Pleading a Loss Cause: Resolving the Pleading Standard for the Element of Loss Causation in a Private Securities Fraud Claim and a Plaintiff's Heavy Burden Pleading it Under IQBAL

Jason N. Haycock

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RESOLVING THE PLEADING STANDARD
FOR THE ELEMENT OF LOSS CAUSATION IN
A PRIVATE SECURITIES FRAUD CLAIM AND
A PLAINTIFF’S HEAVY BURDEN PLEADING
IT UNDER IQBAL

JASON N. HAYCOCK*  

TABLE OF CONTENTS

Introduction ................................................................................................................. 175
I. Background ............................................................................................................. 181
   A. An Introduction to the Element of Loss Causation and the
      General Standards of Pleading ...................................................................... 181
      1. A private securities fraud claim and the element of loss
         causation ................................................................................................. 181
      2. Pleading requirements under the Private Securities
         Litigation Reform Act ............................................................................ 183
      3. Rule 8(a)(2) .......................................................................................... 184
      4. Rule 9(b) ............................................................................................. 187
   B. Judicial Application of Pleading Standards to the Element
      of Loss Causation ....................................................................................... 189
      1. The Supreme Court’s implicit adoption of Rule 8(a)(2).................. 190
      2. The Rule 8(a)(2) approach .................................................................... 191

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American University, Washington College of Law; B.A., Political Science, 2008, University of California, Davis. Foremost, I would like to thank my family and friends, whose love and encouragement inspires my every word and without whom I would surely be a lesser person—I love you all, and I thank you for your continued support. Next, I would like to thank Professor John (Bernie) Corr who encouraged me that I just might have an argument, and my editor, Lisa Kohl, who helped walk me through this process. I would also like to thank the authors cited in this Comment for providing some of the insight that I drew upon. Finally, I would like to thank Bethany Dickman, Kara Karlson, and Ian Spear, who contributed so much of their time, patience, and intellect; and thank you to the entire staff of the American University Law Review whose effort and dedication made this Comment better than I could have made it on my own.
a. Explicit adoption of Rule 8(a)(2) in light of Twombly and Dura: The Fifth Circuit approach ........192
b. Explicit adoption of Rule 8(a)(2) in light of Iqbal: The Eighth Circuit approach ..........................193
3. The Rule 9(b) approach .................................................................194
   a. Explicit adoption of Rule 9(b): The Fourth Circuit approach .................................................194
   b. Implicit adoption of Rule 9(b): The Ninth Circuit approach ................................................195

II. Analysis ...............................................................................................................196
   A. The Proper Pleading Standard for Loss Causation is Rule 8(a)(2) as Demonstrated by an Analysis of “Causation” Generally and Within the Tort Law Context, a Textual Reading of the Rules, Supreme Court Precedent, and an Understanding of the Traditional Common Law Elements of Fraud .........................................................................................................................196
      1. Applying an analysis of causation generally and of proximate cause to a textual reading of Rule 9(b) ........197
      2. Supreme Court precedent and the implicit adoption of Rule 8(a)(2) .................................................199
      3. Common law elements of fraud and the statutorily created element of loss causation ..................200
   B. Pleading Loss Causation Under Iqbal’s Formulation of Rule 8(a)(2) Will Create a Higher Standard for a Plaintiff to Meet than Pleading Under Rule 9(b) Because Rule 8(a)(2) Requires that a Private Securities Fraud Claim Must Meet Plausibility as Well as Particularity ..........................................................201
      1. The first prong of the Iqbal analysis is functionally equivalent to Rule 9(b) ’s particularity requirement ..........................202
      2. Pleading loss causation under the second prong of the Iqbal analysis is particularly difficult due to the complex nature of securities fraud claims ................................................206
   C. As a Policy Matter, Pleading Loss Causation under Iqbal’s Construction of Rule 8(a)(2), Combined with the Strict Pleading Requirements for the other Elements of a Private Securities Fraud Claim, Suggests that a Plaintiff Will Face a Substantial Barrier in Accessing Judicial Redress .................................................209

Conclusion .....................................................................................................................210
The global community just experienced “the second-worst financial crisis in the history of the world,” and the worst economic collapse in seventy years. Individuals lost homes, jobs, life savings, retirement funds, children’s college tuition and more. Not all of these losses were necessary, and victims of various acts of fraud stemming from the financial crisis are looking for someone to make them whole.

One of the most-discussed causes of the financial crisis was the effect of mortgage-lending practices on the securities market. The media has focused much attention on the failure of regulators to prevent “predatory lending” in the mortgage market and the victims that succumbed to those predatory practices, but the general regulatory failure has had more far-reaching consequences. The impact of the predatory lending was not confined to the mortgage markets. Many of its effects found its way into the securities markets in the form of mortgage-backed securities.

Mortgage-backed securities are financial instruments that are underwritten by, and derive their value from, rights to payment streams on


2. See generally Senate Judiciary Committee Hearing on Mortgage Fraud, Securities Fraud, and the Financial Meltdown: Prosecuting Those Responsible; Hearing before the S. Comm. on the Judiciary, 111th Cong. (2009) [hereinafter Fraud Hearings] (statement of Sen. Edward Kaufman, S. Comm. on the Judiciary) (discussing the need to focus on the role of financial fraud and how it contributed to the financial crisis in order to hold accountable those who perpetrated the fraud and prevent future economic collapse).

3. See id. (arguing that the failure of companies to disclose the proper value of mortgage-backed assets and the possibility that companies made false or misleading statements regarding the value of those assets significantly contributed to the financial crisis).


5. Mortgage-backed securities are not a critical part of this Comment, and understanding their intricacies is largely unimportant here. The impact of these financial instruments on the securities markets does, however, provide an illustration as to why private securities litigation is currently relevant, so a cursory understanding is helpful. Mortgage-backed securities are a type of debt obligation financial instrument that represent an interest in a mortgage payment stream. See Mortgage-Backed Securities, U.S. SECURITIES & EXCHANGE COMM’N, http://www.sec.gov/answers/mortgagesecurities.htm (last modified July 23, 2010). The right to individual payment streams received from housing mortgages are purchased by some entity (generally a bank), and then “bundled” or “pooled” into one large financial instrument and used as a form of collateral to create securitized interests in the collective payments streams (i.e., they are securitized into “mortgage-backed securities”). See id. The mortgage-backed securities are then sold as a form of capitalization and investment just as any other security. See id.
mortgages. These instruments can become “toxic” where the mortgages that underwrite the security are high-risk in that the mortgagors are at risk to default or otherwise disrupt the payment stream on the mortgage. The toxicity becomes problematic when the securities are held as assets on companies’ balance sheets where the value of these assets is either uncertain or misrepresented.

Like any other security, companies regularly purchase and sell mortgage-backed securities as a form of investment, profit, and capitalization. However, because the value of these securities is ultimately tied to the mortgage payments that underwrite them, the potential for fraud arises if a company is not forthright about the underlying source of the security’s value. The recent high-profile indictment of the largest investment bank in the United States, Goldman Sachs, illustrates this point. The Securities and Exchange Commission (SEC) alleges that Goldman Sachs intentionally created a mortgage-backed financial instrument comprised of high-risk mortgages with the purpose of inducing private investors to purchase securities in this instrument while Goldman Sachs shorted the instrument to make money on the collapse of the housing market. Under such an arrangement, investors lost money as the crisis unfolded and Goldman Sachs made money by betting that the instrument’s value would decline.

Mortgage-backed securities are not the only origin of securities fraud, and they are not the focus of discussion here. They do, however, represent a considerable source of potential fraud given recent economic events, and they are relevant to this Comment only to the extent that they illustrate the

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6. Id.
7. See Fraud Hearings, supra note 2 (statement of Robert Khuzami, Director, Division of Enforcement, United States Securities and Exchange Commission) (noting that some of the assets on the books of public companies were underwritten by mortgages).
8. Id.
9. See id. (reporting the possible failure of companies to disclose the proper value of mortgage-backed assets and the possibility that companies made false or misleading statements regarding the value of those assets).
12. See id. (reporting that the focus of the SEC’s case is an investment vehicle, Abacus 2007-AC1, created by Goldman Sachs so the bank and some of its clients could bet against the housing market). As a note, since the writing of this Comment, Goldman Sachs has settled its case with the SEC for 550 million dollars. See Sewell Chan & Louise Story, Goldman Pays $550 Million to Settle Fraud Case, N.Y. TIMES, Jul. 16, 2010, at A1.
immediate saliency of private securities litigation. Indeed, in addition to the indictment of Goldman Sachs, the SEC has started to bring a number of actions specifically implicating mortgage-backed securities as a source of securities fraud on the investing public. While the SEC intervenes to protect investors in a general sense by correcting market violations, it does not facilitate individual monetary recovery. Individual investors who sustain financial losses resulting from securities fraud must bring claims in their individual, private capacities. The road to financial recovery begins with properly pleading the elements of the underlying securities fraud claim. This Comment will focus on the pleading standard for one of those elements: the element of “loss causation.”

In 1995, Congress passed the Private Securities Litigation Reform Act (the PSLRA), a statutory scheme that heightened the pleading standard for certain elements of a private securities fraud claim to require “particularity”

13. See Fraud Hearings, supra note 2 (statement of Robert Khuzami, Director, Division of Enforcement, United States Securities and Exchange Commission) (noting that “a central issue” of recent SEC enforcement cases is whether investors received accurate disclosures concerning the deteriorating business conditions, increased risks, and downward pressure on asset values).

14. See, e.g., Complaint at 1–2, SEC v. Morrice, No. SACV09-01426 (C.D. Cal. Dec. 7, 2009) (alleging that the officers of New Century Financial, Corp., one of the largest subprime mortgage lenders in the United States prior to the financial crisis, made material false and misleading statements regarding the true financial health of the company); Complaint at 3–4, SEC v. Mozilo, No. CV 09-03994 (C.D. Cal. June 4, 2009) (charging that officers of Countrywide Financial deliberately misled investors about the significant credit risks the company was taking in its efforts to expand its market share); Complaint at 2–3, SEC v. Strauss, No. 09-CIV-4150 (S.D.N.Y. Apr. 28, 2009) (accusing the officers of American Mortgage Investment Corp. of converting loan losses in the tens of millions of dollars into fictional profits).


16. See discussion infra Part I.A.1 (explaining that the most common form of a securities fraud claim is a Rule 10b-5 claim under § 10(b) of the Exchange Act). This Comment will assume that theory of action when discussing a “securities fraud claim” generically.

