

The Expert's Corner

SUPREME COURT ROUND-UP

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During the Term that just ended, the Supreme Court did not decide any cases involving class action attorney fees, *per se*, but it did decide a number of cases about *class actions* and some concerning *attorney fees*. The three most significant cases are likely to cut back on class action practice and narrow the ability for plaintiff's counsel to secure fees in fee shifting cases.

Class Action Cases

The three most important class action cases arose in the context of pleading. While they therefore involve a mundane aspect of civil practice, their importance is far more than technical.

In *Tellabs Inc., v. Makor Issues & Rights, Ltd.*, the Court interpreted a portion of the Private Securities Litigation Reform Act of 1995 (PSLRA) that requires that plaintiffs "state with particularity facts giving rise to a *strong inference* that the defendant acted with the required state of mind."¹ In an 8-1 decision,² Justice Ginsburg, writing for the majority, stated that a key aspect of deciding whether an inference of scienter is "strong" is that it must be compared to other inferences that can be drawn from the available facts: "A complaint will survive," the Court held, "only if a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged." *Tellabs*, slip op. at 12-13.

Securities fraud class actions filings have declined nearly 50% over the past two years – down to 118 in 2006 from 182 in 2005 and 235 in 2004.³ *Tellabs's* new uniform national standard, while not as strong as that urged by some business groups, is nonetheless likely to make securities class actions

1 15 U.S.C. §78u-4(b)(2) (emphasis supplied). The required state of mind is one of scienter, or the intention to "deceive, manipulate, or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 194, n.12 (1976).

2 Only Justice Stevens dissented from the outcome.

3 The data are available here: <http://securities.stanford.edu/companies.html>.

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more difficult to maintain in many circuits⁴ and hence perpetuate this decline in securities filings.

In *Bell Atlantic Corp. v. Twombly*, an antitrust class action, the Court narrowed its own prior interpretation of the more general pleading standard contained in the Federal Rules of Civil Procedure. Rule 8(a) requires only a "short and plain statement of the claim showing that the pleader is entitled to relief." At least for the past fifty years, Rule 8 has been interpreted to do little more than "give the defendant fair notice of what the . . . claim is and the grounds upon which its rests." *Conley v. Gibson*, 355 U.S. 41, 47 (1957). The laxness of Rule 8's pleading standard is famously reflected in *Conley's* statement that "a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Id.* at 45-46.

In *Twombly*, Justice Souter, writing for seven members of the Court,⁵ explicitly rejected this portion of *Conley*, writing that "this famous observation has earned its retirement." *Twombly*, slip op. at 16. In its place, the Court repeated familiar formulations such as: "a plaintiff's obligation to provide the grounds of his entitlement to relief requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." *Id.* at 8 (citation and internal punctuation omitted). Rather, "[f]actual allegations must be enough to raise a right to relief above the speculative level." *Id.* As applied to the antitrust claim at issue, the Court held that "stating such a claim requires a complaint with enough factual matter (taken as true) to suggest that an agreement [on restraint of trade] was made," *id.* at 9, referring to this as asking for "*plausible* grounds to infer an agreement," "enough fact to raise a reasonable expectation that discovery will reveal evidence of illegal agreement." *Id.* (emphasis supplied).

If there were any doubt about what this "plausibility" standard meant, the Court first squelched that doubt by reversing the Second Circuit and dismissing *Twombly's* complaint. It thus appeared fair to presume that *Twombly* signals to lower courts that they should take a closer look at the pleading stage and that the decision will likely yield an increase in early, pleading-based, dismissals.

4 In *Tellabs*, for example, the Seventh Circuit had declined to consider competing inferences, expressing concern that such standards "could potentially infringe upon plaintiffs' Seventh Amendment rights." *Makor Issues & Rights, Ltd. v. Tellabs, Inc.*, 437 F.3d 588, 602 (7th Cir. 2006).

5 Justices Stevens and Ginsburg dissented.

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