COMMENT

At a Loss with Loss Causation: Resolving the Ninth Circuit's Loss Causation Decisions in *Metzler Investment GMBH v. Corinthian Colleges* and *In re Gilead Sciences*

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INTRODUCTION

When a corporation caught defrauding investors revises its former disclosures to reflect accurate information, investors bear much of the fallout. Consider the following hypothetical: A publicly traded corporation gains commercial success by repeatedly violating federal marketing regulations.[1] The company's Chief Executive Officer willfully omits this information in the company's quarterly disclosures.[2] When news of the fraud leaks, the company revises its financial forecast to reflect lower expected earnings and the company's sales plummet, along with the value of investors' stocks.[3] Do investors have a remedy?[4] The answer may depend on whether the investors properly plead the elements of a Rule 10b-5 claim.[5]

Under the Securities Exchange Act of 1934, corporate officers can be liable for fraud in the sale or purchase of stock.[6] To survive Rule 12(b)(6) dismissal, the plaintiff must sufficiently plead all elements of the Rule 10-b action, including loss causation.[7] Loss causation

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[1] This hypothetical loosely tracks the facts of *In re Gilead Sciences Securities Litigation*, 536 F.3d 1049 (9th Cir. 2008).

[2] *See In re Gilead*, 536 F.3d at 1052-54.

[3] *See id.* at 1053-54 (noting that stock price dropped 12% from previous day's closing price after Gilead's true financial forecast predicted lowered earnings).

[4] *See* Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 730 (1975) (approving private Rule 10b-5 cause of action for securities fraud claims and recognizing that lower courts inferred private right to securities fraud claims); Kardon v. Nat'l Gypsum Co., 69 F. Supp. 512, 513 (E.D. Pa. 1946) (implying private cause of action for securities fraud under Securities Exchange Act of 1934); *see also* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 337 (2005) (recognizing private Rule 10b-5 claims); *In re* Daou Sys., Inc., 411 F.3d 1006, 1014 (9th Cir. 2005) (same).

[5] *See* Private Securities Litigation Reform Act of 1995 § 101(b), 15 U.S.C. § 78u-4 (2006) (standardizing pleading requirements for private Rule 10b-5 claims); *Dura*, 554 U.S. at 341, 346 (identifying private Rule 10b-5 elements and affirming Rule 12(b)(6) dismissal because plaintiff failed to properly plead loss causation); *In re Daou*, 411 F.3d at 1014 (affirming Rule12(b)(6) dismissal because plaintiff failed to plead loss causation); *In re* Vantive Corp., 283 F.3d 1079, 1083-84 (9th Cir. 2002) (same); Schlick v. Penn-Dixie Cement Corp., 507 F.2d 374, 380 (2d Cir. 1974) (same).

[6] Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j (2006); *see Dura*, 544 U.S. at 339-41; Randall v. Loftsgaarden, 478 U.S. 647, 647 (1986); *In re Gilead*, 536 F.3d at 1055; *In re Daou*, 411 F.3d at 1014.

[7] *See Dura*, 544 U.S. at 346-47 (affirming Rule 12(b)(6) dismissal because plaintiff failed to properly plead loss causation element under Rule 10b-5); Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1072 (9th Cir. 2008) (reviewing district court's Rule 12(b)(6) dismissal of plaintiff's complaint and requiring proper pleading of all Rule 10b-5 elements); *In re Gilead*, 536 F.3d at 1050 (same); Semerenko v. Cendant Corp., 223 F.3d 165, 169 (3d Cir. 2000) (same); *see also In re*

requires the plaintiff to establish that the defendant company's misrepresentation proximately caused the plaintiff's loss.[8] Thus, investors must allege that the depreciation of their investment did not result from adverse conditions affecting the market as a whole but from misleading information as to their specific security.[9] This task has become significantly more difficult for investors as the collapse of subprime mortgages created a ripple effect of economic misfortune affecting corporations nationwide.[10] Consequently, the pleading standards governing the element of loss causation has become the subject of fervent debate.[11]

Daou, 411 F.3d at 1014 (recognizing that plaintiff must sufficiently plead loss causation element under Rule 10b-5).

[8] 15 U.S.C. § 78u-4; *see Dura*, 544 U.S. at 344-47; Teachers' Ret. Sys. of La. v. Hunter, 477 F.3d 162, 188 (4th Cir. 2007); *In re Daou*, 411 F.3d at 1025 (requiring proof that defendant's material misrepresentation or omission caused plaintiff's harm). *See generally* 17 C.F.R. § 240.10b-5 (2006) (prohibiting fraud in connection with sale or purchase of stock).

[9] The depreciation of market conditions as a whole, among other things, can be considered an intervening factor that breaks the causal relationship between the fraud and economic loss. *See generally Dura*, 544 U.S. at 347 (observing that intervening factors break chain of proximate cause); *In re Gilead*, 536 F.3d at 1057 (same); Allen Ferrell & Atanu Saha, *The Loss Causation Requirement for Rule 10b-5 Causes-of-Action: The Implication of* Dura Pharmaceuticals v. Broudo, 63 BUS. LAW. 163, 166-67 (2007) (same).

[10] *See generally* Jennifer E. Bethel et al., *Legal and Economic Issues in Litigation Arising from the 2007-2008 Credit Crisis* (Harvard Law School, Discussion Paper No. 612, 2008), *available at* http://www.law.harvard.edu/news/spotlight/business-law/related/brookings_ferrell.pdf (discussing legal and economic repercussions of credit crisis); *Grappling with a Global Confidence Crisis*, KNOWLEDGE W.P. CAREY, Oct. 8, 2008, http://knowledge.wpcarey.asu.edu/article.cfm?articleid=1684 (commenting on long-term economic effects of financial crisis); Ronald D. Utt, *The Subprime Mortgage Market Collapse: A Primer on the Causes and Possible Solutions*, HERITAGE FOUND., Apr. 22, 2008, http://www.heritage.org/research/economy/bg2127.cfm (discussing causes and effects of subprime mortgage collapse on U.S. economy).

[11] *See generally* Elliot Cohen & Robert M. Carmen, *Loss Causation:* Dura Pharmaceuticals *and Its Aftermath*, LEXISNEXIS EXPERT COMMENTARY, 2008 Emerging Issues 2451 (June 2008) (presenting plaintiff approaches to defining corrective disclosure in reaction to *Dura*); Bruce Ericson et al., *Life After* Dura *— Courts Begin to Define Loss Causation in Securities Fraud Cases*, 1613 PILLSBURY WINTHROP SHAW PITTMAN 613 (Aug. 17, 2005), *available at* http://www.pillsburylaw.com/index.cfm?pageid=34&itemid=37801 (asserting that *Dura* left many loss causation issues unanswered); *Ninth Circuit Affirms Dismissal with Prejudice of* Corinthian Colleges *Securities Fraud Class Action*, CORP. & SECS. BLOG, Aug. 7, 2008, http://www.corporatesecuritieslawblog.com/securities-litigation-ninth-circuit-affirms-dismissal-with-prejudice-of-corinthian-colleges-securities-fraud-class-action.html (agreeing with strict pleading in *Metzler* decision); *Ninth Circuit Reverses Dismissal of Securities Fraud Complaint on Loss Causation Grounds Despite Three-Month Delay Between Corrective Disclosure and Market Reaction*, CORP. & SECS. BLOG, Sept. 2, 2008,

Under the Private Securities Litigation Reform Act ("PSLRA") and United States Supreme Court precedent, plaintiffs must plead some Rule 10b-5 elements with particularity.[12] By 1995, however, neither statutes nor case law clearly established pleading standards for loss causation pleading.[13] As a result, lower courts employed conflicting loss causation pleading standards, and in 2005 the Supreme Court addressed this conflict in *Dura Pharmaceuticals v. Broudo*.[14]

In *Dura*, the Supreme Court attempted to clarify the pleading standard for loss causation, but instead confused the standard further.[15] The Ninth Circuit found that plaintiff Daniel Broudo's

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http://www.corporatesecuritieslawblog.com/securities-litigation-ninth-circuit-reverses-dismissal-of-securities-fraud-complaint-on-loss-causation-grounds-despite-threemonth-delay-between-corrective-disclosure-and-market-reaction.html (stating that *Gilead* decision contrasts markedly with *Metzler*).

[12] 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misleading statements and omissions); *id.* § 78u-4(b)(2) (requiring particularized pleading for state of mind); *see* Basic, Inc. v. Levinson, 485 U.S. 224, 231-32 (1998) (requiring heightened pleading for misrepresentation or omission of material fact); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 196 (1976) (requiring heightened pleading for scienter).

[13] *See* 15 U.S.C. § 78u-4(b)(4) (prescribing loss causation requirements); *Dura*, 544 U.S. at 344-47 (deciding not to address loss causation questions aside from price inflation theory's validity); Gebhardt v. Conagra Foods, Inc., 335 F.3d 824, 831 (8th Cir. 2003) (holding that loss causation merely required plaintiff to plead that she paid artificially inflated prices for stocks); Knapp v. Ernst & Whinney, 90 F.3d 1431, 1437-38 (9th Cir. 1996) (same); *In re* Control Data Corp. Sec. Litig., 933 F.2d 616, 619-20 (8th Cir. 1991) (same). *But see* Semerenko v. Cendant Corp., 223 F.3d 165, 185 (3d Cir. 2000) (requiring plaintiff to establish that defendant's misrepresentation proximately caused stocks to decline in value); Robbins v. Kroger Props., Inc., 116 F.3d 1441, 1448 (11th Cir. 1997) (same). *See generally In re Daou*, 411 F.3d at 1014 (requiring Rule 9 heightened pleading for loss causation pleading); Lentell v. Merrill Lynch Co., 396 F.3d 161, 172-73 (3d Cir. 2005) (adopting zone of risk analysis for proximate cause); *In re* White Elec. Designs Corp., 416 F. Supp. 2d 754, 763 (D. Ariz. 2006) (requiring plaintiff to plead loss causation with particularity); *In re* Parlamat Sec. Litig., 375 F. Supp. 2d 278, 286 (S.D.N.Y. 2005) (applying Rule 8 notice pleading for loss causation pleading); *In re* Retek, Inc. Sec., No. CIV 02-4209, 2005 WL 3059566, at *1, *3 (D. Minn. Oct. 21, 2005) (same).

[14] *See Dura*, 544 U.S. at 336 (reconciling circuit split over whether price inflation theory establishes loss causation); *Gebhardt*, 335 F.3d at 831 (holding that loss causation merely required plaintiff to plead that she paid artificially inflated prices for stocks); *Knapp*, 90 F.3d at 1437-38 (same); *In re Control Data Corp.*, 933 F.2d at 619-20 (same). *But see Semerenko*, 223 F.3d at 177 (requiring plaintiff to establish that defendant's misrepresentation caused stocks to decline in value); *Robbins*, 116 F.3d at 1448 (same).