17. See discussion infra Part I.A.1 (discussing the element of “loss causation”).

18. See Securities Exchange Act of 1934 § 21D(b)(4) (requiring a plaintiff to plead the element of loss causation in a private securities claim); Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 346 (2005) (explaining that Congress intended to permit private securities actions only where plaintiffs adequately show the element of causation); see also infra Part I.A.1 (discussing securities fraud claims generally and the element of loss causation specifically).
at the pleadings stage. Additionally, the PSLRA formally created the element of loss causation as a requirement of a private securities fraud claim. The PSLRA did not, however, specify the pleading standard under which loss causation would be pled. Absent statutory guidance, the Federal Rules of Civil Procedure govern the proper pleading standard. Due to the fact that loss causation is an element of a fraud claim, the federal circuits have split regarding whether it should be pled under the fraud pleading provisions of Federal Rule of Civil Procedure 9(b) (Rule 9(b)) or the general pleading provisions of Federal Rule of Civil Procedure 8(a)(2) (Rule 8(a)(2)). This split creates two issues for resolution.

The first issue is the one just mentioned—it is still unclear which pleading standard applies to the element of loss causation. Thus, since the PSLRA does not provide the proper pleading standard for the element of loss causation, the first issue requires resolution of which pleading standard governs pleading loss causation—the general pleading requirements under Rule 8(a)(2), or the particularized requirements under Rule 9(b) governing fraud claims.

As a result of this Comment’s conclusion on the first issue that Rule 8(a)(2) should govern private securities fraud claims, the second issue arises due to the Supreme Court’s reinterpretation of that rule, requiring a claimant to state a “plausible” claim to relief at the pleading stage. The plausibility standard announced in Bell Atlantic Corp. v. Twombly and refined in Ashcroft v. Iqbal looks similar to the particularity requirement under Rule 9(b) despite the Court’s insistence that plausibility pleading is

20. Id. § 105.
21. Id.
23. Compare Lorand v. US Unwired, Inc., 565 F.3d 228, 255 (5th Cir. 2009) (adopting and applying Dura and Twombly’s reading of Rule 8(a)(2) to the element of loss causation), with In re Mut. Funds Inv. Litig., 566 F.3d 111, 120 (4th Cir. 2009) (clarifying that in the Fourth Circuit, Rule 9(b) controls all averments of fraud, and that Rule 9(b) is the proper pleading standard for pleading loss causation).
25. 550 U.S. 544, 556 (2007) (stating that a complaint must show certain factual matter to give rise to the plausibility of entitlement to relief).
not a heightened standard. As a matter of logic, there may be substantial interplay between what is particular and what is plausible. Further, pleading plausibility may actually be a more difficult standard to meet than pleading factual particularity in certain complex pleading contexts such as a securities fraud claim. This is due to the fact that defining the “cause” of a given event often inherently requires a certain level of particularity, and this requirement is augmented by the fact-sensitive nature of a private securities fraud claim. Adding a requirement of plausibility to this factually sensitive context, a plaintiff must not only identify which was the cause of his injury through pleading its factual particularities, a plaintiff must also identify a theory of causation that is plausible. In effect, meeting a standard of plausibility will entail pleading factual particularity. Accordingly, the second issue that this Comment will address is the operation of plausibility pleading in factually complex contexts such as private securities litigation.

A brief explanation will help illuminate this second issue. The basic scheme of loss causation requires a plaintiff to identify the causal chain between the defendant’s act of fraud (a material misstatement or omission) and the plaintiff’s economic injury, which is usually a financial loss in the form of a decline in share price. The difficulty in identifying the correct causal chain derives from the fact that there are a myriad of potential causes for a decline in share price. Even if the defendant perpetrated a fraud, it does not necessarily follow that the fraudulent act, and not some other act (e.g. poor company performance, natural disaster, unfavorable economic conditions generally) caused the decline in share price.

27. See A. Benjamin Spencer, Plausibility Pleading, 49 B.C. L. Rev. 431, 473–75 (2008) (suggesting that it is difficult to distinguish any meaningful difference between “particularity” under Rule 9(b) and “plausibility” under Rule 8(a)(2)).
28. Id.
29. Cf. id. at 475-76 (stating that plausibility under Twombly “is the very definition of particularized pleading”). While it does not necessarily follow from this statement that plausibility under Iqbal is more scrutinizing than particularity pleading under Rule 9(b), it does at least support such a proposition in certain contexts and this proposition will be further supported later in the text. See discussion infra Part II.B.
30. See Jill E. Fisch, Cause for Concern: Causation and Federal Securities Fraud, 94 IOWA L. REV. 811, 821 (2009) (explaining that a loss causation analysis is particularly difficult in the securities fraud context because of the many factors that can affect the value of a securities investment).
31. See Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 343 (2005) (noting that when a purchaser resells shares at a lower price after an alleged misrepresentation by an issuer, the lower price is not necessarily the result of the alleged misrepresentation, but often of changed economic conditions, and “[o]ther things being equal, the longer the time between purchase and sale, . . . the more likely that other factors caused the loss.”).
32. See infra Part II.B.
33. See infra text accompanying notes 51–54.
34. Fisch, supra note 30, at 821.
plaintiff’s subsequent economic injury.\textsuperscript{35} Therefore, the plaintiff must not only sufficiently identify a particular causal chain of events, but that causal chain must also be a plausible explanation for the plaintiff’s loss.

In this situation, it may be that the “general,” plausibility pleading requirements under Rule 8(a)(2) would actually be stricter than a simple particularity requirement under Rule 9(b).\textsuperscript{36} This appears likely in complex claims such as securities fraud where there tends to be a significant amount of factual information surrounding a claim.\textsuperscript{37} It is therefore important to understand not only which rule governs the pleading standard for loss causation, but also the practical effect of the governing rule on a plaintiff’s ability to advance a successful claim.

Part I will provide the background information regarding the pleading standards under Rule 8(a)(2) and Rule 9(b), pleading within the context of a securities fraud claim specifically, and the various circuit courts’ application of the pleading standards to the specific element of loss causation. Part II will analyze and address the proper pleading standard for loss causation as well as the practical effect of that pleading standard on properly pleading loss causation. This Comment will conclude by taking notice of the broader policy implications of these arguments within the general private securities litigation context.

\textsuperscript{35} See \textit{Dura Pharm., Inc.}, 544 U.S. at 343–46 (holding that a complaint in a securities fraud action must prove more than an inflated purchase price on the date of purchase to establish that defendant’s misrepresentation proximately caused economic loss); Law v. Medco Research, Inc., 113 F.3d 781, 786–87 (7th Cir. 1997) (dismissing a securities fraud claim for failure to show loss causation after finding that defendant’s share price moved in tandem with competitors’ share price, so it was sufficient to conclude that market forces created plaintiff’s loss).

\textsuperscript{36} There are some interesting implications following this assertion that touch on broader issues concerning the relationship between the plausibility pleading standard under Rule 8(a)(2) and the particularity pleading standard under Rule 9(b). Plausibility can be a more difficult standard to meet than particularity in certain contexts. As discussed in Part II.B, something can be sufficiently particular without crossing the line into the realm of plausibility. It is possible to imagine that a plaintiff could bring a claim that is highly particular and detailed in its factual recitation. Regardless of how particular that plaintiff’s claim is (even if possible), however, pleading factual particularity does not ensure that the claim will be deemed plausible. This concern has implications broader than the scope of this Comment will allow, but it is important to examine the plausibility-particularity interplay in all complex contexts where, as here, Rule 8(a)(2) and Rule 9(b) run up against each other.

\textsuperscript{37} See \textit{Thomas Lee Hazen, Law of Securities Regulation} § 12:11[3], at 167 (6th ed. 2010) (explaining that pleading loss causation can be a highly factual matter and noting that “failure to specifically allege facts showing loss causation will result in dismissal”) (emphasis added); Fisch, supra note 30, at 821 (noting that stock prices can be impacted by many nonfraudulent events, which the court must ascertain); see also Patricia W. Hatamyar, \textit{The Tao of Pleadings: Do Twombly and Iqbal Matter Empirically?}, 59 A.U. L. REV. 553, 605–09 (2010) (providing empirical data supporting the proposition that more complex claims are more likely to be dismissed under an Iqbal analysis than under Twombly or Conley).
I. BACKGROUND

There are essentially three pleadings standards at issue in the private securities fraud context: (1) the heightened pleading standards under the Private Securities Litigation Reform Act; (2) the general pleading standards under Rule 8(a)(2), and; (3) the particularity pleading standards under Rule 9(b). Part A will address each of these standards as well as begin by introducing a more comprehensive definition of the element of loss causation. Part B will survey the case law to examine how the Supreme Court and the federal circuits have handled these various pleading standards with respect to the element of loss causation.

A. An Introduction to the Element of Loss Causation and the General Standards of Pleading

The three aforementioned pleading standards converge in the context of pleading loss causation. Thus, to persuasively argue which standard applies and to understand the practical effects flowing therefrom, each pleading standard must be parsed and explored, beginning with the standards under the PSLRA and moving to Rule 8(a)(2) and Rule 9(b), respectively. However, to provide context, it is first necessary to understand a private securities fraud claim broadly and the element of loss causation specifically.

1. A private securities fraud claim and the element of loss causation

Section 10(b) of the Securities Exchange Act of 1934 (Exchange Act) prohibits fraud in connection with the purchase or sale of any security. The statutory language itself, however, does not create a cause of action. Rather, it sets up the general prohibition on securities fraud and then delegates the authority to the Securities and Exchange Commission to promulgate rules of enforcement.

The SEC subsequently promulgated Rule 10b-5 to give practical effect to section 10(b) of the Exchange Act. Rule 10b-5 essentially prohibits making any untrue statement of a material fact, or the omission thereof, and the engagement in any fraudulent act in connection with the purchase or sale of any security.

39. Id.
40. Id.
41. See id. (proscribing activity “in contravention of such rules and regulations as the [Securities and Exchange] Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors”).
42. 17 C.F.R. § 240.10b-5 (2004) (interpreting § 10(b) of the Exchange Act to set up an enforceable rule of liability for a violation thereof).
nearly every statement that a company makes concerning its operations subject to certain designated exceptions, or “safe-harbors.”

Rule 10b-5 originally created a cause of action only for the SEC. However, the courts have since interpreted the rule as implying a private right of action as well. In bringing a private claim, however, the courts also require that a complaint include the common law elements of fraud in addition to the two statutory elements created under the PSLRA: economic loss and loss causation.

