity and uniformity necessary to correct the confusion in the circuits over what standard courts are to apply as gatekeepers in screening securities fraud lawsuits.

REASONS FOR GRANTING THE WRIT

I. THE NINTH CIRCUIT'S "NOT *PER SE* IMPLAUSIBLE" STANDARD OF PLEADING WHEN "LOSS CAUSATION" IS ALLEGED IN SECURITIES FRAUD COMPLAINTS CONFLICTS WITH OTHER CIRCUITS WHICH REQUIRE "PARTICULARITY" OR "HEIGHTENED PLEADING."

The opinion in this case exacerbates what has become a "most troublesome question"[5] over which the Circuits are divided – What is the proper pleading standard to apply in federal securities fraud actions based on "loss causation"? The answer to this query – whether a heightened or particularized standard, or a lax, bare-bones "notice" standard applies – is important because it determines whether courts can effectively function as "gatekeepers" to nip meritless securities actions before discovery costs burgeon out of control and discovery abuse occurs. (See, *e.g.*, *Bell Atlantic Corp. v. Twombly,* 550 U.S. 544, ___ (2007). Indeed, "[f]ew issues in civil procedure jurisprudence are more significant than pleading standards, which are the key that opens access to courts" and keeps them from being flooded with groundless litigation. (*Phillips v. County of Allegheny*, 515 F.3d 224, 230 (3d Cir. 2008).

In re Merck & Co. Sec. Litig., 432 F.3d 261, 268 (3d Cir. 2005), for instance, affirmed dismissal of a securities fraud class action against a corporation and its individual officers because the complaint did not

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[5] *Linkletter v. Walker*, 381 U.S. 618, 620 (1965).

satisfy the "heightened pleading" standard that Circuit holds applicable for securities fraud litigation. "To make out a securities fraud claim under section 10(b), a plaintiff must show that . . . 'the plaintiff's reliance on the defendant's misstatement caused him or her injury.'" (*Id. at 268,* quoting *Cal. Pub. Employees' Ret. Sys. v. Chubb Corp.*, 394 F.3d 126, 143 (3d Cir. 2004)). "These requirements are heightened by the PSLRA, which requires that the complaint 'state *with particularity* all facts on which [plaintiff's] belief is formed.'" (*Id.*; alteration in original, quoting 15 U.S.C. § 78u-4(b)(1) (2000).) (*Accord*: *GSC Partners CDO Fund v. Washington*, 368 F.3d 228, 236 (3d Cir. 2004).)

Similarly, *Plotkin v. IP Axess Inc.*, 407 F.3d 690, 696 (5th Cir. 2005), another securities fraud action, holds that to demonstrate a 10b-5 violation, a plaintiff must prove that the defendant proximately caused the plaintiff's injury. (407 F.3d at 696.) The PSLRA, according to the *Plotkin* opinion, "requires a securities fraud plaintiff . . . to plead these substantive [10(b)] elements with *particularity*. The PSLRA's particularity requirement incorporates, at a minimum, the pleading . . . under Federal Rule of Civil Procedure 9(b)." (*Id.*, emphasis added, citation omitted.)

Finally, as Petitioners show, the Second, Fourth and Eighth Circuits also demand "a heightened degree of factual specificity in pleading loss causation" in securities fraud claims (Petition ("Pet.") 18); and "a plethora of recent cases [in federal district courts] have applied heightened pleading standards to loss causation." (Brandon C. Helms, *Note: The Supreme Court's Dura Decision Unfortunately Secures a Brighter Future for 10b-5 Defendants*, 56 *DEPAUL L. REV.* 189, 218 (2006).) These five circuits, then,

squarely contradict the Ninth Circuit's holding in this case that all a plaintiff need plead to pass muster in a securities fraud action for "loss causation" is "facts to support a theory that is not facially implausible." (App. 17a.) Other Circuits may, to be sure, more closely align themselves with the Ninth in their tolerance toward what is required by way of a pleading standard for securities fraud; and plaintiffs will likely bring them to the Court's attention. The point here is not to count heads, however, but to recognize that a genuine conflict between the Circuits exists over this important issue, and these deep differences have drawn the attention of courts and commentators. "[N]otwithstanding efforts to constrain judicial decision-making through articulation of a seemingly-specific heightened pleading standard, interpretive variance by the courts has been marked." (Lonny S. Hoffman, *Burn up the Chaff with Unquenchable Fire: What Two Doctrinal Intersections Can Teach Us about Judicial Power over Pleadings*, 88 *B.U. L. REV.* 1217, 1260 (2008).)[6]