[15] *See Dura*, 544 U.S. at 336 (reconciling circuit split over whether price inflation theory establishes loss causation). *Compare* Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1063 (9th Cir. 2008) (adopting strict proximate cause burden), *with In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057-58 (9th Cir. 2008) (favoring Third Circuit's proximate cause analysis and more lenient pleading requirements). *See*

allegation that he purchased artificially inflated Dura Pharmaceuticals stock satisfied loss causation.[16] The Supreme Court disagreed, holding that to survive the motion to dismiss Broudo had to establish that Dura Pharmaceuticals' misrepresentation proximately caused his loss.[17] The Supreme Court thus defined loss causation synonymously with proximate cause.[18] Unfortunately, the Court did not clarify the contours of proximate cause, stirring more disagreement in lower courts about the proper pleading standards for loss causation.[19]

Dura's unanswered questions generated a loss causation conflict within the Ninth Circuit Court of Appeals.[20] The Ninth Circuit's 2008 decisions in *Metzler Investment GMBH v. Corinthian Colleges* and *In re Gilead Sciences* illustrate this conflict.[21] *Metzler* adopts heightened loss causation pleadings by requiring the plaintiff to provide sound empirical evidence that the market understood the fraud in order to establish proximate cause.[22] By contrast, *Gilead*'s more lenient pleading standard permits the plaintiff to establish proximate cause through a chain of inferences linking fraud to the plaintiff's loss.[23] As illustrated by these two cases, the procedural uncertainty attributable

generally In re Daou, 411 F.3d at 1014 (requiring Rule 9 heightened pleading for loss causation pleading); *Lentell*, 396 F.3d at 172-73 (adopting zone of risk analysis for proximate cause); *In re White Elec.*, 416 F. Supp. 2d at 763 (requiring plaintiff to plead loss causation with particularity); *In re Parlamat*, 375 F. Supp. 2d at 286 (requiring Rule 8 notice pleading for loss causation pleading); *In re Retek*, 2005 WL 3059566, at *1, *3 (same).

[16] *Dura*, 544 U.S. at 337, 344-47.

[17] *Id.* at 344-47.

[18] *See id.* This Comment uses the term loss causation and proximate cause interchangeably in conformity with the Supreme Court's decision in *Dura*.

[19] *See id.*; *Metzler*, 540 F.3d at 1063 (adopting strict proximate cause burden); *In re Gilead*, 536 F.3d at 1057-58 (endorsing broad proximate cause formulation); *see also In re Daou*, 411 F.3d at 1014 (requiring Rule 9 heightened pleading for loss causation pleading); *Lentell*, 396 F.3d at 172-73 (adopting zone of risk analysis for proximate cause); *In re White Elec.*, 416 F. Supp. 2d at 763 (requiring plaintiff to plead loss causation with particularity); *In re Parlamat*, 375 F. Supp. 2d at 286 (requiring Rule 8 notice pleading for loss causation pleading); *In re Retek*, 2005 WL 3059566, at *1, *3 (same).

[20] *Compare Metzler*, 540 F.3d at 1063 (adopting strict proximate cause burden), *and In re Daou*, 411 F.3d at 1014 (requiring Rule 9 heightened pleading for loss causation pleading), *with In re Gilead*, 536 F.3d at 1057-58 (favoring Third Circuit's proximate cause analysis and more lenient pleading requirements).

[21] *See generally Metzler*, 540 F.3d 1049 (adopting strict analysis of proximate cause and heightened pleading for loss causation); *In re Gilead*, 536 F.3d 1049 (permitting broad interpretation of proximate cause and notice pleading for loss causation).

[22] *Metzler*, 540 F.3d at 1063.

[23] *In re Gilead*, 536 F.3d at 1057-58.

to *Dura's* elusive loss causation holding has led to an additional hurdle for plaintiffs.[24] This same uncertainty may also hinder efforts to restore confidence in U.S. public markets.[25]

This Comment argues that the Ninth Circuit's decision in *Gilead* sets forth the proper pleading standards for loss causation.[26] Part I examines the legal background of loss causation under Rule 10b-5, the PSLRA, and the Supreme Court's decision in *Dura*.[27] Part II explores the Ninth Circuit's loss causation decisions in *Metzler* and *Gilead*, and explains why they are irreconcilable.[28] Part III offers three reasons the Ninth Circuit should reconcile its intra-circuit split in favor of *Gilead*'s pleading standards.[29] First, *Gilead* is consistent with the Supreme Court's loss causation decision in *Dura*.[30] Second, *Gilead*'s notice pleading standard respects Congress's decision not to impose heightened loss causation pleading standards in the PSLRA.[31] Third, *Gilead*'s standard better effectuates Rule 10b-5's deterrence function, which is necessary to restore investor confidence in the U.S. public markets.[32] This Comment concludes by urging the Ninth Circuit to resolve its intra-circuit split by adopting Gilead's notice pleading standard.[33] It further suggests that if the Supreme Court re-examines *Dura*'s loss causation holding, the Court should articulate more definite guidelines that embrace *Gilead*'s broad formulation of loss causation pleadings.[34]

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[24] *See* sources cited *supra* note 11 (demonstrating confusion over loss causation pleading standard after *Dura*).

[25] *See* Kenneth P. Held et al., *Recent Treatment of Loss Causation Across the Circuits*, in *Securities Litigation Insights*, VINSON & ELKINS 7, Fall 2009, at 7-10, *available at* http://www.vinson-elkins.com/uploadedFiles/VEsite/Resources/SecuritiesLitigationInsights Fall2009.pdf (presenting recent conflicting treatment of loss causation among circuit courts); *see also* sources cited *supra* note 10 (demonstrating urgency and necessity to restore confidence in U.S. public markets in light of current financial crisis).

[26] *See infra* Part III.

[27] *See infra* Part I.

[28] *See infra* Part II. *See generally* Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049 (9th Cir. 2008); *In re Gilead*, 536 F.3d 1049 (permitting broad interpretation of proximate cause and notice pleading for loss causation).

[29] *See infra* Part III.

[30] *See infra* Part III.A.

[31] *See infra* Part III.B.

[32] *See infra* Part III.C.

[33] *See infra* Part III.C (discussing how *Gilead* better effectuates Congress's intent behind PSLRA and comports with Supreme Court's decision in *Dura*).

[34] *See* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 344 (2005) (requiring Broudo to prove that fraud proximately caused his economic loss); *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057-58 (9th Cir. 2008) (holding that class proved proximate cause

I. BACKGROUND

The Ninth Circuit's decisions in *Metzler* and *Gilead* reach diametric conclusions on the proper pleading standard for loss causation under Rule 10b-5.[35] To analyze these opposing views, it is necessary to first outline the history and elements of the Rule 10b-5 cause of action.[36] From there, this Part explores the evolution of loss causation from its origin as judicial doctrine to its codification in the PSLRA.[37] With these foundations in mind, this Part then describes the Supreme Court's landmark loss causation decision in *Dura*, which set the stage for the conflict between *Metzler* and *Gilead*.[38]

A. *History of the Rule 10b-5 Action*

Congress enacted the Securities Exchange Act of 1934 ("1934 Act") in reaction to the market collapse in 1929.[39] During the years leading to the Great Depression, United States public markets were largely unregulated and many investors unknowingly invested in fraudulent stocks.[40] Without regulation such fraud continued relatively unchecked, culminating in the stock market crash of 1929.[41]

by linking corrective disclosure and loss to fraud); *see also infra* Part II.A.

[35] *See generally* Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049 (9th Cir. 2008) (adopting strict pleading standard for loss causation); *In re Gilead*, 536 F.3d 1049 (permitting lower pleading standards for loss causation).

[36] *See infra* Part I.A.

[37] *See* Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 730 (1975) (approving lower court's decision to grant private 10b-5 remedy); *see also Dura*, 544 U.S. at 337; *In re* Daou Sys., Inc., 411 F.3d 1006, 1014 (9th Cir. 2005). *See generally* 17 C.F.R. § 240.10b-5 (2006) (prohibiting use of fraud in purchase or sale of securities but providing no language in support of private securities fraud claims).

[38] *See infra* Part I.C. *See generally Dura*, 544 U.S. 336 (choosing not to consider loss causation questions aside from price inflation); *Metzler*, 540 F.3d 1049 (adopting strict pleading standard for loss causation); *In re Gilead*, 536 F.3d 1049 (permitting lower pleading standards for loss causation).

[39] *See* 15 U.S.C. § 78j (2006); H.R. REP. NO. 73-85, at 2-3 (1933); James Landis, *The Legislative History of the Securities Act of 1933*, 28 GEO. WASH. L. REV. 29, 30 (1959); Highlight Invs. Group, *History of U.S. Stock Market Crashes*, http://www.marketvolume.com/info/stock_market_crashes.asp (last visited Feb. 3, 2009).

[40] *See* H.R. REP. NO. 73-85, at 2-3; *see also* Landis, *supra* note 39, at 30; Highlight Invs. Group, *supra* note 39.

[41] *See* H.R. REP. NO. 73-85, at 2-3; JAMES COX ET AL., SECURITIES REGULATION: CASES AND MATERIALS 6 (6th ed. 2009); *see also* Landis, *supra* note 39, at 30; Finanzas e Inversion, *Could the Crash of 1929 Be Repeated?*, http://www.wharton.universia.net/index.cfm?fa=viewArticle&id=860&language=english (last visited Feb. 3, 2009); Highlight Invs. Group, *supra* note 39.

In response, Congress enacted the 1934 Act to require disclosure and proscribe deception in the sale and purchase of securities.[42] The 1934 Act sought to restore confidence in the market by requiring all publicly traded corporations to make mandatory public disclosures.[43] Section 10(b) of the 1934 Act sought to deter fraud by prohibiting manipulative or deceptive devices in the sale or purchase of securities.[44] To further these goals, Congress gave the Securities and Exchange Commission ("SEC") authority to promulgate rules encompassing the 1934 Act.[45]

Pursuant to this authority, the SEC adopted Rule 10b-5 in 1942 to deter corporate fiduciaries from misleading public investors for personal gain.[46] Mirroring Section 10(b)'s language, Rule 10b-5 makes it illegal for anyone to provide misleading statements in connection with the sale or purchase of securities.[47] Today, Rule 10b-5 remains the SEC's preferred vehicle for civil and criminal prosecution of corporate actors who mislead the investing public.[48]

Although Rule 10b-5 did not expressly create a private right of action, in 1975 the Supreme Court recognized an implied right in *Blue Chip Stamps v. Manor Drug Stores*.[49] Thereafter, private 10b-5 claims

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[42] 15 U.S.C. § 78j; *see* S. REP. NO. 104-98, at 4 (1995); H.R. REP. NO. 104-369, at 3 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 679, 682; *see also Dura*, 544 U.S. at 345.