Loss causation is defined in section 21D(b)(4) of the Exchange Act and provides that for any private action, a plaintiff must prove that the act complained of caused the loss for which the plaintiff seeks to recover damages. Analytically, loss causation is often best understood as analogous to the tort element of “proximate cause.” At its simplest, it is the causal link between the defendant’s fraudulent act and the plaintiff’s economic injury.

Like proximate cause, loss causation adopts the “legal cause” (as opposed to the “but for” cause) approach to attaching liability. That is, a plaintiff must show that his injury is directly attributable to the defendant’s fraudulent act, but not that the defendant’s act was the “but for” cause of plaintiff’s injury. It should be noted, however, that loss causation generally receives greater scrutiny in assessing the viability of

43. Id. (“[I]n connection with the purchase or sale of any security”).

44. “Safe harbor” refers to exceptions created by statute or rule that allow certain statements to be protected against liability under Rule 10b-5. See, e.g., Securities Exchange Act of 1934, § 21E (providing a safe harbor for “forward-looking” statements that attempt to forecast future business conditions).


46. The Supreme Court has never squarely held that a private right of action lies for a Rule 10b-5 claim. There is, however, well-recognized support for that proposition. See Herman & MacLean v. Huddleston, 459 U.S. 375, 380 (1983) (observing that for forty years, the lower courts have recognized implied private rights of action under section 10(b) of the Securities Exchange Act of 1934 and its counterpart, Rule 10b-5, and stating that “[t]he existence of this implied remedy is simply beyond peradventure”).

47. See, e.g., Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 341 (2005) (outlining the requirements for a securities fraud claim as: (1) a material misrepresentation, or omission, of fact; (2) scienter, i.e., a wrongful state of mind; (3) in connection with the purchase or sale of a security; (4) reliance (sometimes referred to as “transaction causation”); (5) economic loss; and (6) loss causation, i.e. a causal connection between the material misrepresentation and the loss).

48. See Securities Exchange Act of 1934 § 21D(b)(4) (defining the element of “loss causation” and requiring a private plaintiff to plead it in his claim of securities fraud).

49. See, e.g., McAdams v. McCord, 584 F.3d 1111, 1114 (8th Cir. 2009) (explaining that, similar to tort law, a securities fraud plaintiff “must show that the loss was foreseeable and that the loss was caused by the materialization of the concealed risk”).

50. Id.

51. See HAZEN, supra note 37, § 12:11[1], at 152 (explaining that causation in securities law involves a similar analysis as causation under the common law for tort and contracts cases).

52. See id. § 12:11[3], at 159.
securities fraud claims than does the element of proximate cause in general fraud claims. Additionally, although the focus of this Comment is on the procedural aspects of loss causation, it is helpful to understand that as a substantive matter, loss causation is most commonly shown where there is a price movement in shares that sufficiently corresponds to the fraudulent misstatement or omission.

2. **Pleading requirements under the Private Securities Litigation Reform Act**

In 1995, Congress passed the PSLRA to raise the pleading standards in private securities fraud litigation in an effort to curb abusive litigation. The heightened pleading standards resemble the particularity standards of Rule 9(b). Section 21D(b)(1) of the Exchange Act essentially requires that for any private action alleging a misstatement or omission of material fact, the plaintiff must plead with particularity.

The revised pleading standards under the PSLRA do not, however, discuss their applicability to the other elements of a 10b-5 claim beyond their applicability to the element of a misstatement or omission of material fact. With respect to the element of loss causation, section 21D(b)(4) of the Exchange Act states only that a plaintiff must prove that the act or omission was the cause of the loss; it does not state the pleading standard that the plaintiff must meet in attempting to show that causal connection at the pleading stage. Consistent with the Exchange Act’s lack of specific application, the Supreme Court has given strong indication (and the federal

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53. *See id.* (contrasting the level of scrutiny in the analysis of loss causation and proximate causation and noting that loss causation in securities law imposes stricter requirements than proximate causation would in general fraud claims).

54. *Id.* § 12:11[1], at 150–52.


56. *Compare* Fed. R. Civ. P. 9(b) (“[A] party must state with particularity the circumstances constituting fraud or mistake.”), *with Securities Exchange Act of 1934 § 21D(b)(1), 15 U.S.C. 78u-4 (2006) (“[T]he complaint shall specify each statement alleged to have been misleading . . . and, if [the] allegation . . . is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed.”) (emphasis added).

57. Thus, the requirements do not apply to the Securities and Exchange Commission.


59. *See id.* (applying the particularity standard only to statements alleged to be misleading).

60. *See id.* § 21D(b)(4) (stating only that the plaintiff has “the burden of proving” the requisite causal connection, but omitting any definition of what that burden of proof shall require at the pleading stage).
circuit courts have agreed) that the heightened pleading standards of the PSLRA do not apply to the element of loss causation. 61 Thus, if the heightened pleading standards of the PSLRA do not apply to loss causation (due to the statute’s silence and the courts’ recognition of that silence), 62 then a reasonable question arises regarding which pleading standard does apply—the traditional pleading standard under Rule 8(a)(2), or the heightened particularity standard under Rule 9(b), which was specifically designed to apply to claims alleging fraud. 63

3. Rule 8(a)(2)

Rule 8(a)(2) sets out the fundamental pleading standard for civil litigation and governs all claims in a civil suit. 64 It requires that a claim contain “a short and plain statement . . . showing that the pleader is entitled to relief.” 65 For the past sixty years, the “short and plain statement” recital has been commonly referred to as “notice pleading.” 66

The development of notice pleading was a cognizant attempt to relax pleading standards and to move away from the confusing Code pleadings scheme of the nineteenth century. 67 Notice pleading was intended to be liberal in allowing claims to advance procedurally so that they would receive an evaluation on their merits. 68

The adequacy of the pleading was


62. See, e.g., In re Mut. Funds Inv. Litig., 566 F.3d 111, 119–20 (4th Cir. 2009) (“Because Congress only addressed misrepresentations[,] [fraud] and scienter in § 78u-4b [of the PSLRA], the other elements of a securities fraud claim are analyzed under the pleading standards of the Federal Rules of Civil Procedure. . . . [T]he PSLRA’s heightened pleading requirements do not govern our analysis of . . . loss causation.”).

63. FED. R. CIV. P. 9(b).

64. See WRIGHT & MILLER, supra note 22, § 1202, at 87 (3d ed. 2004) (noting that Rule 8 is the “keystone” of the Rules-based pleading system).

65. FED. R. CIV. P. 8(a)(2).

66. See Conley v. Gibson, 355 U.S. 41, 47 (1957) (“All the Rules require is a short and plain statement of the claim that will give the defendant fair notice of what the plaintiff’s claim is and the grounds upon which it rests.”).

67. See Robert G. Bone, Plausibility Pleading Revisited and Revised: A Comment on Ashcroft v. Iqbal, 85 Notre Dame L. Rev. 849, 862–66 (2010) (discussing the Code pleading system as an evolution from the belief in the ability to concretely distinguish a statement of fact from a conclusion of law and as a reaction to the perceived “hypertechnicality and . . . irrationality of the common law forms of action and common law pleading[,]” explaining how the drafters of the Federal Rules of Civil Procedure were reacting, in turn, to the legal realist movement that critiqued the ability to meaningfully distinguish between a statement of fact and a legal conclusion—in essence, the distinction “depends on the degree of factual specificity”). The author also argues that the “pure notice pleading system has little need for a distinction between legal conclusions and factual allegations [because . . . [t]he question for notice pleading is whether the complaint, taken as a whole, gives fair notice of what the dispute is about.” Id.

68. Id. at 864–65.
analyzed under the “no set of facts” standard, where courts would appraise
the sufficiency of a complaint on whether “it appear[ed] beyond a
reasonable doubt that the plaintiff can prove no set of facts in support of his
claim which would entitle him to relief.” To determine whether no set of
facts existed, the courts took a holistic approach, evaluating the claim in its
factual entirety.70

The traditional notice pleading under the no set of facts standard, however, is no longer good law.71 In 2007, the Supreme Court clarified
that a complaint’s sufficiency had always entailed the notion that the claim
to relief must be plausible.72 In Twombly the Supreme Court abrogated its
no set of facts standard derived from Conley v. Gibson and instead
required that a plaintiff present enough factual matter to lead to a plausible
conclusion of wrongdoing.76 The Court was careful to clarify that requiring
“plausible grounds to infer [illegal conduct]” was not the same as
“impos[ing] a probability requirement at the pleading stage.”77

Though the Court stressed that it did not impose a probability standard at
the pleadings stage it nonetheless emphasized that Conley was never
intended to be read so strictly as to positively require a complaint to move
forward unless it was impossible to show some set of facts on which the
plaintiff could prevail.78 Rather, “a complaint . . . must contain either direct
or inferential allegations respecting all the material elements necessary to

69. See Conley, 355 U.S. at 45–46 (emphasis added) (outlining the “no set of facts”
standard).
70. See Bone, supra note 67, at 865–66 (explaining that the purpose of notice pleading
is very simply to provide notice, and in determining whether the notice is sufficient, the
entire complaint must be taken under consideration).
71. See Conley, 355 U.S. at 45–46 (outlining the traditionally liberal pleading standard
that a complaint should not be dismissed “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”).
Twombly retired the Conley no-set-of-facts test . . . .").
requirement in Conley’s “no set of facts” standard to have implicitly required plausibility
when considered within the context of the complaint as a whole); see also Wright &
Miller, supra note 22, § 1202, at 94 (acknowledging that the Rules Advisory Committee
intended the rule to “contemplate the statement of circumstances, occurrences, and events in
support of the claim presented”).
74. See Twombly, 550 U.S. at 563 (stating that because the phrase “no set of facts” has
been so misunderstood—to the point that the plausibility concept that the Court now claims
is inherent in its reading is most often left unapplied—the term has “earned its retirement”
and is “best forgotten as . . . incomplete”).
75. 355 U.S. 41 (1957).
76. Twombly, 550 U.S. at 557.
77. Id. at 556.
78. Id. at 561–62 (referencing courts and commentators who have resisted a literal
reading of Conley’s no-set-of-facts language).
sustain recovery under some viable legal theory.”  That is, the complaint taken as a whole requires some element of plausibility, and plausibility is sufficient where the complaint alleges factual matter that allows for “direct or inferential allegations respecting all the material elements [of the claim] . . .”