Given the Ninth Circuit's demonstrated willingness in this case to extrapolate to the stars, building inference upon speculative inference in an attempt to puff the FDA Warning Letter into a "plausible" *cause* for the October drop in Gileads' stock price, it is

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[6] See also Joseph A. Grundfest & A.C. Pritchard, *Statutes with Multiple Personality Disorders: The Value of Ambiguity in Statutory Design and Interpretation*, 54 *STAN. L. REV.* 627, 633-34 (2002). The authors examined thirty-three courts of appeals decisions and one hundred sixty-seven district court decisions and concluded that Congress' ability to draft the pleading standard ambiguously as a means of legislative compromise prevailed over the courts' abilities to interpret the pleading standard uniformly.

difficult to imagine a complaint that would not satisfy its lax pleading standard. When there is a gulf in pleading hurdles as great as that shown between the Ninth and at least five other circuits, however, the consequence to the administration of justice is dire. Absent a uniform pleading standard for securities fraud, jurisdictions with less restrictive standards will understandably attract, like iron filings to a magnet, a disproportionate share of securities fraud litigation. "Heightened pleading standards in securities fraud actions contribute to a 39.1% dismissal rate at this early litigation phase." (Elizabeth Chamblee Burch, *Securities Class Actions as Pragmatic ex Post Regulation*, 43 *GA. L. REV.* 63, 80 (2008).) Looser pleading standards make it easier to evade the court as "gatekeeper" and yield recovery for dubious claims. See Robert J. Giuffra Jr., *CEOs Beware: The Strike Suit Lives*, *WALL ST. J.*, Sept. 13, 1999, at A45 (noting that because of the circuit division, "the regulation of the securities markets will become a game of roulette, with the outcome turning on whether a securities class action is filed in New York or Silicon Valley.").

The Court's guidance is sorely needed to bring uniformity and certainty to the issue of what pleading standard applies in securities fraud claims for "loss causation." Only with that guidance, and only if it provides for a more particularized standard that permits the weeding out of groundless claims, can strike suits, forum shopping, needless discovery costs and discovery abuse be curtailed at the earliest and most economic opportunity.

II. THE PSLRA AND SOUND PUBLIC POLICY FAVOR A "PARTICULARIZED" OR "HEIGHTENED" PLEADING STANDARD IN SECURITIES FRAUD CLAIMS FOR "LOSS CAUSATION" INSTEAD OF THE "NOT PER SE IMPLAUSIBLE" STANDARD APPLIED IN THIS CASE.

When Congress passed the PSLRA it provided for heightened pleading requirements in federal securities fraud actions under Rule 10b-5. (*See* 15 U.S.C. § 78u-4(b)(1).) More specifically, sections 21D(b)(1) and (2) explicitly created heightened pleading requirements for the misrepresentation and scienter elements of a Rule 10b-5 claim. While the provision in the PSLRA that addressed "loss causation" did not expressly call for the application of a heightened pleading standard to plaintiffs' loss causation pleadings,[7] reading the PSLRA to add the loss causation element and then excluding it from the new pleading standard is illogical and counter to the legislation's purpose.

The Court has the opportunity in this case to hold that the PSLRA implicitly requires loss causation to be pled with particularity just like scienter and misrepresentation. Indeed, this is precisely the type of role the framers intended the Court to exercise.

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[7] *See* 15 U.S.C. § 78u-4(b)(4) (2000) (stating that "[i]n any private action arising under this chapter, the plaintiff shall have the burden of proving that the act or omission of the defendant alleged to violate this chapter *caused the loss for which the plaintiff seeks to recover damages*" (emphasis added)).