[43] *See* S. REP. NO. 104-98, at 4, *reprinted in* 1995 U.S.C.C.A.N. 679, 683; H.R. REP. NO. 104-369, at 3 (Conf. Rep.); COX ET AL., *supra* note 41, at 5 (stating that "Congress' enactment of [] securities laws was devoted to accounts of trading practices by unscrupulous market manipulators"); *see also Dura*, 544 U.S. at 345; United States v. O'Hagan, 521 U.S. 642, 644 (1997); Randall v. Loftsgaarden, 478 U.S. 647, 664 (1986).

[44] *See* 15 U.S.C. § 78j; *Dura*, 544 U.S. at 345; *O'Hagan*, 521 U.S. at 644; S. REP. NO. 104-98; H.R. REP. NO. 104-369, at 3 (Conf. Rep.).

[45] *See* Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 729 (1975); *see also Dura*, 544 U.S. at 341; *O'Hagan*, 521 U.S. at 644; Livid Holdings v. Salomon Smith Barney, Inc., 416 F.3d 940, 946 (9th Cir. 2005); 17 C.F.R. § 240.10b-5 (2006).

[46] *See* 17 C.F.R. § 240.10b-5; Employment of Manipulative and Deceptive Devices, Exchange Act Release No. 3230, 1942 SEC LEXIS 485 (May 21, 1942); Thomas Lee Hazen, The Jurisprudence of SEC Rule 10b-5, Address at Securities Law for Nonsecurities Lawyers (July 28-29, 2005), *available at* http://files.ali-aba.org/thumbs/datastorage/skoobescruoc/pdf/Cl001-ch36Uthumb.pdf; *see also Dura*, 544 U.S. at 341; Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1064 (9th Cir. 2008); *In re* Daou Sys., Inc., 411 F.3d 1006, 1014 (9th Cir. 2005).

[47] *See Blue Chip Stamps*, 421 U.S. at 729-30; 17 C.F.R. § 240.10b-5; *see also Dura*, 544 U.S. at 341; *O'Hagan*, 521 U.S. at 643.

[48] *See* 17 C.F.R. § 240.10b-5; *see also Dura*, 544 U.S. at 341; *Metzler*, 540 F.3d at 1064; *In re Daou*, 411 F.3d at 1014.

[49] *Blue Chip Stamps*, 421 U.S. at 729-30 (approving private Rule 10b-5 securities

increased Rule 10b-5's deterrence potential as plaintiffs's attorneys became significant players in monitoring corporate conduct.[50] By creating potential civil liability, the private 10b-5 action stimulated corporate diligence and furthered the 1934 Act's goals of restoring confidence in public markets.[51] Private 10b-5 claims, however, also became vehicles for abusive practices, including frivolous suits.[52] Thus, although private 10b-5 actions deterred fraud, they also had the potential to clog judicial dockets with unmeritorious claims.[53]

B. Loss Causation and the PSLRA

There are six elements of a private Rule 10b-5 action.[54] These elements were developed by lower courts; neither Congress nor the SEC expressly contemplated private Rule 10b-5 actions.[55] The first five

fraud claims and recognizing that ". . . the history of [Section 10(b) does not] provide any indication that Congress considered the problem of private rights under it at the time of its passage. Similarly, there is no indication that the Commission in adopting Rule 10b-5 considered the question of private civil remedies under this provision"); *see* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 196 (1976) (indicating that neither Congress or Commission contemplated creation of private right of action under Rule 10b-5); *cf.* 15 U.S.C. § 78j (reflecting no mention of private right to securities fraud claims); *Dura*, 544 U.S. at 344 (recognizing private Rule 10b-5's judicially inferred elements); 17 C.F.R. § 240.10b-5 (reflecting no mention of private Rule 10b-5 claims).

[50] *See Dura*, 544 U.S. at 345 (stating that securities statutes deter fraud, in part, through private securities fraud action); *O'Hagan*, 521 U.S. at 664; Randall v. Loftsgaarden, 478 U.S. 647, 664 (1986); Elizabeth Chamblee Burch, *Reassessing Damages in Securities Fraud Class Actions*, 66 MD. L. REV. 348, 380-81 (2007).

[51] *See* S. REP. NO. 104-98, at 4 (1995), *reprinted in* 1995 U.S.C.C.A.N. 679, 683; H.R. REP. NO. 104-369, at 3 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 679, 682; *see also Dura*, 544 U.S. at 345 (stating that private securities actions assist in deterring corporate fraud); *O'Hagan*, 521 U.S. at 644; *Loftsgaarden*, 478 U.S at 664; Burch, *supra* note 50, at 380-81.

[52] *See Dura*, 544 U.S. at 347 (recognizing that private 10b-5 remedy has potential for abusive routine filing of suits); *Blue Chip Stamps*, 421 U.S. at 741 (same); *Metzler*, 540 F.3d at 1064 (same); H.R. REP. NO. 104-369, at 3 (Conf. Rep.) (same).

[53] *See Dura*, 544 U.S. at 345; *O'Hagan*, 521 U.S. at 644; *In re Daou*, 411 F.3d at 1014. *But see Dura*, 544 U.S. at 347 (recognizing that private Rule 10b-5 remedy has potential for abusive routine filing of suits); *Blue Chip Stamps*, 421 U.S. at 741 (same); *Metzler*, 540 F.3d at 1064 (same); H.R. REP. NO. 104-369, at 3 (Conf. Rep.) (same).

[54] *See Dura*, 544 U.S. at 341; *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1055 (9th Cir. 2008) (identifying basic elements of 10b-5 claims); *In re Daou*, 411 F.3d at 1014; 17 C.F.R. § 240.10b-5.

[55] *See* 15 U.S.C. § 78j(b) (2006) (reflecting no mention of private right to securities fraud claims); 17 C.F.R. § 240.10b-5 (reflecting no mention of private 10b-5 claims); *see also Dura*, 544 U.S. at 341-43 (recognizing judge-made elements for 10b-5 claims); *Blue Chip Stamps*, 421 U.S. at 730 (recognizing private 10b-5 securities fraud claims); *Metzler*, 540 F.3d at 1061; *In re Gilead*, 536 F.3d at 1055 (identifying basic elements of

elements draw on common law deceit: (1) misrepresentation,[56] (2) scienter,[57] (3) connection with the purchase or sale of security,[58] (4) transaction causation,[59] and (5) economic loss.[60] Consistent with these roots in common law deceit, lower courts imposed particularized pleading for elements such as misrepresentation and scienter.[61] In contrast, lower courts also developed a sixth element — loss causation — from the common law doctrine of proximate cause.[62] Unlike the other Rule 10b-5 elements, loss causation merely requires proof of a causal connection between the company's fraud and the plaintiff's economic loss.[63] As with proximate cause, a defendant's proof of intervening causal factors establishes an affirmative defense to loss causation.[64] Because of this, defendant corporations often contest the

10b-5 claims); Livid Holdings v. Salomon Smith Barney, Inc., 416 F.3d 940, 946 (9th Cir. 2005); *In re Daou*, 411 F.3d at 1014 (citing *Dura*, 544 U.S. at 341-43).

56 *See Dura*, 544 U.S. at 341; Basic, Inc. v. Levinson, 485 U.S. 224, 231-32 (1998); *In re Daou*, 411 F.3d at 1014.

57 *See Dura*, 544 U.S. at 341; Ernst & Ernst v. Hochfelder, 425 U.S. 185, 197 (1976); *In re Daou*, 411 F.3d at 1014; Greebel v. FTP Software, Inc., 194 F.3d 185, 203 (1st Cir. 1999); *see also In re* McKesson HBOC, Inc. Sec. Litig., 126 F. Supp. 2d 1248, 1273 (N.D. Cal. 2000).

58 *See Dura*, 544 U.S. at 341; *Blue Chip Stamps*, 421 U.S. at 730; *In re Daou*, 411 F.3d at 1014.

59 *See* Hatrock v. Edward D. Jones & Co., 750 F.2d 767, 773 (9th Cir. 1984) (explaining that transactional causation requires proof that plaintiff relied on misrepresentation); Huddleston v. Herman & MacLean, 640 F.2d 534, 547-49 (5th Cir. 1981); Schlick v. Penn-Dixie Cement Corp., 507 F.2d 374, 380 (2d Cir. 1973).

60 *See Dura*, 544 U.S. at 341; *Livid Holdings*, 416 F.3d at 946; *In re Daou*, 411 F.3d at 1014.

61 *See Dura*, 544 U.S. at 343 (recognizing that judicially implied private securities elements stemmed from common law deceit); *Basic*, 485 U.S. at 231-32 (requiring heightened pleading for material misrepresentation or omissions); *Hochfelder*, 425 U.S. at 204 (requiring heightened pleading for scienter); *Blue Chip Stamps*, 421 U.S. at 746; *In re Daou*, 411 F.3d at 1014.

62 *See Dura*, 544 U.S. at 342; Tricontinental Indus. v. Pricewaterhouse Coopers, 475 F.3d 824, 842 (7th Cir. 2007); *In re Daou*, 411 F.3d at 1014; Caremark, Inc. v. Coram Healthcare Corp., 113 F.3d 645, 648 (7th Cir. 1997).

63 *See Dura*, 544 U.S. at 344-47; Teachers' Ret. Sys. of La. v. Hunter, 477 F.3d 162, 186 (4th Cir. 2007); *In re Daou*, 411 F.3d at 1014, 1025; Sec. Inv. Prot. Corp. v. Vigman, 908 F.2d 1461, 1467-68 (9th Cir. 1990); Weiss v. Amkor Tech., Inc., 527 F. Supp. 2d 938, 946-48 (D. Ariz. 2007); Initial Pub. Offering Sec. Litig., 399 F. Supp. 2d 261, 266, 308 (S.D.N.Y. 2005); *see also In re* Compuware Sec. Litig., 386 F. Supp. 2d 913, 918 (E.D. Mich. 2005).

64 *See Dura*, 544 U.S. at 342-43; *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057-58 (9th Cir. 2008); *see also* Ferrell & Saha, *supra* note 9, at 166-67.

adequacy of a plaintiff's loss causation theory by moving to dismiss the Rule 10b-5 claim.[65]

Congress codified and standardized these six elements when it enacted the PSLRA in 1995.[66] The PSLRA supplied pleading requirements for each 10b-5 element and expressly requires the plaintiff's "complaint" to "plead" with particularity the elements of misrepresentation and scienter.[67] The PSLRA also sought to reduce frivolous private securities suits by imposing heightened pleading requirements for some 10b-5 elements such as misrepresentation and scienter.[68] In this way, the PSLRA was consistent with Rule 9 of the Federal Rules of Civil Procedure, which requires particularized pleading for averments of fraud.[69]

By contrast, the PSLRA's loss causation provisions did not impose particularized pleading requirements.[70] Unlike the PSLRA's provisions for misrepresentation and scienter, the PSLRA's loss causation provision does not mention "plead[ings]" or "complaint[s]."[71] Instead,

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[65] *See Dura*, 544 U.S. at 340; *In re Gilead*, 536 F.3d at 1057; *Teachers' Ret. Sys. of La.*, 477 F.3d at 167; *Tricontintental Indus.*, 475 F.3d at 827; *Livid Holdings*, 416 F.3d at 944.