In *Iqbal*, the Court explicitly extended the *Twombly* plausibility pleading standard to all civil litigation and modified the formal analysis in determining sufficient plausibility. The Court formalized a two-prong approach that it claimed applied the underlying jurisprudential principles of the *Twombly* decision. The first prong required the Court to separate factual allegations from legal conclusions. The Court then dismissed those allegations deemed to be “conclusory” on the basis that bare legal conclusions are not entitled to the privilege that all well-pled facts be taken as true at the motion to dismiss stage. The second prong then applied the plausibility test to the remaining allegations. The formal two-prong approach is the current standard for evaluating the plausibility of a complaint under Rule 8(a)(2).

4. *Rule 9(b)*

Whereas Rule 8(a)(2) applies to civil claims generally, Rule 9(b) is the traditional standard for pleading claims that assert a commission of fraud. It requires a claimant to state with particularity the circumstances that constitute that act of fraud. Because claims of fraud entail a certain stigmatizing effect upon the defendant, the purpose of requiring

79. Id. at 562 (quoting Ascon Props., Inc. v. Mobil Oil Co., 866 F.2d 1149, 1155 (9th Cir. 1989)).
80. Id.; see Bone, supra note 67, at 859 (explaining that *Twombly* interprets the complaint as a whole when determining which statements are simply conclusory and do not contribute anything factually new to the complaint). *But see* Ashcroft v. *Iqbal*, 129 S. Ct. 1937, 1960–61 (2009) (Souter, J., dissenting) (arguing that the Court erred in analyzing the complaint in isolated parts because Iqbal’s allegations are sufficiently specific when considering the complaint as a whole).
81. 129 S. Ct. at 1953 (stating that *Twombly* is applicable to “all civil actions”).
82. Id. at 1949–50.
83. Id.
84. Id. (explaining that while the court must “take all of the factual allegations in the complaint as true”, it is “not bound to accept as true a legal conclusion couched as a factual allegation” (internal quotation marks omitted)).
85. Id. at 1950.
86. See Fed. R. Civ. P. 9(b) (stating that for “fraud or mistake” a plaintiff must plead with “particularity”).
87. However, the particularity requirement does not apply to elements consisting of a person’s state of mind in a fraud claim; the second sentence of Rule 9(b) allows such elements to be alleged generally. Id.
88. See Vess v. Ciba-Geigy Corp., 317 F.3d 1097, 1104 (9th Cir. 2003) (describing the purpose of Rule 9(b) as protecting a defendant against reputational harm consequent of claims of fraudulent conduct); see also Kearns v. Ford Motor Co.,
particularity in a fraud claim is to ensure responsibility and accuracy in the claimant’s complaint. The text of Rule 9(b) does not explicitly state what particularity requires, but it has generally been interpreted to include the “who, what, when, where, and how” of the alleged fraud. The exact kind of facts required for a claim to be sufficiently particular will tend to vary with the context of the underlying claim. While it is clear that Rule 9(b) applies to all claims that “alleg[e] fraud or mistake[,]” what is not as clear is the scope of the “circumstances [that] constitute[e] [the] fraud or mistake.” “Circumstances” becomes a difficult term to define. While the term generally includes the “who, what, when, where, and how” discussed above, the term is ambiguous enough to potentially sweep up any and all elements of a claim of fraud—including, theoretically, the element of loss causation in a securities fraud claim.

567 F.3d 1120, 1125 (9th Cir. 2009) (listing the three purposes of Rule 9(b) as: (1) providing defendants with adequate notice while at the same time preventing plaintiffs from filing complaints as a pretext for discovery of unknown wrongs; (2) protecting defendants from reputational harm; (3) avoiding the social and economic costs of litigation absent factual basis for a claim).

89. See Wright & Miller, supra note 22, § 1296, at 38–39 (noting that courts are frequently concerned with irresponsible “fishing expeditions” that seek to use litigation and the prospect of discovery solely as an attempt to learn “whether unknown wrongs actually have occurred,” and that forcing a plaintiff to be more particular helps to ensure that plaintiffs are more responsible in bringing their claims and allows defendants to have accurate information upon which to build an adequate defense).

90. See Bell Atl. Corp. v. Twombly, 550 U.S. 544, 569 n.14 (2007) (commenting on the utility of Rule 9(b)’s particularity requirement in the context of certain subjects [such as fraud] because they otherwise risk “abusive litigation” under the general pleading standard of Rule 8(a)(2)); Borsellino v. Goldman Sachs Group, Inc., 477 F.3d 502, 507 (7th Cir. 2007) (citing Payton v. Rush-Presbyterian-St. Luke’s Med. Ctr., 184 F.3d 623, 627 (7th Cir. 1999)) (clarifying that the reason for the heightened pleading of “particularity” is to ensure that the claim of alleged fraud is “responsible and supported, rather than defamatory and extortionate” (internal citation omitted)); see also Wright & Miller, supra note 22, § 1296, at 31 (identifying the primary purpose of the heightened pleading requirements under Rule 9(b) as a desire to protect a defendant’s “reputation and goodwill,” and extensively detailing the case law across the circuits in support of this proposition.).

91. See, e.g., United States ex rel. Lusby v. Rolls-Royce Corp., 570 F.3d 849, 853 (7th Cir. 2009) (stating that “particularity” means providing the essential elements found “in the first paragraph of any newspaper story”).

92. See Wright & Miller, supra note 22, § 1296, at 53 (recognizing that the particularity requirement will have varying effect in different contexts and that in some situations “a motion to dismiss alleging noncompliance . . . is virtually assured in certain categories . . . . “) (emphasis added); cf. Spencer, supra note 27, at 441–47 (discussing that in the context of plausibility pleading under Rule 8(a)(2), facts sufficient to lead to a plausible claim will generally vary considerably with the context of the underlying claim itself).

93. FED. R. CIV. P. 9(b).

94. Id.

95. See, e.g., Lusby, 570 F.3d at 853 (defining “particularity” as “the who, what, when, where, and how: the first paragraph of any newspaper story.”).

96. See Wright & Miller, supra note 22, § 1297, at 74 (suggesting that a “prudent” lawyer may wish to plead “all of the elements of fraud [with
Given the fact that a securities fraud claim is predicated on the commission of a fraud—an intentional misstatement or omission of material fact—there is a legitimate question as to whether Rule 9(b) should govern the pleading standard for all elements of a securities fraud claim not already covered by the PSLRA, such as the element of loss causation. Moreover, Congress made explicit its desire to heighten pleading standards in the private securities fraud context in order to curb frivolous and abusive litigation. Thus, if Congress desired to heighten the pleading standards in private securities fraud litigation generally, requiring loss causation to be pled under Rule 9(b) would be consistent with that congressional intent and therefore may be the proper standard.

... whenever that is possible... [because] sometimes federal judges have gone beyond the limited text of Rule 9(b) and have required more particularity on a greater range of subjects” (emphasis added).

97. Cf. SEC v. U.S. Environmental, Inc., 82 F. Supp. 2d 237, 240 (S.D.N.Y. 2000) (addressing a market manipulation claim and asserting that “[t]o satisfy Rule 9(b) ... [the] claim must specify what manipulative acts were performed, which defendants performed them, when the manipulative acts were performed, and what effect the scheme had on the market for the securities at issue”) (emphasis added). The added requirement that the plaintiff must show in his claim the effect of the scheme is suggestive of a sort of causal relationship—how some action affected or caused some detriment; this lends some support for the proposition that the element of loss causation could be swept up in Rule 9(b)’s particularity requirement. But see, e.g., United States ex rel. Marlar v. BWXT Y-12, L.L.C, 525 F.3d 439, 444 (6th Cir. 2008) (restating the oft-used recitals of the minimum requirements for Rule 9(b) as essentially: time, place, and content; reliance; the fraudulent scheme itself; fraudulent intent; and injury resulting from the fraud). These familiar Rule 9(b) recitals mention the requirements of “fraudulent scheme” and “injury,” but they consistently fail to include the requirement of the causal connection between the two. See, e.g., id.

98. See In re Mut. Funds Inv. Litig., 566 F.3d 111, 119–20 (4th Cir. 2009) (“Congress only addressed misrepresentations[,] [fraud] and scienter in [the PSLRA], the other elements of a securities fraud claim are analyzed under the pleading standards of the Federal Rules of Civil Procedure... the PSLRA’s heightened pleading requirements do not govern our analysis of... loss causation.”).

99. See Private Securities Litigation Reform Act, Pub. L. 104-67, § 101(b), 109 Stat. 737, 743–49 (1996) (codified as amended in scattered sections of 15 U.S.C.) (listing the heightened pleading standard requirements in a section titled “Reduction of Abusive Litigation”); WRIGHT & MILLER, supra note 22, § 1301.1, at 279 (detailing congressional concern that Rule 9(b) was not being properly applied to “frivolous” securities litigation and that more action was needed to curb abusive litigation).

B. Judicial Application of Pleading Standards to the
Element of Loss Causation

While the courts have been consistent in acknowledging that the
pleading standards under the PSLRA do not apply to the element of loss
causation, they have diverged on whether the proper standard should be
Rule 8(a)(2) or Rule 9(b). To determine what the proper pleading standard
should be, it is important to survey the courts’ reasoning in support of each
approach. The survey will begin with the Supreme Court’s decision in
Dura Pharmaceuticals, Inc. v. Broudo where the Court assumed Rule
8(a)(2) as the pleading standard for the purpose of addressing the
substantive requirements of loss causation. The survey will continue with
an examination of the federal circuit courts that follow the Rule 8(a)(2)
approach, and those courts that follow the Rule 9(b) approach.

1. The Supreme Court’s implicit adoption of Rule 8(a)(2)

In Dura, the Supreme Court addressed a Ninth Circuit decision
holding that the purchase of an artificially inflated stock price, without
more, was sufficient to establish the element of loss causation. The
Ninth Circuit reasoned that when a material misstatement or omission
causes the price of a stock to be artificially inflated, the purchaser of that
stock would necessarily suffer the economic loss at the time of purchase.
Therefore, because the material misstatement or omission caused the
artificial price, that same material misstatement or omission legally caused
the economic loss to the purchaser (the form of economic loss being the
initial overpayment for the stock).