> It is now a commonplace that courts, not only of common law jurisdictions but also those which have codified statutory law as their base, participate in the lawmaking process. The commonplace, for which the Holmeses and the Cardozos had to blaze a trail in the judicial realm, assumes the rightness of courts in making interstitial law, filling gaps in the statutory and decisional rules, and at a snail-like pace giving some forward movement to the developing law.[8]

Indeed, the Court recently adjudicated in precisely this fashion when it defined more clearly what the 104th Congress meant by "strong inference" when it used that term as part of a more stringent pleading standard for scienter in the PSLRA. *See Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, ___ (2007). The Court can and should act similarly here in recognizing that the heightened pleading standards in the PSLRA were putatively modeled after the Second Circuit's standard, which required more than notice pleading for loss causation at the time the PSLRA was drafted. *See* S. REP. NO. 104-98, at 7 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 679, 686 (stating that the purpose of the original PSLRA bill was, "[to clarify] the *pleading requirements* for bringing securities fraud claims by adopting a standard modelled [sic] on that currently applied by the United

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[8] Norman J. Singer, *STATUTES AND STATUTORY CONSTRUCTION* § 5A:2 (6th ed. 2002).

States Court of Appeals for the Second Circuit, the leading circuit court in [the] area." (emphasis added).[9]

Respected jurists and legal scholars agree that the Court must, at the very least, look at the problem a piece of legislation purports to address and construe ambiguous language within that statute to further that purpose most effectively.

> [I]f the words used by the legislature are open to more than one [meaning] – as is often the case in disputes . . . that reach the courts – the court must look harder and longer and consider the legislative purpose behind the statute, the legislative history, and perhaps the canons of construction. Whether 'intent' or 'purpose' or some other similar measure serves as the benchmark, the traditional approach assumes a discoverable legislative design, and the court's

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[9] As Petitioners explain, "the Second Circuit has applied Rule 9(b) to loss causation in the RICO context, holding that a plaintiff 'must allege loss causation with *sufficient particularity* such that we can determine whether the factual basis for the claim, if proven, could support an inference of proximate cause.'" Pet. 18, emphasis added, citing *First Nationwide Bank v. Gelt Funding Corp.*, 27 F.3d 763, 770-72 (2d Cir. 1994). See also Devin F. Ryan, Comment, *Yet Another Bough on the "Judicial Oak": The Second Circuit Clarifies Inquiry Notice and Its Loss Causation Requirement under the PSLRA in Lentell v. Merrill Lynch & Co.*, 79 *ST. JOHN'S L. REV.* 485, note 34, at 489 (2005) (observing that the Second Circuit announced in *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161 (2d Cir. 2005), *cert. denied*, 546 U.S. 935 (2005) that loss causation must be plead to a higher standard than notice pleading, and that the standard to which it must be pled is similar to the one subsequently proscribed by Congress via the PSLRA for scienter and misrepresentation).

> cardinal obligation remains to identify and execute that design . . .. [T]he traditional approach to statutory interpretation, . . . focuses judicial attention on the dispositive 'legislative intent.' . . . [T]his conception gives judges clear marching orders. If the words of the statute unambiguously reflect legislative intent, the court should go no further.[10]

"[A]lthough the [PSLRA] was intended to provide a uniform pleading standard in securities class action litigation, courts have issued splintered opinions regarding the proper standards." (R. Tyler Hand, *Note: the Private Securities Litigation Reform Act of 1995: Heightened Pleading Standards in Class Action Litigation*, 26 *AM. J. TRIAL ADVOC.* 685, 690 (2003).) Ambiguity about the pleading standard required for "loss causation" by the PSLRA breeds uncertainty and, as the opinions from the Circuits show, conflict. This defeats the purpose of the legislation, leading to forum shopping amongst plaintiffs for jurisdictions with lax pleading standards and a more inviting climate for groundless strike-suits the PSLRA was enacted to curtail. This vexing situation calls for the Court to interpret and apply the PSLRA in the context of its clear purpose,[11] providing needed certainty, clarity and uniformity.

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[10] Jane S. Schecter, *Metademocracy: The Changing Structure of Legitimacy in Statutory Interpretation*, 108 *HARV. L. REV.* 593, 594-95 (1997).

[11] Interpretation . . . depends on reading the whole statutory text, *considering the purpose* and context of the statute, and consulting any precedents or authorities that inform the analysis. *Dolan v. Postal Service*, 546 U.S. 481, 486 (2006) (emphasis added).

CONCLUSION

For all the aforementioned reasons, the Court should grant the petition for review filed by Gilead and its top officers.

Respectfully submitted,

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