[66] Pub. L. No. 104-67, § 101, 109 Stat. 737, 758 (1995) (codified at 15 U.S.C. § 78u-4(b)(4) (2006)); *Dura*, 544 U.S. at 345-46; *In re Daou*, 411 F.3d at 1014; *In re* Vantive Corp., 283 F.3d 1079, 1083-84 (9th Cir. 2002); Schlick v. Penn-Dixie Cement Corp., 507 F.2d 374, 380 (2d Cir. 1974) (discussing judicially inferred element of loss causation prior to PSLRA).

[67] *See* 15 U.S.C. § 78u-4 (2006) (setting forth 10b-5 elements); *id.* § 78u-4(b)(1)-(2) (requiring particularized pleading for misrepresentation and scienter); *see also Livid Holdings*, 416 F.3d at 946; Roconi v. Larkin, 253 F.3d 423, 429 (9th Cir. 2001); Greebel v. FTP Software, Inc., 194 F.3d 185, 203-04 (1st Cir. 1999).

[68] *See Dura*, 544 U.S. 344-47 (discussing Congress's intent to reduce frivolous litigation); Basic, Inc. v. Levinson, 485 U.S. 224, 231-32 (2006). *See generally* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation); *id.* § 78u-4(b)(2) (requiring particularized pleading for scienter).

[69] *Compare* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation), *and id.* § 78u-4(b)(2) (requiring particularized pleading for scienter), *with* FED. R. CIV. P. 9(b) (requiring particularized pleading for averments of fraud), *and Teachers' Ret. Sys. of La.*, 477 F.3d at 185-86 (recognizing that loss causation pleading could fall under Rule 9(b)).

[70] *Compare* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation), *and id.* § 78u-4(b)(2) (requiring particularized pleading for scienter), *with id.* § 78u-4(b)(4) (requiring proof that defendant's fraud caused plaintiff's loss).

[71] *Compare id.* § 78u-4(b)(1) (requiring particularized pleading for misrepresentation), *and id.* § 78u-4(b)(2) (requiring particularized pleading for scienter), *with* FED. R. CIV. P. 9(b) (requiring particularized pleading for averments of fraud). *But see* 15 U.S.C. § 78u-4(b)(4) (requiring proof that defendant's fraud caused plaintiff's loss).

the PSLRA's loss causation requirement calls for proof of a causal connection between the company's misrepresentation and the plaintiff's economic loss.[72] Consequently, some courts have held that Rule 8 governs loss causation pleadings, requiring only a short and plain statement of the plaintiff's causation theory.[73] Other courts have concluded that Rule 9 applies.[74]

Following the PSLRA's enactment, lower courts also disagreed on whether pleading "price inflation" was sufficient to establish loss causation.[75] Some courts held that a plaintiff could satisfy loss causation by demonstrating that the defendant company's misrepresentation artificially raised the price she paid for the company's stock.[76] In contrast, other courts held that a plaintiff could not suffer a Rule 10b-5 injury by merely purchasing an artificially inflated stock.[77] To plead loss causation, these courts instead required

[72] *See* 15 U.S.C. § 78u-4(b)(1)-(3); 17 C.F.R. § 240.10b-5 (2006); *see also Dura*, 544 U.S. at 341, 344-47 (recognizing that securities statutes permit actions where plaintiffs properly prove causation and loss); *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1055 (9th Cir. 2008) (requiring proof of a causal connection); *In re* Daou Sys., Inc., 411 F.3d 1006, 1014 (9th Cir. 2005); Hatrock v. Edward D. Jones & Co., 750 F.2d 767, 774 & n.5 (9th Cir. 1984); Weiss v. Amkor Tech., Inc., 527 F. Supp. 2d 938, 948 (D. Ariz. 2007); *In re* Pub. Offering Sec. Litig., 399 F. Supp. 2d 298, 308 (S.D.N.Y. 2005); *In re* Compuware Sec. Litig., 386 F. Supp. 2d 913, 918 (E.D. Mich. 2005).

[73] *See, e.g.*, Hunt v. Enzo Biochem, Inc., 471 F. Supp. 2d 390, 409 n.120 (S.D.N.Y. 2006) (interpreting *Dura* as permitting loss causation pleading under Rule 8); *In re* Parlamat Sec. Litig., 375 F. Supp. 2d 278, 286 (S.D.N.Y. 2005) (requiring Rule 8 notice pleading for loss causation pleading); *In re* Retek, Inc. Sec., No. CIV 02-4209, 2005 WL 3059566, at *1, *3 (D. Minn. Oct. 21, 2005) (same).

[74] *See, e.g.*, *In re Daou*, 411 F.3d at 1014 (requiring Rule 9 heightened pleading for loss causation pleading); Caremark, Inc. v. Coram Healthcare Corp., 113 F.3d 645, 650 n.7 (7th Cir. 1997) (discussing applicability of Rule 9 pleading standard); *In re* White Elec. Designs Corp., 416 F. Supp. 2d 754, 763 (D. Ariz. 2006) (requiring plaintiff to plead loss causation with particularity).

[75] *See* 15 U.S.C. § 78u-4(b)(4) (requiring proof of causation but not mentioning pleading requirements); Gebhardt v. Con Agra Foods, Inc., 335 F.3d 824, 831 (8th Cir. 2003) (holding that loss causation merely required plaintiff to plead that she paid artificially inflated prices for stocks); Knapp v. Ernst & Whinney, 90 F.3d 1431, 1437-38 (9th Cir. 1996) (same); *In re* Control Data Corp. Sec. Litig., 933 F.2d 616, 619-20 (8th Cir. 1991) (same). *But see* Semerenko v. Cendant Corp., 223 F.3d 165, 177 (3d Cir. 2000) (requiring proof that defendant's fraud caused plaintiff's loss); Robbins v. Kroger Props., Inc., 116 F.3d 1441, 1448 (11th Cir. 1997) (same).

[76] *See Dura*, 544 U.S. at 344; Lentell v. Merrill Lynch Co., 396 F.3d 161, 172-73 (3d Cir. 2005); *Gebhardt*, 335 F.3d at 831; *Knapp*, 90 F.3d at 1437-38; *In re Control Data Corp.*, 933 F.2d at 619-20.

[77] *See* Newton v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 259 F.3d 154, 174 (3d Cir. 2001); *Semerenko*, 223 F.3d at 177; *Robbins*, 116 F.3d at 1448.

the plaintiff to show that the defendant company's misrepresentation caused her stocks to decrease in value.[78] In 2005, the Supreme Court granted certiorari to resolve this split.[79]

C. Dura Pharmaceuticals v. Broudo

The dispute in *Dura* centered on the adequacy of the plaintiff's loss causation pleading.[80] The plaintiff, Daniel Broudo, sued Dura Pharmaceuticals under Rule 10b-5, alleging that due to Dura's misleading financial forecasts, he paid artificially inflated prices for Dura's stocks.[81] The district court granted Dura's Rule 12(b)(6) motion to dismiss, concluding that Broudo failed to plead that Dura's fraud proximately caused any economic loss.[82] The Ninth Circuit reversed on appeal, approving Broudo's price inflation theory as sufficient to establish loss causation.[83]

On review, the Supreme Court dismissed Broudo's complaint and held that Broudo did not establish an economic loss or a sufficient loss causation theory.[84] First, the Court observed that a plaintiff suffers an economic loss only when the company's fraud causes its stocks to drop significantly in value.[85] Because Broudo claimed that he suffered an injury by paying inflated stock prices, the Court held that he failed to establish an economic loss.[86] Second, the Court recognized that price inflation's lenient standard might transform Rule 10b-5 into investors' insurance by enabling investors to sue whenever stock prices fall.[87] The Court thus held that loss causation was tantamount to proximate cause and required Broudo to establish a causal theory linking fraud to his loss.[88] The holding was not comprehensive, however, as the Court left at least two issues unanswered.[89] First, the

[78] *See, e.g.*, *Newton*, 259 F.3d at 174 (requiring proof of proximate cause); *Semerenko*, 223 F.3d at 177 (requiring proof that defendant's fraud caused plaintiff's loss); *Robbins*, 116 F.3d at 1448 (same).

[79] *See generally Dura*, 544 U.S. 336 (reconciling circuit split over whether price inflation establishes loss causation).

[80] *See id.* at 337.

[81] *Id.*

[82] *Id.* at 338.

[83] *Id.*

[84] *Id.* at 344-47.

[85] *Id.* at 347.

[86] *Id.* at 344-46.

[87] *Id.* at 344-47.

[88] *See id.*

[89] *See id.* at 336, 344-47 (choosing not to address other issues related to proximate

Court did not specify the contours of proximate cause under Rule 10b-5.[90] Second, it did not specify whether notice or heightened pleadings govern loss causation.[91] Even so, the Court's language manifests guiding principles.[92]

Dura held that loss causation required proof that the company's shares fell significantly after revelation of the "truth."[93] Lower courts refer to this truth as "corrective disclosure."[94] The Supreme Court did not specify what factual predicates constitute a corrective disclosure, nor did it explain what it meant by "truth."[95] Yet the Court did state that loss causation pleadings should not impose a great burden on private 10b-5 plaintiffs.[96]

Dura further recognized that the Federal Rules of Civil Procedure and securities statutes merely require a short and plain statement suggesting a loss causation theory.[97] The Court indicated that Broudo should have provided notice of his causation theory, but rejected those complaints manifesting a "faint hope" of producing plausible actions.[98] If a plaintiff provided "some" indication of her loss and causation theory, however, her Rule 10b-5 claim would survive Rule 12(b)(6).[99] Because of *Dura*'s elusive instructions, some courts interpreted *Dura* to require Rule 8 notice pleadings, while others required Rule 9 heightened pleadings.[100]

cause and issues related to pleading standards).

[90] *See id.*

[91] *See id.* at 344-47.

[92] *See id.* (establishing that loss causation required proximate cause and revelation of truth).

[93] *Id.*

[94] *Id.* at 347; *see* Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1064-65 (9th Cir. 2008) (adopting strict proximate cause pleading burden); *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1058 (9th Cir. 2008); Weiss v. Amkor Tech., Inc., 527 F. Supp. 2d 938, 946 (D. Ariz. 2007).

[95] *See Dura*, 544 U.S. at 346-47.

[96] *Id.* at 347.

[97] *Id.* at 346.

[98] *See id.* at 346-47.