The Supreme Court rejected this approach and ultimately found that
an “‘artificially inflated purchase price’ is not itself a relevant economic
loss.” The Court reasoned that the transaction involving the artificially
inflated price did not guarantee that an injury or loss would occur; the

101. See, e.g., In re Mut. Funds Inv. Litig., 566 F.3d at 120 (recognizing that Congress
only addressed the pleading standards of the elements of misrepresentation, fraud, and
scienter with the PSLRA; it did not address the element of loss causation, so it is governed
103. Id.
104. See Broudo v. Dura Pharm., Inc., 339 F.3d 933, 938 (9th Cir. 2003) (holding that
showing the purchase of an inflated stock price, absent showing the subsequent decline in
stock price, is sufficient as a substantive showing of loss causation) rev’d 544 U.S. 336, remanded to 452 F.Supp. 2d 1005 (S.D. Cal. 2006).
105. Id.
106. See Dura Pharm., Inc., 544 U.S. at 342–44 (restating the reasoning of the 9th Circuit’s decision).
107. Id. at 338.
108. Id. at 347.
causal requirement (loss causation) was not necessarily satisfied because the purchase of the stock at the inflated price alone did not result in an injury in fact where it was not accompanied by some actual economic loss (through the sale of the stock). The Court noted that when the purchaser finally sells the share, even at a lower price, the lower price might be the product of other factors and not necessarily the result of the material misstatements or omissions. Thus, the “purchase price will not itself constitute or proximately cause the relevant economic loss.”

While the Court’s determination of the substantive requirements of loss causation has implications for the procedural pleading requirements of loss causation, the Court’s loss causation analysis within the pleading context of Rule 8(a)(2) is the immediate concern. The Court explained that the “ordinary pleading rules [in Rule 8] are not meant to impose a great burden upon a plaintiff.” The Court then cited Conley for the proposition that even though the claim may be a “short and plain statement . . . [it] must provide the defendant with ‘fair notice of what the plaintiff’s claim is and the grounds upon which it rests.’” That is, the plaintiff in Dura failed to meet Rule 8(a)(2)’s pleading standard because he failed to provide “adequate grounds” for a right to relief. The Court went on to discuss that while there should not be too heavy of a burden on the plaintiff in showing loss causation, it must be balanced against the purpose of the securities statutes in curbing abusive litigation practices. While the Court did not directly hold that the element of loss causation would be evaluated under Rule 8(a)(2), by assuming the Rule 8(a)(2) pleading standard in its substantive analysis, the Court gave clear indication of a preference for that rule over Rule 9(b) in assessing the adequacy of pleading loss causation.

109. Id. at 342–43.
110. Id.
111. Id. at 342.
113. Dura Pharm., Inc., 544 U.S. at 346. Interestingly, this language arguably serves as the foundation for the Court’s rhetorical shift to the “enough factual matter (taken as true)” language in Bell Atlantic Corp. v. Twombly, 550 U.S. 550, 556 (2007), to requiring a plaintiff to allege sufficient factual content to “[nudge his claim] . . . across the line from conceivable to plausible” in Ashcroft v. Iqbal, 129 S. Ct. 1937, 1952 (2009).
114. Dura Pharm., Inc., 544 U.S. at 346.
115. Id. at 347.
116. Id. (citing H.R. Rep. No. 104-369, at 31 (1995) (Conf. Rep.) 1995 U.S.C.C.A.N. 730, 730 (noting a desire to curb “abusive practices including the routine filing of lawsuits . . . with only a faint hope that the discovery process might lead eventually to some plausible cause of action” (emphasis added)).
2. The Rule 8(a)(2) approach

Both the Fifth and Eighth Circuits have clearly adopted Rule 8(a)(2) as the pleading standard for loss causation. The Fifth Circuit has adopted Rule 8(a)(2) as the governing standard while specifically including *Twombly’s* plausibility gloss.\(^{118}\) The Eighth Circuit is the first circuit court to address loss causation since the Supreme Court handed down *Iqbal*, and it expressly applied *Iqbal’s* two-prong analysis.\(^ {119}\)

\[\text{a. Explicit adoption of Rule 8(a)(2) in light of *Twombly* and *Dura*:}
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The Fifth Circuit approach

In *Lormand v. US Unwired, Inc.*,\(^ {120}\) the Fifth Circuit specifically discussed the effect of the *Twombly* plausibility standard on the element of loss causation in a Rule 10b-5 claim. The court began by suggesting that the *Twombly* Court relied, in part, on the *Dura* Court’s discussion of the purpose of securities legislation and the desire to avoid abusive litigation in developing the plausibility pleading standard.\(^ {121}\) The Fifth Circuit concluded that a contiguous reading of *Dura* and *Twombly* required that loss causation be pled under the plausibility standard of Rule 8(a)(2).\(^ {122}\)

Consistent with the *Dura* and *Twombly* Courts, the Fifth Circuit noted that the plausibility standard was not meant to be overly burdensome on the plaintiff. The standard only required that the plaintiff allege enough factual matter to allow the court to reasonably expect that discovery will reveal a legitimate claim.\(^ {123}\) The plausibility test for loss causation, according to the Fifth Circuit, is one in the alternative that requires the “plaintiff [either] to allege . . . a facially ‘plausible’ causal relationship between the fraudulent statements or omissions and the plaintiff’s economic loss [as *Dura* indicates] . . . or, as *Twombly* indicates, . . . allege enough facts to give rise to a

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the enactment of the PSLRA, the sufficiency of a complaint for securities fraud was governed *not* by Rule 8, but by the heightened pleading standards set forth in Rule 9(b)” (emphasis added).

\(^{118}\) See *Lormand v. US Unwired, Inc.*, 565 F.3d 228, 255 (5th Cir. 2009) (adopting the Rule 8(a)(2) standard while giving deference to *Twombly’s* interpretation thereof).

\(^ {119}\) See *McAdams v. McCord*, 584 F.3d 1111, 1113 (8th Cir. 2009) (relying on *Iqbal* in noting that the court is not required to accept as true a legal conclusion “couched as factual allegation,” and that the complaint must instead contain “sufficient factual matter, accepted as true, to ‘state a claim to relief that is plausible on its face.’”).

\(^{120}\) 565 F.3d 228 (5th Cir. 2009).

\(^{121}\) Id. at 255.

\(^{122}\) Id.

\(^{123}\) Id. at 258 (quoting Bell Atl. Corp. v. Twombly, 550 U.S. 554, 556 (2007)) (―Asking for plausible grounds to infer an agreement does not impose a probability requirement at the pleading stage; it simply calls for enough fact to raise a reasonable expectation that discovery will reveal evidence of the illegal agreement.”).
reasonable hope or expectation that discovery will reveal evidence of the
foregoing elements of loss causation.”

In its analysis, the Fifth Circuit approached the issue flexibly. Because it
formulated a test in the alternative, a plaintiff is provided with two options
to advance a claim. Additionally, the court read Dura to require only
that a plaintiff “provide[] the defendants with notice of what the relevant
economic loss might be . . . and of what the causal connection might be
between that loss and the defendants’ alleged misrepresentations.” It
also read the Twombly plausibility standard somewhat permissively,
requiring only that the allegation of facts give rise to a “reasonable hope or
expectation” that discovery will provide the necessary evidence.

In Lormand, the court found that both of these standards were met
(though meeting only one is sufficient). The Dura pleading standard was
satisfied because the plaintiff was suitably specific in detailing his loss—a
drop in share price of eighty-two percent—and he gave the defendant fair
notice about his theory of loss causation where the omission of the effects
of the sub-prime credit program proximately caused the eighty-two percent
decrease. The Twombly pleading standard was satisfied because the
plaintiff presented enough by way of factual allegations (an eighty-two
percent decline in share price, and the omission of the effects of the sub-
prime credit program) to give rise to a reasonable “hope or expectation”
that discovery would reveal evidence that loss causation existed in fact.

b. Explicit adoption of Rule 8(a)(2) in light of Iqbal: The Eighth
Circuit approach

In McAdams v. McCord, the Eighth Circuit went out of its way to
apply the newly explicated Iqbal plausibility standard. The district court
dismissed the plaintiffs’ claim based on a failure to meet the pleading
requirements of Rule 9(b) and the PSLRA for the elements of fraud and
scienter. The Eighth Circuit, however, asserted its authority to review
dismissals under Rule 12(b)(6) de novo. It noted that the district court did not reach the issue of loss causation, but

124. Id. at 258.
125. Id.
126. Id. at 262 (emphasis added).
127. Id.
128. Id.
129. Id.
130. Id.
131. Id. at 263.
132. 584 F.3d 1111 (8th Cir. 2009).
133. Id. at 1113.
134. Id.
because it wanted to decide the matter, the court reiterated that it “may affirm the district court’s judgment ‘on any basis supported by the record.’”\footnote{135} The court began with the now familiar \textit{Iqbal} recital that it is “not bound to accept as true legal conclusions couched as a factual allegation,”\footnote{136} and that a “complaint must contain sufficient factual matter . . . to state a claim to relief that is plausible on its face.”\footnote{137}

In its analysis, the court quickly moved to the “threadbare,” “conclusory” language of \textit{Iqbal} to conclude that the plaintiffs’ claims of losses exceeding ten million dollars (the figure that represented the total amount of their investment) due to material misstatements and omissions of fact were simply conclusory.\footnote{138} The court required the complaint to plead both the purchase price of the share and the share price immediately following the revelation of the misstatement.\footnote{139} The lack of this specific (or “particular”) information rendered the allegations conclusory and “defeat[ed] the plausibility of the investors’ claim that [the defendant’s] audit opinions . . . caused their losses.”\footnote{140}

3. \textit{The Rule 9(b) approach}

Both the Fourth Circuit and the Ninth Circuit have indicated a willingness to analyze pleading loss causation under Rule 9(b). The Fourth Circuit has explicitly stated that it will evaluate the element of loss causation under Rule 9(b).\footnote{141} The Ninth Circuit, after having its analysis concerning the substantive sufficiency of loss causation as pled under Rule 8(a)(2) overturned by the Supreme Court in \textit{Dura}, has since assumed that Rule 9(b) governed pleading loss causation in a 2008 case.\footnote{142} The Ninth Circuit did not, however, directly hold that Rule 9(b) is the applicable pleading standard.\footnote{143}

\textit{a. Explicit adoption of Rule 9(b): The Fourth Circuit approach}

In \textit{In re Mutual Funds Investment Litigation},\footnote{144} the Fourth Circuit recognized that the heightened pleading requirements of the PSLRA do not
govern the issue of loss causation.\textsuperscript{145} It then stated that “[p]rior to the enactment of the [PSLRA], § 10(b) fraud claims in this circuit were governed by Federal Rule of Civil Procedure 9(b), not Rule 8.”\textsuperscript{146} The Fourth Circuit therefore explained that under Rule 9(b) a plaintiff must show loss causation with “sufficient specificity to enable the court to evaluate whether the necessary causal link exists.”\textsuperscript{147} The court made reference to Rule 8(a)(2) only to note that it was never used to plead claims of fraud in the Fourth Circuit, and the court made no mention at all of the \textit{Twombly} plausibility pleading standard in the loss causation context.\textsuperscript{148}