[99] *See id.*

[100] *See* Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1063 (9th Cir. 2008); *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057-58 (9th Cir. 2008) (favoring Third Circuit's proximate cause analysis but not explicitly adopting zone of risk); Lentell v. Merrill Lynch Co., 396 F.3d 161, 172-73 (3d Cir. 2005) (adopting zone of risk analysis for proximate cause); *see also In re* Daou Sys., Inc., 411 F.3d 1006, 1014 (9th Cir. 2005) (requiring Rule 9 heightened pleading for loss causation pleading); *In re* White Elec. Designs Corp., 416 F. Supp. 2d 754, 763 (D. Ariz. 2006) (requiring plaintiff to plead loss causation with particularity); *In re* Parlamat Sec. Litig., 375 F. Supp. 2d 278, 286 (S.D.N.Y. 2005) (applying Rule 8 notice pleading for loss causation

II. INTRA-CIRCUIT SPLIT

Dura's lack of clarity produced dissonance among lower courts regarding the proper pleading standards for loss causation.[101] The Ninth Circuit's opinions in *Gilead* and *Metzler* provide an intra-circuit illustration of this divide, and reflect conflicting views on the requirements for establishing both a corrective disclosure and proximate causation.[102] Moreover, the decisions reflect diametric views on the proper pleading standards for loss causation.[103]

A. In re Gilead Sciences

In *Gilead*, class action plaintiffs brought a Rule 10b-5 claim alleging that Gilead Sciences misrepresented its off-label marketing practices to the public.[104] The class claimed that Gilead unlawfully marketed its product, Viread, but repeatedly assured the public that its marketing practices complied with federal and state regulations.[105] When the Federal Drug Administration publicly revealed a warning letter detailing Gilead's illegal practices, Gilead's customers switched to competitor brands and Viread's sales plummeted.[106] Even so, Gilead's stocks plunged only after Gilead revised its third quarter forecast.[107] Thus, the class's loss causation theory alleged that Gilead's true financial forecast linked the subsequent loss in stock value back to Gilead's marketing fraud.[108] The district court dismissed their claim under Rule 12(b)(6), concluding that the class failed to properly allege corrective disclosure or proximate cause.[109]

The Ninth Circuit reversed, finding instead that the class's complaint adequately pleaded both corrective disclosure and

pleading); *In re* Retek, Inc. Sec., No. CIV 02-4209, 2005 WL 3059566, at *2-3 (D. Minn. Oct. 21, 2005) (same).

[101] *See* sources cited *supra* note 100.

[102] *See generally Metzler*, 540 F.3d at 1064-65 (adopting strict pleading standard for loss causation and observing that revelation of true earnings does not constitute corrective disclosure); *In re Gilead*, 536 F.3d at 1058 (permitting lower pleading standards for loss causation and recognizing that true financial forecast constitutes corrective disclosure).

[103] *See* sources cited *supra* note 102.

[104] *In re Gilead*, 536 F.3d at 1050-51.

[105] *Id.* (explaining that off-label uses refer to non-FDA-approved uses).

[106] *Id.* at 1052-53.

[107] *Id.* at 1054.

[108] *See id.* at 1053-54.

[109] *Id.* at 1050.

proximate cause.[110] The court permitted the class to establish both theories through a chain of inferences linking Gilead's fraud to the class's loss.[111] First, the court looked to the public's reaction following the alleged disclosure to determine whether it constituted a corrective disclosure.[112] Following Gilead's press release, Gilead's investors promptly sold their stocks, causing the steep drop in Gilead's stock price.[113] Because the press release announcing Gilead's true financial forecast prompted the class's economic loss, the court concluded that it constituted a corrective disclosure.[114] Second, the court determined that the class sufficiently alleged proximate cause by showing that Gilead's corrective disclosure related to its misrepresentation.[115] The court observed that Gilead's true forecast reflected lowered earnings as a result of its illegal off-label marketing practices.[116] Accordingly, the court reasoned that the class established a plausible link between the class's loss in stock value and Gilead's marketing fraud.[117] *Gilead* thus held that a plaintiff satisfies proximate cause by identifying a corrective disclosure that links the plaintiff's loss back to the defendant's misrepresentation.[118]

Gilead did not expressly endorse either Rule 8 or Rule 9 of the Federal Rules of Civil Procedure.[119] Instead, the court required the class to plead only enough facts to support a reasonable expectation that discovery would produce evidence of loss causation.[120] The court recognized that a causation theory's plausibility evolves in later stages of the proceedings, when parties have access to discovery.[121] Thus, the holding in *Gilead* is that so long as the class's loss causation theory is not facially implausible, Rule 12(b)(6) dismissal is inappropriate.[122]

[110] *Id.* at 1055, 1058.
[111] *Id.* at 1057-58.
[112] *Id.* at 1056.
[113] *Id.* at 1054.
[114] *Id.* at 1056, 1058.
[115] *Id.* at 1056-58.
[116] *Id.* at 1058.
[117] *Id.*
[118] *Id.*
[119] *See id.* at 1056 (refusing to decide whether Rule 8 or Rule 9 governs loss causation pleadings).
[120] *See id.* at 1057.
[121] *See id.*
[122] *Id.*

B. Metzler v. Corinthian Colleges

Like *Gilead*, *Metzler* involved a dispute over the adequacy of the plaintiff's loss causation pleading.[123] Defendant Corinthian Colleges derived its revenue from federal educational funding, and in 2004 underwent investigation for manipulating financial aid documents.[124] *Financial Times* reported the investigation, and when Corinthian confirmed the story, its stock price fell by ten percent.[125] Corinthian's stock price dropped another forty five percent when it issued a press release revealing reduced earnings and another pending investigation.[126]

Metzler Investments GMBH, a Corinthian shareholder, brought suit under Rule 10b-5, alleging that both the *Financial Times* article and the press release constituted corrective disclosures revealing Corinthian's fraud.[127] Corinthian moved to dismiss under Rule 12(b)(6), arguing that Metzler failed to plead proximate causation and a corrective disclosure.[128] The district court agreed.[129]

The Ninth Circuit affirmed, holding that Metzler failed to plead loss causation.[130] Because the company released multiple pieces of information regarding its poor performance, the court held that neither the article nor the press release detailing Corinthian's true financial picture constituted a corrective disclosure.[131] Thus, the court recognized that neither publication established proximate cause because they failed to indicate that the market "understood" that fraud caused Corinthian's stock prices to fall.[132]

Although *Metzler* acknowledged that *Dura* did not require particularized pleading or an admission of fraud, it nevertheless rejected pleadings that merely support inferences of fraud.[133] *Metzler* required a corrective disclosure to reveal fraud, rather than the company's true financial picture resulting from fraud.[134] Accordingly, *Metzler*'s loss causation pleading standard requires the plaintiff to

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[123] Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1055 (9th Cir. 2008).

[124] *Id.* at 1055-56.

[125] *Id.* at 1057, 1059.

[126] *Id.* at 1059.

[127] *Id.*

[128] *Id.* at 1055.

[129] *Id.*

[130] *Id.* at 1055, 1072.

[131] *Id.* at 1063-65.

[132] *Id.* at 1065.

[133] *Id.* at 1064-65.

[134] *See id.*

present solid empirical evidence that the fraud affected the value of the company's stocks, a markedly different view of corrective disclosure and proximate causation than *Gilead*.[135]

III. Analysis

The Ninth Circuit's decision in *Gilead* represents the proper loss causation pleading standards for three reasons.[136] First, *Gilead*'s analysis is consistent with the Supreme Court's loss causation pleading standards in *Dura*.[137] Second, *Gilead*'s notice pleading standard comports with Congress's intent to not impose heightened pleading standards for loss causation in the PSLRA.[138] Third, *Gilead*'s standard better effectuates Rule 10b-5's fraud deterrence function which can benefit the current state of U.S. public markets.[139]

A. Gilead *Is Consistent with the Supreme Court's Decision in* Dura

Dura did not specify what constitutes corrective disclosure or how to link it to loss, but its language endorses a broad construction of loss causation.[140] First, *Dura* emphasized a broad formulation of proximate cause.[141] Second, *Dura* was more concerned with providing notice to defendants than imposing a great pleading burden on plaintiffs.[142] *Gilead* conforms to *Dura*'s construction of loss causation by endorsing a broad formulation of proximate cause that is consistent with notice pleading.[143]

1. A Broad Formulation of Proximate Cause

Dura recognized that loss causation was similar to the proximate cause element in common law torts.[144] Although the Court did not define the contours of proximate cause, it required a connection between a defendant's misrepresentation and a plaintiff's economic

[135] *See* cases cited *supra* note 102.
[136] *See infra* Part III.A-C.
[137] *See infra* Part III.A.
[138] *See infra* Part III.B.
[139] *See infra* Part III.C.
[140] *See* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 346 (2005).
[141] *Id.* at 344-47.
[142] *Id.* at 346-47.
[143] *Cf. In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057-58 (9th Cir. 2008) (rejecting bright-line rule for market reaction to fraud); *see also infra* Part III.A.1.
[144] *See Dura*, 544 U.S. at 343-44.

loss.[145] The Court suggested that Broudo had to establish that Dura's stock price fell significantly after a revelation of truth, but indicated that loss causation should not impose a great pleading burden on plaintiffs.[146] This suggests that the Supreme Court intended a broad formulation of proximate cause, requiring only a link between misrepresentation and the plaintiff's economic loss.[147]

Gilead adopts *Dura*'s broad formulation of proximate cause by permitting the class to plead facts supporting an inference of a plausible causal link.[148] The *Gilead* court recognized that the press release revealing the true financial forecast constituted a corrective disclosure because it prompted Gilead's stocks to plunge.[149] The court thus held that the class established proximate cause by alleging that Gilead's true financial forecast related to its fraudulent marketing practices.[150] Under *Gilead*, a plaintiff can establish a causal link by pleading that the defendant's disclosure triggered her financial loss and related to the defendant's misrepresentation.[151] Accordingly, *Gilead* mirrors *Dura*'s basic proximate cause requirements and assertion that loss causation pleading should not impose a great pleading burden on the plaintiff.[152]

By contrast, *Metzler*'s heightened proximate cause pleading requirement is inconsistent with *Dura*.[153] The *Metzler* court suggested that a corrective disclosure must reveal the fraud rather than the mere possibility of fraud.[154] Thus, although Corinthian's press release revealing its true financial forecast reflected earnings due to fraud, the court held that it was not a corrective disclosure.[155] Moreover, the

[145] *See id.* at 347.

[146] *See id.*; *see also* Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1064-65 (9th Cir. 2008) (recognizing that *Dura* did not impose great loss causation pleading burden for plaintiff); Weiss v. Amkor Tech., Inc., 527 F. Supp. 2d 938, 946 (D. Ariz. 2007) (same).

[147] *See Metzler*, 540 F.3d at 1064; *In re Gilead*, 536 F.3d at 1058.

[148] *In re Gilead*, 536 F.3d at 1057-58.

[149] *See id.*

[150] *Id.*

[151] *See id.* at 1058.

[152] *See* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 346-47 (2005); *In re Gilead*, 536 F.3d at 1057-58.

[153] Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1064-65 (9th Cir. 2008) (requiring that plaintiff prove market understood fraud in order to establish proximate cause).

[154] *See id.* at 1063-64 (suggesting that corrective disclosure revealing "risk" or "potential" of corporate fraud is insufficient to support element of loss causation under Supreme Court and Ninth Circuit precedent).

[155] *Id.* at 1065.

Metzler court refused to consider the stock drop following Corinthian's press release as proof of a corrective disclosure.[156] Instead, the court reasoned that a corrective disclosure must indicate that the market understood Corinthian's fraud.[157] This suggests that in order to plead proximate cause, Metzler should have established that Corinthian actually admitted or disclosed its fraudulent conduct to the public.[158] Consequently, *Metzler* reflects a narrow view of proximate cause, requiring corrective disclosure to reveal fraud rather than the company's true financial picture resulting from fraud.[159] This is unrealistic, overly burdensome, and contrary to *Dura*.[160] *Gilead*'s broad construction of corrective disclosure and proximate cause analysis better illustrates *Dura*'s loss causation pleading standards.[161]

2. Notice Pleading Standards for Loss Causation

Dura's language embraces a notice pleading standard for loss causation, even though *Dura* did not expressly hold that Rule 8 governed loss causation pleading.[162] Throughout the opinion, the *Dura* Court distinguished loss causation from misrepresentation and scienter, and suggested that loss causation was subject to a lower pleading burden.[163] *Dura* recognized that neither the Federal Rules nor the securities statutes require plaintiffs to plead more than a short and plain statement of loss causation.[164] Moreover, the Court insisted that Broudo should have provided Dura with "some" indication of the

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[156] *See id.* at 1064.

[157] *See id.*

[158] *See id.*

[159] *See id.*

[160] *See* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 344 (2005) (recognizing that loss causation reflects traditional requirements of proximate cause); *id.* at 347 (recognizing that loss causation pleadings should not create burdensome requirements for Broudo). *But see Metzler*, 540 F.3d at 1064 (requiring that public market understood fraud).

[161] *See Dura*, 544 U.S. at 344-47 (requiring Broudo to prove that fraud proximately caused his economic loss); *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057-58 (9th Cir. 2008) (holding that class proved proximate cause by linking corrective disclosure and loss to fraud); *see also supra* Part II.A.

[162] *See Dura*, 544 U.S. at 346.

[163] *See id.* at 344-46 (requiring particularized pleading for misrepresentation and scienter but recognizing that loss causation resembles proximate cause); *see also id.* at 347 (recognizing and assuming that securities statutes require nothing more than notice pleading for loss causation).

[164] *See id.* at 346.

causal connection between Dura's fraud and his economic loss.[165] Rather than a short and plain statement, the Court required Broudo to plead the elements of misrepresentation and scienter with particularity.[166] This distinction suggests that the Court intended notice pleading standards for loss causation.[167]

Gilead comports with *Dura*'s notice pleading standards because it requires facts sufficient to support an expectation that discovery will produce evidence of loss causation.[168] The *Gilead* court held that if a plaintiff's theory of loss causation is not facially implausible, a Rule 12(b)(6) dismissal is inappropriate.[169] Therefore, even though *Gilead* did not expressly endorse either Rule 8 or 9, the court's holding is consistent with a notice pleading standard.[170]

Even *Metzler* observed that loss causation under *Dura* does not require anything beyond Rule 8 notice pleadings, including an admission of fraud.[171] By requiring the plaintiff to establish that the market understood fraud, however, *Metzler* elevates the plaintiff's loss causation pleading burden beyond *Dura*'s requirements.[172] The *Metzler* court held that an inference of proximate causation would not be enough to properly plead loss causation.[173] Rather, the court proposed that Metzler should have established that the market in fact understood Corinthian's disclosures as revealing its fraud.[174] This suggests that *Metzler* requires a plaintiff to plead loss causation with a degree of certainty, thus demanding factual specificity beyond notice pleading requirements.[175]

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[165] *Id.* at 347.

[166] *See id.* at 346.

[167] *See supra* Part II.A; *see also* Hunt v. Enzo Biochem, Inc., 471 F. Supp. 2d 390, 409 n.120 (S.D.N.Y. 2006); Ong v. Sears, Roebuck & Co., 459 F. Supp. 2d 729, 742-43 (N.D. Ill. 2006); *In re* Enron Corp. Sec., Deriv. & ERISA Litig., 439 F. Supp. 2d 692, 714 (S.D. Tex. 2006).

[168] *See In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057 (9th Cir. 2008).

[169] *See id.*

[170] *See id.* at 1056.

[171] *See* Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1064 (9th Cir. 2008).

[172] *Compare* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 344-47 (2005) (recognizing that loss causation reflects traditional requirements of proximate cause and that pleading loss causation should not create burdensome requirements for plaintiff), *with Metzler*, 540 F.3d at 1064 (requiring that public market understood fraud).

[173] *See Metzler*, 540 F.3d at 1064-65.

[174] *Id.* at 1064.

[175] *Compare* FED. R. CIV. P. 8(a)(2) (requiring "a short and plain statement" of plaintiff's claim), *with Metzler*, 540 F.3d at 1064-65 (requiring proof that public

Some might argue that *Metzler*'s heightened loss causation pleading standards better addresses the Supreme Court's concern with preventing frivolous 10b-5 lawsuits.[176] The Court in *Dura* feared that a lenient loss causation standard would transform Rule 10b-5 actions into investors' insurance, thus explaining that it would dismiss those theories with only a "faint hope" of producing a plausible cause of action.[177] By requiring plaintiffs to plead loss causation with greater certainty, *Metzler*'s pleading standard reduces frivolous 10b-5 suits.[178]

Using a different approach, *Gilead*'s loss causation pleading standards and *Dura*'s proximate cause requirement also address the Supreme Court's concerns about frivolous Rule 10b-5 litigation.[179] The Ninth Circuit in *Gilead* required the class to prove that intervening causes did not cause its economic loss.[180] The presence of intervening causes remains an affirmative defense to loss causation, and effectively separates groundless 10b-5 claims from meritorious ones at the pleading stage.[181] Moreover, the Supreme Court's holding in *Dura* deters frivolous suits by rejecting the price inflation theory.[182] By requiring proof of proximate cause, *Dura* remains an effective hurdle for groundless Rule 10b-5 claims.[183]

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market understood fraud).

[176] *See Dura*, 544 U.S. at 345 (explaining that private securities fraud actions should not provide investors with broad insurance against losses); Basic, Inc. v. Levinson, 485 U.S. 224, 252 (1998); *Metzler*, 540 F.3d at 1063 (requiring plaintiff to show evidence that market understood fraud).

[177] *Dura*, 544 U.S. at 345, 347; *see also* H.R. REP. NO. 104-339, at 31 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 730, 730 (criticizing routine filing of frivolous lawsuits).

[178] *See Metzler*, 540 F.3d at 1063 (requiring plaintiff to show evidence that market understood fraud); *see also Dura*, 544 U.S. at 347 (recognizing that lenient standards run risk of permitting frivolous litigation); H.R. REP. NO. 104-339, at 31 (Conf. Rep.) (criticizing routine filing of frivolous lawsuits and adopting heightened pleading to prevent frivolous suits); *supra* Part II.B.

[179] *See Dura*, 544 U.S. at 347 (stating that proximate cause serves to avoid harm of increased frivolous lawsuits); *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057 (9th Cir. 2008) (requiring proof of reasonable proximate cause theory); *see also* McCabe v. Ernst & Young, LLP, 494 F.3d 418, 427 n.4 (3d Cir. 2007); Emergent Capital Inv. Mgmt., LLC v. Stonepath Group, Inc., 343 F.3d 189, 197 (2d Cir. 2003).

[180] *See In re Gilead*, 536 F.3d at 1057-58.

[181] *See id.*; *see also Dura*, 544 U.S. at 342-43 (recognizing that intervening causes may break causal chain); Ferrell & Saha, *supra* note 9, at 165-66 (same).

[182] *See Dura*, 544 U.S. at 347 (stating that proximate cause serves to avoid harm of increased frivolous lawsuits); Glaser v. Enzo Biochem, Inc., 464 F.3d 474, 477 (4th Cir. 2006); Madge S. Thorsen et al., *Rediscovering the Economics of Loss Causation*, 6 J. BUS. & SECS. L. 93, 105-06 (2006).

[183] *See Dura*, 544 U.S. at 347; *Enzo Biochem*, 464 F.3d at 477; Thorsen et al., *supra*

B. Gilead *Comports with Congress's Intent Not to Subject Loss Causation to Heightened Pleading Standards*

A literal and careful reading of the PSLRA's text reveals Congress's deliberate choice not to subject loss causation to heightened pleading requirements.[184] Under the PSLRA, the plaintiff's "complaint" must "plead" misrepresentation and scienter with particularity.[185] By contrast, the PSLRA's loss causation requirement merely allocates the burden of proof to the plaintiff and does not mention pleading standards, "plead[ings]," or "complaint[s]."[186] This suggests that Congress recognized that causation evidence emerges in the proof stage and did not intend to scrutinize loss causation at the pleadings stage.[187] Accordingly, Congress made no attempt to subject loss causation to heightened pleading standards elsewhere in the PSLRA.[188]

Gilead typifies congressional intent by imposing a notice pleading standard and recognizing that loss causation is "critical at the proof stage."[189] *Gilead* respects the PSLRA's distinction between loss causation pleading from the Rule 10b-5 elements requiring particularized pleading.[190] The court merely required that the plaintiff class plead a chain of inferences to establish a plausible loss causation theory.[191] *Gilead*'s standard thus mirrors a notice pleading requirement by calling only for a short and plain statement of a plausible causation

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note 182, at 105-06.

[184] *See* S. REP. NO. 104-98, at 4 (1995), *reprinted in* 1995 U.S.C.C.A.N. 679, 683; H.R. REP. NO. 104-369, at 41 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 730, 740. *Compare* 15 U.S.C. § 78u-4(b)(1) (2006) (requiring particularized pleading for misrepresentation), *and id.* § 78u-4(b)(2) (requiring particularized pleading for scienter), *with id.* § 78u-4(b)(4) (requiring that plaintiff prove causation between misrepresentation and loss).

[185] *See* 15 U.S.C. § 78u-4(b)(1)-(2).

[186] *See id.* § 78u-4(b)(4); *see also* Teachers' Ret. Sys. of La. v. Hunter, 477 F.3d 162, 186 (4th Cir. 2007).