In its analysis, the Fourth Circuit concluded that the plaintiff pled the element of loss causation with sufficient specificity.\textsuperscript{149} The plaintiffs provided particular facts regarding the misstatements in the prospectuses, the revelation that the statements were false, the payment of fines for the false statements, and the subsequent decline in share price.\textsuperscript{150} By alleging that the false or misleading statements printed in the prospectuses that were drafted and disseminated by the defendants were at least a “substantial cause” in the decrease in share price, the plaintiff was able to satisfy the Rule 9(b) pleading standard.\textsuperscript{151}

\textit{b. Implicit adoption of Rule 9(b): The Ninth Circuit approach}

In \textit{Berson v. Applied Signal Technology, Inc.},\textsuperscript{152} the Ninth Circuit did not directly rule on which pleading standard applied to loss causation, but it did assume a permissive formulation of Rule 9(b) for the purpose of analysis. The plaintiffs argued for what was then the somewhat less stringent standard under Rule 8(a)(2), while the defendants argued for the heightened standard under Rule 9(b).\textsuperscript{153} The court acknowledged that neither it nor the Supreme Court had decided the matter, and proceeded to “assume—without deciding—that Rule 9(b) governs,” and required that a plaintiff plead loss causation with particularity.\textsuperscript{154} More specifically, the plaintiff was required to give “sufficient detail to give defendants ample notice of plaintiff’s loss causation theory, and to give the court some assurance that the theory has a basis in fact.”\textsuperscript{155} Like the Fourth Circuit in \textit{In re Mutual
Funds Investment Litigation, the Ninth Circuit made no mention of plausibility. Moreover, after it explained that the plaintiff need only give the court "some assurance" that the claim had a basis in fact, the court went on to declare that "Rule 9(b) require[d] no more." The court's rhetoric suggests that the Ninth Circuit might be flexible in its pleading analysis even under the heightened pleading standard of Rule 9(b).

In Berson, the Ninth Circuit concluded that the plaintiffs sufficiently pled loss causation under Rule 9(b). The court found that the plaintiffs alleged facts particular enough to show that "but for the circumstances that the fraud concealed—namely, the fact that much of Applied Signal's backlog had been halted by stop-work orders—plaintiffs' investment... would not have lost its value." Pivotal to this conclusion may have been the fact that the plaintiffs were able to describe the effect of these stop-work orders on the company's revenue. The plaintiffs showed that the stop-work orders caused revenue to drop by twenty-five percent, which subsequently led to a sixteen percent drop in the company's stock price.

There is no discussion of the credibility of these calculations, but the court found them sufficiently particular at the pleading stage.

II. ANALYSIS

There are credible arguments on both sides of this federal circuit split. Part A will set out to resolve which is the proper approach to pleading loss causation. Resolving the proper pleading standard, however, is not enough. Part B will explore the practical effects of that pleading standard on pleading loss causation.

156. See id. (omitting from the analysis any mention of other circuits' analysis of the element under Rule 8(a)(2) or the plausibility standard therein).
157. Id. (emphasis added).
158. Id.
160. Berson, 527 F.3d at 989.
161. Id.
162. Id.
163. Id.
164. Id.
A. **The Proper Pleading Standard for Loss Causation is Rule 8(a)(2)**
as Demonstrated by an Analysis of “Causation” Generally and
Within the Tort Law Context, a Textual Reading of the Rules,
Supreme Court Precedent, and an Understanding of
the Traditional Common Law Elements of Fraud

As illustrated above, the federal circuit courts are split regarding the
proper pleading standard for loss causation. The Fourth Circuit makes
the reasonable argument for Rule 9(b) essentially through simple
syllogism: Rule 9(b) governs general fraud claims; a private securities
fraud claim is a subset of a general fraud claim; loss causation is an
element of a private securities fraud claim; therefore, Rule 9(b) should
govern the pleading standard for loss causation. Moreover, the Supreme
Court has used broad language in dicta to suggest that Rule 9(b) governs all
securities fraud claims. On the other hand, the Fifth Circuit’s survey of
the evolution of Supreme Court precedent, combined with Iqbal’s broad
extension of plausibility pleading and the Eight Circuit’s application
thereof, is an equally persuasive indication that the proper standard for
pleading loss causation is under Rule 8(a)(2).

1. **Applying an analysis of causation generally and of proximate cause to a textual reading of Rule 9(b)**

To determine which pleading standard applies to the element of loss
causation, it is first important to appreciate the concept of causation
generally. Causation as an element of a cause of action is difficult to define
legally. It does not readily lend itself to the same conceptually concrete

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165. *See Dura Pharm., Inc. v. Broudo*, 544 U.S. 335, 346–47 (2005) (deciding the case under the pre-*Twombly* Rule 8(a)(2) standard, but not directly holding that Rule 8(a)(2) is the proper pleading standard for loss causation). *Compare Berson*, 527 F.3d at 989 (claiming that the Supreme Court assumed, but did not decide that Rule 8(a)(2) governs the pleading of loss causation so this court was free to assume—without deciding—that Rule 9(b) applied), *with Lormand v. US Unwired, Inc.*, 565 F.3d 228, 255 (5th Cir. 2009) (synthesizing *Dura* and *Twombly* to conclude that in deciding the *Dura* case under Rule 8(a)(2), the Supreme Court had essentially “identified the basic principles of pleading loss causation under Federal Rule of Procedure 8(a)(2)”).


167. *See Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 319 (2007) (stating in dicta that as a general matter, “[p]rior to the enactment of the PSLRA, the sufficiency of a complaint for securities fraud was governed not by Rule 8, but by the heightened pleading standards set forth in Rule 9(b)”(emphasis added)).

168. *See Lormand*, 565 F.3d at 255–56 (detailing the progression and refinement of pleading under Rule 8(a)(2) from *Dura to Twombly*).

169. *See Dobbs, THE LAW OF TORTS*, § 180, at 443 (3d ed. 2004) (discussing that despite its name, “proximate cause” is not truly about causation, but rather, it is about the appropriate scope of liability).
explanation that an element such as “material misstatement” (i.e. some important statement that is untrue) does. Logically, it is often difficult to distinguish a causal event from an event simply resulting from some other cause or event.

For example: if A caused B and B caused C, then A caused C in at least some respect because B necessarily could not have caused C until A caused B. Therefore, although we see B as the most immediate cause of C, it is possible to argue that B was not the true cause of C because without A there would have been no B to cause C. Viewed this way, A is the true cause of C. Of course, A is nothing more than an event brought about by some other event such as A’, thereby further confusing the “true” cause, or cause in fact, of C. Consequently, the law endeavors to circumvent and simplify this enigma by narrowing what is otherwise an infinite chain of cause and effect for the purposes of determining and attaching liability.\textsuperscript{170} That is, the law actually defines the element of causation within a context of seeking to determine responsibility and liability rather than seeking to glean the “true” or ultimate cause of a given event or injury.\textsuperscript{171}

Perhaps the best approach to understanding loss causation and which pleading standard should apply to it is by analogy. The element of proximate cause in the tort context is the most apt analogy for this purpose.\textsuperscript{172} While proximate cause is an element of a tort claim, it is analytically distinct from the negligent act that represents the underlying source of the claim.\textsuperscript{173} This distinction is critical to understanding why Rule 8(a)(2) is the applicable standard of pleading loss causation because loss causation is not a “circumstance constituting the fraud” within the meaning of Rule 9(b).\textsuperscript{174}

In the tort law context, proximate cause represents the merger between cause in fact (i.e. the sort of physics-oriented causal chain of events described in the example above) and a policy decision that the law makes

\textsuperscript{170} Id.

\textsuperscript{171} Id.

\textsuperscript{172} See McAdams v. McCord, 584 F.3d 1111, 1114 (8th Cir. 2009) (analogizing loss causation in the securities fraud context to the common law requirement of “proximate causation” in the tort context); \textit{see also} HAZEN, \textit{supra} note 37, § 12:11[1], at 479–81 (describing the analysis of loss causation as similar to the analysis of proximate cause).

\textsuperscript{173} See DOBBS, \textit{supra} note 169, § 182, at 447–48 (clarifying that the issue of proximate cause is distinct from a defendant’s negligent action and does not arise until after some negligence has been identified).

\textsuperscript{174} FED. R. CIV. P. 9(b).
in defining the scope of liability for some actor’s conduct. More simply, proximate cause creates the legal connection between a defendant’s negligent conduct and a plaintiff’s harm sufficient for the law to say that the defendant “caused,” and is therefore liable for, the plaintiff’s injury. That causal connection, however, is itself something distinct from the defendant’s action—it simply represents a string that fastens the act to the injury and thus creates the basis for the actor’s legal liability. The question of causation itself does not arise until after a defendant has committed some act that creates the basis for his liability. The causal chain of events, beginning with a defendant’s action and resulting in a plaintiff’s injury, is therefore not itself an event that constitutes the defendant’s action.

By analogy then, the element of loss causation is not a circumstance that constitutes an act of securities fraud, so it should not be pled under Rule 9(b). Because the issue of causation arises only after the commission of an act that gives rise to legal liability, the element of causation cannot properly be said to be a “circumstance[] constituting” that act within the language of Rule 9(b). Rather, it is simply the legal device that strings together the defendant’s already constituted fraudulent act and the plaintiff’s economic loss for the purpose of attaching legal accountability. Thus, given that the PSLRA does not specify any pleading standard, and causal elements do not properly fall within the language of Rule 9(b), Rule 8(a)(2) must apply as the proper pleading standard for the element of loss causation.