[187] 15 U.S.C. § 78u-4(b)(4) (stating that plaintiff has burden of proving causal connection without mentioning pleading standards); *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057 (9th Cir. 2008); McCabe v. Ernst & Young, LLP, 494 F.3d 418, 427 n.4 (3d Cir. 2007); Emergent Capital Inv. Mgmt., LLC v. Stonepath Group, Inc., 343 F.3d 189, 197 (2d Cir. 2003).

[188] *See* sources cited *supra* note 187.

[189] *See In re Gilead*, 536 F.3d at 1057.

[190] *See id. Compare* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation), *and id.* § 78u-4(b)(2) (requiring particularized pleading for scienter), *with id.* § 78u-4(b)(4) (requiring proof of causal connection between fraud and loss).

[191] *See In re Gilead*, 536 F.3d at 1057-58.

theory.[192] Moreover, *Gilead* is consistent with Congress's recognition that proving loss causation is more appropriate during the proof stage rather than on a motion to dismiss.[193] *Gilead* recognizes that loss causation evolves after discovery and requires pleadings to merely support a reasonable expectation that discovery will reveal loss causation.[194] Thus, *Gilead* executes Congress's intent to not subject loss causation to heightened pleadings under the PSLRA.[195]

By contrast, *Metzler* ignores the PSLRA's language distinguishing loss causation from heightened pleading standards by requiring the plaintiff to plead loss causation with near certainty.[196] By demanding the plaintiff to produce solid evidence that the market understood defendant's fraud, the *Metzler* court essentially required the plaintiff to prove loss causation in the pleading stage.[197] This pleading requirement creates infeasible hurdles for Rule 10b-5 plaintiffs, because it means such plaintiffs must provide empirical evidence of causation prior to discovery.[198] Furthermore, by requiring a plaintiff to prove the disclosure of fraud, *Metzler* ignores the PSLRA's provision which simply asks for a connection between misrepresentation and

[192] *Id.* at 1057 (requiring plaintiff to plead enough facts to support plausible loss causation theory); *see also* FED. R. CIV. P. 8(a)(2) (prescribing that notice pleadings require only short and plain statement of claim).

[193] *See In re Gilead*, 536 F.3d at 1057 (insisting that loss causation emerges in proof rather than pleadings); *see also* McCabe v. Ernst & Young, LLP, 494 F.3d 418, 427 n.4 (3d Cir. 2007) (proposing that loss causation is more critical after pleadings stage); Emergent Capital Inv. Mgmt., LLC v. Stonepath Group, Inc., 343 F.3d 189, 197 (2d Cir. 2003) (same).

[194] *See* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 344-47 (2005); *In re Gilead*, 536 F.3d at 1057; *McCabe*, 494 F.3d at 427 n.4.

[195] *Compare* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation), *and id.* § 78u-4(b)(2) (requiring particularized pleading for scienter), *with id.* § 78u-4(b)(4) (requiring that plaintiff prove causation between misrepresentation and loss), *and In re Gilead*, 536 F.3d at 1057 (requiring plaintiff to plead enough facts to support plausible loss causation theory).

[196] *See, e.g.*, Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1064-65 (9th Cir. 2008) (requiring proof that market understood fraud in order to establish loss causation); *see also* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation); *id.* § 78u-4(b)(2) (requiring particularized pleading for scienter); *id.* § 78u-4(b)(4) (requiring proof that defendant's fraud caused plaintiff's loss).

[197] *See Metzler*, 540 F.3d at 1063 (requiring plaintiff to show evidence that market understood fraud).

[198] *See id.* at 1064-65 (requiring proof that market understood fraud in order to establish loss causation); *see also In re Gilead*, 536 F.3d at 1057 (recognizing that loss causation evolves after parties have access to discovery); *McCabe*, 494 F.3d at 427 n.4 (same). *But see Dura*, 544 U.S. at 341, 346 (observing that plaintiff must sufficiently plead loss causation theory to survive motion to dismiss).

loss.[199] Therefore, *Gilead* better respects Congress's choice not to subject loss causation to heightened pleading under the PSLRA.[200]

Critics argue that the Federal Rules of Civil Procedure require heightened pleading for Rule 10b-5 claims because they are fraud claims.[201] Rule 9(b) governs pleading standards for averments of fraud and demands particularized pleading for all circumstances constituting fraud.[202] Moreover, lower courts developed most of the private Rule 10b-5 elements from the tort of deceit, which is subject to Rule 9(b)'s particularized pleading.[203] Accordingly, critics argue that loss causation, as an element of a Rule 10b-5 securities fraud claim, is subject to Rule 9(b).[204]

This argument fails because although Rule 9(b) requires heightened pleadings for fraud claims, its particularity requirement does not

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[199] *See Metzler*, 540 F.3d at 1064-65 (requiring proof that market understood fraud in order to establish loss causation); *see also* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation); *id.* § 78u-4(b)(2) (requiring particularized pleading for scienter); *id.* § 78u-4(b)(4) (requiring proof of causation between fraud and loss to establish loss causation).

[200] *See In re Gilead*, 536 F.3d at 1056 (requiring sufficient basis in fact to support causation); *see also* H.R. REP. NO. 104-369, at 41 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 730, 740. *Compare* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation), *and id.* § 78u-4(b)(2) (requiring particularized pleading for scienter), *with id.* § 78u-4(b)(4) (requiring plaintiff to plead that defendant's fraud caused plaintiff's economic loss).

[201] *See* Teachers' Ret. Sys. of La. v. Hunter, 477 F.3d 162, 185-86 (4th Cir. 2007); *see also* Tricontinental Indus. v. Pricewaterhouse Coopers, 475 F.3d 824, 842-43 (7th Cir. 2007); *In re* Daou Sys., Inc., 411 F.3d 1006, 1014 (9th Cir. 2005) (requiring Rule 9 heightened pleading); *In re* White Elec. Designs Corp., 416 F. Supp. 2d 754, 763 (D. Ariz. 2006) (requiring plaintiff to plead with particularity); Cohen & Carmen, *supra* note 11, at 8.

[202] *See* FED. R. CIV. P. 9(b)*; see also* 15 U.S.C. § 78u-4(b)(1)-(2); *Teachers' Ret. Sys. of La.*, 477 F.3d at 185-86; *In re White Elecs.*, 416 F. Supp. 2d at 762-63.

[203] *See Dura*, 544 U.S. at 343 (recognizing that judicially implied private securities elements stemmed from common law deceit); Basic, Inc. v. Levinson, 485 U.S. 224, 243 (1998) (requiring heightened pleading for material misrepresentation or omissions); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 185-86, 196 (1976) (requiring heightened pleading for scienter, which is "intent to deceive, manipulate, or defraud on the defendant's part").

[204] *See* 15 U.S.C. § 78u-4(b)(4); FED. R. CIV. P. 9(b); *Teachers' Ret. Sys. of La.*, 477 F.3d at 185-86 (suggesting that "a strong case can be made that because loss causation is among the 'circumstances constituting fraud for which Rule 9(b) demands particularity, loss causation should be pleaded with particularity' "); *In re Daou*, 411 F.3d at 1014 (expressing that "[i]t is well established that claims brought under Rule 10b-5 and section 10(b) must meet the particularity requirements of Federal Rule of Civil Procedure 9(b)"); 17 C.F.R. § 240.10b-5 (2006); Cohen & Carmen, *supra* note 11, at 8.

extend to nonfraud elements of fraud claims.[205] While loss causation is an element of the Rule 10b-5 securities fraud claim, loss causation evolved as a judicial doctrine similar to proximate cause.[206] Consequently, courts developed loss causation pleading standards from the doctrine of proximate cause rather than the tort of deceit.[207] Rule 9(b)'s heightened pleading standards therefore do not extend to loss causation pleadings.[208] Moreover, neither Congress nor the Supreme Court has held that loss causation is an averment of fraud subject to the requirements of Rule 9(b).[209] If loss causation does not originate from a claim expressly listed under Rule 9(b), then *a fortiori*, heightened pleadings do not govern loss causation.[210] *Gilead*'s notice pleading standard for loss causation thus embodies Congress's intent

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[205] *See* FED. R. CIV. P. 9(b); Swierkiewicz v. Sorema, 534 U.S. 506, 512 (2002); Leatherman v. Tarrant County Narcotics Intelligence & Coordination Unit, 507 U.S. 163, 168-69 (1993); *see, e.g.*, Hunt v. Enzo Biochem, Inc., 471 F. Supp. 2d 390, 409 n.120 (S.D.N.Y. 2006) (interpreting *Dura* as permitting loss causation pleading under Rule 8); Ong v. Sears, Roebuck & Co., 459 F. Supp. 2d 729, 742-43 (N.D. Ill. 2006) (same); *In re* Enron Corp. Sec., Deriv. & ERISA Litig., 439 F. Supp. 2d 692, 714 (S.D. Tex. 2006) (same).

[206] *See In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1055, 1057 (9th Cir. 2008) (identifying basic elements of 10b-5 claims); *Teachers' Ret. Sys. of La.*, 477 F.3d at 186; *In re Daou*, 411 F.3d at 1014 (citing *Dura*, 544 U.S. at 341-43) (recognizing judge-made elements for 10b-5 claims); *supra* Part I.B; *see also Dura*, 544 U.S. at 344-47 (holding that loss causation resembles proximate cause in torts); Livid Holdings v. Salomon Smith Barney, Inc., 416 F.3d 940, 949 (9th Cir. 2005) (recognizing that loss causation resembles proximate cause); Sec. Inv. Prot. Corp. v. Vigman, 908 F.2d 1461, 1467-68 (9th Cir. 1990) (recognizing that loss causation resembles proximate cause); Weiss v. Amkor Tech., Inc., 527 F. Supp. 2d 938, 946-47 (D. Ariz. 2007) (same); Initial Public Offering Sec. Litig., 399 F. Supp. 2d 261, 265 (S.D.N.Y. 2005) (same).

[207] *Compare Dura*, 544 U.S. at 344 (recognizing that judicially implied private securities elements stemmed from common law deceit), *Basic*, 485 U.S. at 231-32 (requiring heightened pleading for material misrepresentation or omissions), *and Hochfelder*, 425 U.S. at 196 (requiring heightened pleading for scienter), *with* Tricontinental Indus. v. Pricewaterhouse Coopers, 475 F.3d 842, 843 (7th Cir. 2007) (same), *In re Daou.*, 411 F.3d at 1014 (same), *and* Caremark, Inc. v. Coram Healthcare Corp., 113 F.3d 645, 648 (7th Cir. 1997) (same).

[208] *Cf. In re Gilead*, 536 F.3d at 1057-58 (establishing loss causation pleading requirements consistent with notice pleading); *In re* Retek, Inc. Sec., No. CIV 02-4209, 2005 WL 3059566, at *1, *3 (D. Minn. Oct. 21, 2005) (same); *In re* Parlamat Sec. Litig., 375 F. Supp. 2d 278, 286 (S.D.N.Y. 2005) (applying Rule 8 notice pleading for loss causation pleading).