2. Supreme Court precedent and the implicit adoption of Rule 8(a)(2)

An additional factor suggesting that Rule 8(a)(2) is the proper pleading standard for loss causation is the fact that the Supreme Court assumed, even though it did not hold, that Rule 8(a)(2) governed loss causation in its decision in Dura. The Court was clear that it would assume that “neither the Rules nor the securities statutes impose any special further

175. See Dobbs, supra note 169, § 181, at 445 (explaining that proximate cause is a causal connection that is aimed at expressing a value judgment about a defendant’s behavior and the appropriate scope of the defendant’s exposure to liability for that behavior).
176. Id. § 180, at 443.
177. See id. § 182, at 447–48 (noting that proximate cause is distinct from negligence because the former can only arise after the latter has been identified).
178. Id.
179. Id.
180. Id.
182. See supra Part I.A.2.
“requirement” with respect to pleading loss causation.\textsuperscript{184} The mention of a “special further requirement” suggests that the Court drew a distinction between the standard that it used to dismiss this case with the further particularity requirements of Rule 9(b) and the PSLRA.\textsuperscript{185} If the Court made clear that it would use neither Rule 9(b) nor the PSLRA as the pleading standard, then the only remaining pleading standard is Rule 8(a)(2). While the Ninth Circuit is correct in explaining that the Supreme Court did not directly rule on the issue of what pleading standard is required for loss causation,\textsuperscript{186} the Court made a significant, if only implicit, embrace of Rule 8(a)(2) as the proper standard by using it as the basis for its substantive conclusions.\textsuperscript{187}

Adding weight to this implicit adoption of Rule 8(a)(2) is the Fifth Circuit’s analysis recognizing the consistent line of progression from Conley through Dura to Twombly.\textsuperscript{188} The Twombly Court itself suggested that the notion of plausibility was implicit in its reasoning in Dura.\textsuperscript{189} There, the Court emphasized that in Dura, it “explained that something beyond the mere possibility of loss causation must be alleged . . . “.\textsuperscript{190} Thus, if Dura is the jurisprudential genesis of the plausibility requirement, it stands to reason that the plausibility standard under Rule 8(a)(2), conceived of in Dura (a loss causation case) and refined in Twombly and Iqbal, is the same standard that ought to apply to all subsequent loss causation cases.\textsuperscript{191}

3. Common law elements of fraud and the statutorily created element of loss causation

Finally, loss causation, though analogous to causal elements under the common law such as proximate cause, is not one of the common law

\textsuperscript{184} Id. (emphasis added).
\textsuperscript{185} Id.
\textsuperscript{186} See Berson v. Applied Signal Tech., Inc., 527 F.3d 982, 989 (9th Cir. 2008).
\textsuperscript{187} See Dura Pharm, Inc., 544 U.S. at 346, 348 (assuming Rule 8(a)(2) as the proper pleading standard while dismissing plaintiff’s claim).
\textsuperscript{188} See Lormand v. US Unwired, Inc., 565 F.3d 228, 255–57 (5th Cir. 2009) (describing an emerging plausibility standard implied by Rule 8(a)(2) from Conley to Twombly).
\textsuperscript{189} See Bell Atl. Corp. v. Twombly, 550 U.S. 544, 557–58 (2007) (recognizing Dura as a source of the concept of plausibility and that insufficient claims should be cut off at the earliest point).
\textsuperscript{190} Id. at 557–58 (citing Dura Pharm, Inc., 544 U.S. at 347).
\textsuperscript{191} See Lormand, 565 F.3d at 255 (discussing Dura and applying Twombly’s reading of Rule 8(a)(2) to the element of loss causation to require facially “plausible” causation or allegation of enough facts); McAdams v. McCord, 584 F.3d 1111, 1113–14 (8th Cir. 2009) (applying Iqbal’s formulation of Rule 8(a)(2) to the element of loss causation and emphasizing the requirement of sufficient factual allegations to create a plausible causal connection).
elements of a fraud claim in fact, so pleading standards designed to govern common law claims of fraud should not control it.\textsuperscript{192} Rule 9(b) generally applies only to the “traditional” elements of a fraud claim.\textsuperscript{193} Loss causation is not one of the traditional elements of a fraud claim.\textsuperscript{194} Rather, loss causation is a statutorily created element of a securities fraud claim,\textsuperscript{195} and the statute that created the element, the PSLRA, does not specify which pleading standard should apply.\textsuperscript{196} Thus, not being a common law element of fraud, Rule 9(b) would not control the pleading standard for loss causation, thereby leaving Rule 8(a)(2) as the governing pleading standard.

B. Pleading Loss Causation Under Iqbal’s Formulation of Rule 8(a)(2) Will Create a Higher Standard for a Plaintiff to Meet than Pleading Under Rule 9(b) Because Rule 8(a)(2) Requires that a Private Securities Fraud Claim Must Meet Plausibility as Well as Particularity

It is not yet clear the degree to which Twombly and Iqbal altered general pleading standards under Rule 8(a)(2).\textsuperscript{197} It is at least clear that the Twombly Court intended the scrutiny of plausibility to be something more than mere “possibility.”\textsuperscript{198} Further, Iqbal may be a higher pleading standard in some contexts than what the Twombly Court originally envisioned because the formalized two-step analysis begins by removing certain “conclusory” recitals from consideration under the plausibility standard.

\textsuperscript{192} See Securities Exchange Act of 1934 § 21D(b)(4), 15 U.S.C. § 78u-4 (b)(4) (2006) (creating the requirement that a plaintiff prove the element of loss causation); Wright & Miller, supra note 22, § 1297, at 60–71 (outlining the traditional common law elements of fraud and Rule 9(b)’s applicability to those elements but omitting the element of loss causation from the list).

\textsuperscript{193} Wright & Miller, supra note 22, § 1297, at 56.

\textsuperscript{194} Id. at 60–70.

\textsuperscript{195} See Securities Exchange Act of 1934 § 21D(b)(4) (creating the requirement that a plaintiff prove the element of loss causation).

\textsuperscript{196} See id. Securities Exchange Act of 1934 § 21D(B)(1)(B) codified at 15 U.S.C § 78u-4(b)(1), (b)(4) (applying, specifically, the heightened pleading standard of particularity to averments of misstatements and omissions, but remaining silent on the element of loss causation).

\textsuperscript{197} See Bone, supra note 67, at 867–83 (arguing that Iqbal significantly heightened the Twombly plausibility pleading standard through the alteration of the “conclusory statements” analysis); Hatamyar, supra note 37, at 596–625 (2010) (providing an interesting and novel empirical analysis of the increase in the rate at which courts have granted motions to dismiss from Conley through Twombly to Iqbal and suggesting the demise of notice pleading). But see Douglas G. Smith, The Twombly Revolution?, 36 Pepp. L. Rev. 1063, 1098 (2009) (arguing that the Twombly “plausibility standard does not represent a deviation from traditional notice pleading”).

\textsuperscript{198} See Ashcroft v. Iqbal, 129 S. Ct. 1937, 1949 (2009) (explaining that the plausibility standard does not require a probabilistic analysis, but holding that sheer possibility is insufficient); Bell Atl. Corp. v. Twombly, 550 U.S. 544, 557 (2007) (distinguishing between what is possible and what is plausible and requiring the latter).
Isolating and removing from the plausibility analysis allegations deemed to be “conclusory” could create a more difficult standard for a plaintiff to meet because he will not have the benefit of those recitals when a court passes on his claim’s overall plausibility. In pleading loss causation, notwithstanding the fact that Rule 9(b) is not the proper pleading standard, *Iqbal*’s two prong formulation of plausibility may actually encompass Rule 9(b) particularity pleading in the first prong, and go further to require plausibility in the second prong.

1. The first prong of the *Iqbal* analysis is functionally equivalent to Rule 9(b)’s particularity requirement

The *Iqbal* Court actually strengthened the pleading standard set out in *Twombly* by formalizing the plausibility analysis through a two-prong approach. This is accomplished primarily through the *Iqbal* Court’s application of the first prong. The first prong requires the reviewing court to search out and identify claims that are deemed too “conclusory” and eliminate them from the plausibility analysis as nothing more than “[t]hreadbare recitals of the elements of a cause of action.” Once eliminated, these “conclusory” statements are effectively removed from consideration under the actual plausibility analysis in the second prong. Thus, the plausibility analysis is ultimately applied to a redacted version of the original complaint. In such a context, it is easy to see how a claim that might otherwise seem plausible when considered as a whole

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199. *See Iqbal*, 129 S. Ct. at 1960 (Souter, J., dissenting) (taking issue with the majority’s approaching “conclusory” statements in isolation rather than within the context of the complaint as a whole); *see also Bone*, supra note 67, at 859–62 (characterizing *Iqbal*’s first prong as problematic, especially because *Iqbal* provides no guidance where “classification of allegations as legal conclusions can be decisive,” and agreeing with Souter’s opinion that factual allegations can be specific when read in the context of a complaint as a whole).

200. *Contra Twombly*, 550 U.S. at 561–62 (reading *Conley*’s “no set of facts” standard to implicitly require factual plausibility when considered in the context of the complaint as a whole).

201. *See Bone*, supra note 67, at 870–79 (arguing that *Iqbal*’s formal two-prong approach sets up a “thick screening model” that is more discriminating in its evaluation of a pleading’s sufficiency than *Twombly*’s “thin screening model” approach).

202. *Id.* at 859–60 (discussing the inevitable condemnation of claims deemed to be conclusory).


204. *See Bone*, supra note 67, at 861–62 (finding that *Iqbal*’s first prong is decisive and does “all the work”).

205. *Id.* *Contra Twombly*, 550 U.S. at 564–65 (analyzing the complaint as a whole in determining that certain claims were too conclusory).
(conclusory statements and all), is considered implausible when selectively analyzed after the first prong’s hollowing effect on the complaint. In *Twombly*, the Court claimed that it was not expanding the heightened factual particularity requirements under Rule 9(b) to all civil litigation. In *Iqbal*, however, the Court stated that to show facial plausibility, a plaintiff must plead sufficient “factual content that allows the court to draw the reasonable inference that the defendant is liable.” The *Iqbal* Court emphasized the requirement of pleading sufficient “factual content to nudge [the plaintiff’s] claim . . . across the line from conceivable to plausible” in developing the first prong of the formal two-prong analysis.

Justice Souter, who authored *Twombly*, dissented in *Iqbal*, calling the analysis a misapplication of *Twombly* and arguing that the factual allegations that the Court dismissed as “conclusory” should not have been read in isolation. Rather, the statements should be read in the context of the complaint as a whole. While *Twombly* utilized the “conclusory” language in its analysis, the distinction, as Justice Souter noted, is that the *Twombly* court interpreted the complaint as a whole and only excluded from the analysis those statements that were conclusory restatements of conduct alleged elsewhere in the complaint that did not add anything factually new to the complaint. In contrast, *Iqbal* began by utilizing the

206. See Bone, supra note 67, at 861–62 (explaining how the first prong essentially does all of the work so that what factual matter remains is likely to appear implausible if not considered within the context of the complaint as a whole).

207. See *Iqbal*, 129 S. Ct. at 1949 (citing the *Twombly* language and reiterating the point that “detailed factual allegations” are not required for the Rule 8 pleading standard); *Twombly*, 550 U.S. at 555 (stating that a pleading under Rule 8(a)(2) “does not need detailed factual allegations.”).