[209] *See* 15 U.S.C. § 78u-4(b)(4) (2006); 17 C.F.R. § 240.10b-5 (2006); *see also Dura*, 544 U.S. at 347; *Teachers' Ret. Sys. of La.*, 477 F.3d at 185-86.

[210] *See* FED. R. CIV. P. 9(b) (revealing claims subject to particularized pleading); *see also Dura*, 544 U.S. at 344 (recognizing heightened pleadings for misrepresentation and scienter but observing notice pleadings for loss causation); *Hunt*, 471 F. Supp. 2d at 409 n.120 (recognizing that Rule 8(a)(2) governs loss causation pleadings).

not to subject loss causation to heightened pleadings under the PSLRA.[211]

C. The Deterrence Function of Rule 10b-5

Congress passed the 1934 Act to maintain public confidence in the marketplace.[212] Both Congress and the Supreme Court recognize that private 10b-5 actions realize this purpose by deterring corporate actors from publishing misleading public information.[213] Because corporate fiduciaries face potential civil liability, private Rule 10b-5 actions stimulate corporate diligence and ensure that accurate information reaches the investing public.[214]

The current financial crisis intensifies the additional hurdle created by requiring proof of loss causation in the pleading stage.[215] Although companies nationwide are experiencing financial adversity, the economic meltdown should not grant corporate officers a free pass to commit fraud at the expense of injured investors.[216] Even though investors may not recover the depreciated value of their investment due to the financial crises, they should still recover the amount of value depreciation caused by fraud.[217] *Gilead*'s notice pleading and broad proximate cause requirements permit meritorious claims to

[211] *Compare* 15 U.S.C. § 78u-4(b)(1) (requiring particularized pleading for misrepresentation), *and id.* § 78u-4(b)(2) (requiring particularized pleading for scienter), *with id.* § 78u-4(b)(4) (requiring that plaintiff prove causation between misrepresentation and loss), *and In re Gilead*, 536 F.3d at 1057 (requiring plaintiff to plead enough facts to support plausible loss causation theory).

[212] S. REP. NO. 104-98, at 4 (1995); H.R. REP. NO. 104-369, at 3 (1995) (Conf. Rep.), *reprinted in* 1995 U.S.C.C.A.N. 679, 682; *see also Dura*, 544 U.S. at 345 (stating that private securities actions assist in deterring corporate fraud); United States v. O'Hagan, 521 U.S. 642, 644 (1997); Burch, *supra* note 50, at 380-81. *See generally* Randall v. Loftsgaarden, 478 U.S. 647, 664 (1986) (holding that private securities actions maintain confidence in markets by deterring fraud).

[213] S. REP. NO. 104-98, at 4, *reprinted in* 1995 U.S.C.C.A.N. 679, 683; *see also Dura*, 544 U.S. at 345 (noting that securities statutes served to maintain market confidence and deter fraud); *Loftsgaarden*, 478 U.S. at 664 (holding that private securities actions maintain market confidence by deterring fraud); Joseph W. Bishop, Jr., *New Problems in Indemnifying and Insuring Directors: Protection Against Liability Under the Federal Securities Laws*, 1972 DUKE L.J. 1153, 1162. *See generally* Burch, *supra* note 50, at 380-81 (arguing that private class actions promote deterrence of corporate fraud).

[214] S. REP. NO. 104-98, at 4; H.R. REP. NO. 104-369, at 3 (Conf. Rep.); *see also Dura*, 544 U.S. at 344; *O'Hagan*, 521 U.S. at 644; *Loftsgaarden*, 478 U.S. at 664; Burch, *supra* note 50, at 380-81.

[215] *See* sources cited *supra* note 10.

[216] *See* sources cited *supra* note 10 and accompanying text.

[217] *See* sources cited *supra* note 10 and accompanying text.

move forward by requiring the plaintiff to plead a plausible causation theory.[218] Thus, *Gilead*'s standard better effectuates Rule 10b-5's deterrence function by reducing Rule 12(b)(6) dismissals of meritorious claims.[219]

Metzler's heightened pleading standard undermines Rule 10b-5's deterrence function by raising the plaintiff's loss causation pleading burden, which may leave corporate wrongdoers unpunished.[220] By requiring proof that the market understood the fraud, *Metzler* requires proof of information that is unavailable to plaintiffs during the pleading stage.[221] *Metzler*'s strict loss causation requirements create unreasonable hurdles for Rule 10b-5 plaintiffs, and may lead to premature dismissal of meritorious claims.[222] Moreover, *Metzler* enables corporate officers to avoid liability by simply releasing its corrective disclosure with other bad news so that plaintiffs cannot separate the loss associated with the actual correction.[223] As a result,

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[218] *See In re* Gilead Scis. Sec. Litig., 536 F.3d 1049, 1057 (9th Cir. 2008); *see also* 15 U.S.C. § 78u-4(b)(4) (2006) (requiring proof of causation between fraud and loss); *Dura*, 544 U.S. at 347 (stating that proximate cause serves to avoid harm of increased frivolous lawsuits); McCabe v. Ernst & Young, LLP, 494 F.3d 418, 427 n.4 (3d Cir. 2007) (same); Emergent Capital Inv. Mgmt., LLC v. Stonepath Group, Inc., 343 F.3d 189, 197 (2d Cir. 2003) (same).

[219] *See* S. REP. NO. 104-98, at 4 (1995); H.R. REP. NO. 104-369, at 3 (1995) (Conf. Rep.); *see also Dura*, 544 U.S. at 345 (stating that private securities actions assist in deterring corporate fraud); *O'Hagan*, 521 U.S. at 644-45; Burch, *supra* note 50, at 380-81. *See generally Loftsgaarden*, 478 U.S. at 664 (observing that private securities actions maintain confidence in markets by deterring fraud); *supra* Part I.A (discussing Congress's intent behind passing 1934 Act); *supra* Part III.B (discussing PSLRA's loss causation pleading requirements); *supra* Part III.C (discussing Rule 10b-5's deterrence function).

[220] *See* S. REP. NO. 104-98, at 4; *see also Dura*, 544 U.S. at 345; *O'Hagan*, 521 U.S. at 644-45; *supra* Part I.A.

[221] *Compare* Metzler Inv. GMBH v. Corinthian Colls., 540 F.3d 1049, 1064-65 (9th Cir. 2008) (requiring proof that market understood fraud in order to establish loss causation), *In re Gilead*, 536 F.3d at 1057 (recognizing that loss causation evolves after parties have access to discovery), *and McCabe*, 494 F.3d at 427 n.4 (same), *with Dura*, 544 U.S. at 346 (observing that plaintiff must sufficiently plead loss causation theory to survive motion to dismiss).

[222] *See Metzler*, 540 F.3d at 1064-65 (requiring proof that market understood fraud in order to establish loss causation); *see also Dura*, 544 U.S. at 345 (stating that private securities actions assist in deterring corporate fraud); *O'Hagan*, 521 U.S. at 644-45; Burch, *supra* note 50, at 380-81.

[223] *See Metzler*, 540 F.3d at 1064-65; COX ET AL., *supra* note 41, at 724. *See generally* Oscar Private Equity Invs. v. Allegiance, 487 F.3d 261 (5th Cir. 2007) (denying class certification because plaintiffs failed to separate corrective disclosure of fraud from bundle of bad news).

Metzler's standard may interfere with Rule 10b-5's role in instilling confidence in U.S. financial markets.[224]

CONCLUSION

The Ninth Circuit should resolve this intra-circuit loss causation conflict by adopting *Gilead*'s approach.[225] *Gilead*'s broad construction of loss causation complies with *Dura*, reflects congressional intent behind the PSLRA, and effectuates Rule 10b-5's deterrence function.[226] Conversely, *Metzler*'s strict requirements run contrary to both *Dura* and the PSLRA, and may interfere with Rule 10b-5's deterrence function and Congress's intent to restore confidence in the U.S. public markets.[227] Therefore, the Ninth Circuit should approve *Gilead* as the loss causation standard for Rule 10b-5 claims.[228] Furthermore, if the Supreme Court revisits *Dura*'s loss causation holding, it should articulate definite requirements that embrace *Gilead*'s broad formulation of loss causation pleadings.[229]

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[224] *See* S. REP. NO. 104-98, at 4 (recognizing that purpose of securities laws is to maintain confidence in U.S. public markets); H.R. REP. NO. 104-369, at 3 (Conf. Rep.) (same); *see also Dura*, 544 U.S. at 345 (stating that private securities actions assist in deterring corporate fraud); *O'Hagan*, 521 U.S. at 644; Burch, *supra* note 50, at 380-81 (stating that private securities fraud class action suits are "in accord with Congress's goal of ensuring market integrity"). *See generally Loftsgaarden*, 478 U.S. at 664 (observing that private securities actions maintain confidence in markets by deterring fraud).

[225] *See supra* Part III (discussing how *Gilead* better effectuates Congress's intent behind PSLRA and comports with Supreme Court's decision in *Dura*).

[226] *See* S. REP. NO. 104-98, at 4; H.R. REP. NO. 104-369, at 3 (Conf. Rep.); *see also Dura*, 544 U.S. at 344 (stating that private securities actions assist in deterring corporate fraud); *O'Hagan*, 521 U.S. at 644-45; Burch, *supra* note 50, at 380-81. *See generally Loftsgaarden*, 478 U.S. at 664 (observing that private securities actions maintain confidence in markets by deterring fraud); *supra* Part I.A (discussing Congress's intent behind passing 1934 Act); *supra* Part III.B (discussing PSLRA's loss causation pleading requirements); *supra* Part III.C (discussing Rule 10b-5's deterrence function).

[227] S. REP. NO. 104-98, at 4; H.R. REP. NO. 104-369, at 41 (Conf. Rep.); *see also* 15 U.S.C. § 78u-4(b)(4) (2006); *Dura*, 544 U.S. at 341, 344-46 (recognizing that loss causation resembles proximate cause and observing that loss causation pleading requirements should not create heightened pleading burden for plaintiffs); *O'Hagan*, 521 U.S. at 644-45; *Loftsgaarden*, 478 U.S. at 664; Burch, *supra* note 50, at 380-81. *See generally supra* Part I.A (discussing Congress's intent behind passing 1934 Act); *supra* Part III.B (discussing PSLRA's loss causation pleading requirements); *supra* Part III.C (discussing Rule 10b-5's deterrence function).

[228] *See supra* Part III (discussing how *Gilead* better effectuates Congress's intent behind PSLRA and comports with Supreme Court's decision in *Dura*).

[229] *See Dura*, 544 U.S. at 344 (requiring Broudo to prove that fraud proximately

caused his economic loss); *In re* Gilead Scis. Secs. Litig., 536 F.3d 1049, 1057-58 (9th Cir. 2008) (holding that class proved proximate cause by linking corrective disclosure and loss to fraud); *see also supra* Part II.A.