208. See *Iqbal*, 129 S. Ct. at 1949 (emphasis added).

209. Id. at 1952 (internal quotations omitted) (citing *Twombly*, 550 U.S. at 570).

210. See id. at 1949–52 (outlining a two-prong approach that begins with the identification and dismissal of any “conclusory” statements, and then moves to a plausibility analysis of the remaining factual claims); see also Bone, supra note 67, at 851 (“*Twombly* uses plausibility to screen only for truly meritless suits, but *Iqbal* uses it to screen for weak lawsuits too.”).

211. See *Iqbal*, 129 S. Ct. at 1960–61 (Souter, J., dissenting) (criticizing the majority for examining claims in isolation rather than within the context of the complaint as a whole).

212. Id.; see Bone, supra note 67, at 861–62 (critiquing the use of the first prong to isolate and eliminate certain claims).

213. *Twombly*, 550 U.S. at 556–57 (“[A] conclusory allegation of agreement at some unidentified point does not supply facts adequate to show illegality.”).

214. See *Iqbal*, 129 S. Ct. at 1960 (Souter, J., dissenting) (arguing that the mere recitation of the elements of a cause of action does not entitle the plaintiff to the assumption that those statements are true, but that those statement ought to be evaluated within the context of the whole complaint); *Twombly*, 550 U.S. at 564 (examining the claim in its entirety); see also Bone, supra note 67, at 861–62 (discussing the two distinct approaches of the Supreme Court in *Twombly* and *Iqbal*).
first prong to eliminate from the plausibility analysis any statements
deemed to be conclusory, and then used the second prong to apply the
plausibility analysis to what remained.\textsuperscript{215}

It is problematic that the Court provided no clarity regarding how to
apply the first prong.\textsuperscript{216} Rather than provide criteria for assessing which
statements are conclusory, the \textit{Iqbal} Court simply states that certain claims
just are conclusory.\textsuperscript{217} Without guidance, it is difficult to discern what a
fatal assertion of a legal conclusion is, and what a proper assertion of a fact
is because the distinction between the two is likely to turn on their relative degree of specificity
or particularity.\textsuperscript{218} Therefore, it may be that properly pleading plausibility
entails that the complaint’s factual recitals be particularly pled so as to pass
the scrutiny of \textit{Iqbal}'s conclusory analysis in the first prong.\textsuperscript{220}

The conclusory analysis essentially utilizes concepts similar to
those that underlie Rule 9(b)—a plaintiff cannot simply state the
element of a claim without a sufficiently particularized factual
underpinning.\textsuperscript{221} The rhetorical similarities between the first prong of the
plausibility analysis under Rule 8(a)(2) and the particularity requirement

\textsuperscript{215} See \textit{Iqbal}, 129 S. Ct. at 1949–52 (asserting that the two-pronged approach
conformed with and clarified \textit{Twombly}); Bone, \textit{supra} note 67, at 859–62 (interpreting the
\textit{Iqbal} court to have found “some defect or deficiency intrinsic to the allegation itself” and
repeating Souter’s argument that allegations that appear generalized and formulaic can gain
specificity when read in context). \textit{But see Twombly}, 550 U.S. at 564–65 (analyzing the
complaint as a whole without the formal two-prong approach).

\textsuperscript{216} See Bone, \textit{supra} note 67, at 859–60 (criticizing the Court for its lack of clarity
regarding the proper application of the first prong).

\textsuperscript{217} See \textit{Iqbal}, 129 S. Ct. at 1951 (“It is the conclusory nature of respondent’s
allegations, rather than their extravagantly fanciful nature, that disentitles them to the
presumption of truth.”); Bone, \textit{supra} note 67, at 859 (highlighting the fact that the Court
failed to provide guidance on how to determine whether an allegation is conclusory or not).

\textsuperscript{218} See Bone, \textit{supra} note 67, at 864 (gathering from Walter Wheeler Cook’s legal
realist critique of pleading the proposition that the “distinction between legal conclusions
and factual allegations is necessarily a matter of degree rather than in kind, and in particular
depends on the degree of factual specificity.” (citing Walter Wheeler Cook, \textit{‘Facts’ and
‘Statements of Fact’}, 4 U. Chi. L. Rev. 233, 242–44 (1936)).

\textsuperscript{219} Id.

\textsuperscript{220} \textit{Contra Twombly}, 550 U.S. at 555 (stating that a pleading under Rule 8(a)(2) “does
not need detailed factual allegations.”) (emphasis added); \textit{Iqbal}, 129 S. Ct. at 1949 (citing to the
\textit{Twombly} language and reiterating the point that “detailed factual allegations” are not
1947) (deeming, as the chief architect of the Federal Rules of Civil Procedure, as an
improvement the fact that the Federal Rules avoided the code distinction between factual
and legal conclusions by refraining from using the term “fact” in a simplified pleading rule).

\textsuperscript{221} Compare \textit{Wright & Miller, supra} note 22, § 1297, at 152, 160 (“A pleading that
simply avers the technical elements of fraud without providing any showing that a factual
relationship exists between the defendant . . . and the . . . conduct does not have sufficient
informational content to satisfy [Rule 9(b)’s] pleading-with-particularity requirement.”),
\textit{with Iqbal}, 129 S. Ct. at 1949 (“Threadbare recitals of the elements of a cause of action,
supported by mere conclusory statements, do not suffice.”).
under Rule 9(b) suggest that they may operate in the same way in certain applications.\textsuperscript{222} Thus, there appears to be no meaningful distinction between whether a plaintiff is required to plead “factual particularity” under Rule 9(b) or sufficient “factual content” under Rule 8(a)(2) to meet the conclusory analysis of the first prong.\textsuperscript{223}

The Eighth Circuit’s approach in \textit{McAdams} illustrates how the distinction between legal conclusion and factual allegation is generally a matter of specificity and is difficult to distinguish.\textsuperscript{224} The plaintiffs, who invested a total of $11 million dollars in the defendant company, UCAP,\textsuperscript{225} alleged that the defendant made two statements that misrepresented its overall financial condition.\textsuperscript{226} At a later date, the company revised those statements to reflect the truth about the company’s financial condition.\textsuperscript{227} The Eighth Circuit found that the plaintiffs failed to provide the value of UCAP’s stock either before, during, or after the announcements correcting the previous misstatements.\textsuperscript{228} Without this crucial, but seemingly elementary information, the court was able to call the plaintiffs’ assertions of loss causation conclusory, eliminate them from the analysis, and ultimately deem the rest of the claim implausible.\textsuperscript{229} Had the plaintiffs provided this crucial bit of information and provided more factual particularity, it appears that the court would have been willing to let the claim proceed. As the analysis does appear to turn simply on a matter of factual particularity, this decision is consistent with \textit{Iqbal}’s stricture in its first prong of analysis, requiring a claim to be pled at a certain level of particularity lest it be deemed conclusory.\textsuperscript{230} Pleading particularity to meet the requirements of \textit{Iqbal}’s first prong, however, is only the first step; the particular factual recitals and legal assertions must also be plausible.\textsuperscript{231}

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{222} See \textit{Id.}
\item \textsuperscript{223} See \textit{Spencer, supra note 27}, at 473–77 (suggesting that \textit{Twombly}’s plausibility standard inherently rejects a generalized pleading approach to the particularity requirement of Rule 9(b) because “[r]equiring specific facts that back up a conclusory allegation of wrongdoing is the very definition of particularized pleading.”).
\item \textsuperscript{224} See \textit{McAdams v. McCord}, 584 F.3d 1115 (8th Cir. 2009) (describing how missing facts affected the plausibility of the allegations).
\item \textsuperscript{225} \textit{Id.}
\item \textsuperscript{226} \textit{Id. at 1114.}
\item \textsuperscript{227} \textit{Id. at 1114–15.}
\item \textsuperscript{228} \textit{Id. at 1115.}
\item \textsuperscript{229} \textit{Id.}
\item \textsuperscript{230} \textit{Id.; see also Bone, supra note 67, at 864 (explaining that the distinction between legal conclusion and factual assertion is a matter of particularity because statements of fact “pitched at too high a level of generality” can so easily be interpreted as legal conclusions).}
\item \textsuperscript{231} See \textit{Ashcroft v. \textit{Iqbal}}, 129 S. Ct. 1937, 1949–50 (2009) (clarifying that while Rule 8(a)(2) might have relaxed the older system of code-pleading, it did not loosen the standard so much as to allow a plaintiff to proceed only on conclusions, and further, that plausibility is required to survive a motion to dismiss).
\end{itemize}
\end{footnotesize}
2. **Pleading loss causation under the second prong of the Iqbal analysis is particularly difficult due to the complex nature of securities fraud claims**

The plausibility analysis under Iqbal’s second prong may pose a particularly challenging standard in the loss causation context. This is due to two factors: as a matter of logic, even if a claim is sufficiently particular, it does not guarantee that it will be sufficiently plausible; and, even assuming that a claim could be said to be “plausible” in isolation, the Supreme Court, in other contexts, has indicated a willingness to engage in a type of “plausibility in light of the alternatives” analysis where it could look to alternative explanations of causation that are determined to be more plausible than the plaintiff’s theory.\(^\text{232}\)

The Supreme Court called Rule 8(a)(2)’s pleading requirements “less rigid” than a heightened pleading standard,\(^\text{233}\) but it is not clear that the Iqbal gloss on Rule 8(a)(2) ensures that it remains “less rigid” than Rule 9(b) in all situations.\(^\text{234}\) Regardless of what the Court claims is more or less rigid, as a matter of logic, it seems nearly impossible (or at least “implausible”) to advance a plausible claim if it is not sufficiently particular.\(^\text{235}\) Indeed, it would be difficult to find a claim plausible if that claim did not also state particularities such that they would “nudge [the claim] . . . across the line from conceivable to plausible.”\(^\text{236}\)

While particularity may be necessary to stating a plausible claim, it is unlikely to be sufficient. A claim can be adequately particular so as to avoid being conclusory under Iqbal’s first prong, but, for some other reason, that claim is not sufficiently plausible under the second prong. Moreover, in a loss causation context, the factual posture is generally such that multiple factors potentially contribute to an individual’s loss, thereby augmenting the difficulty already inherent in the fact that pleading

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232. *See id.* at 1951 (concluding that there was an “obvious alternative explanation” to the plaintiff’s theory of liability) (citing Bell Atl. Corp. v. Twombly, 550 U.S. 554, 567 (2007) where the Court also found an “obvious alternative explanation” to plaintiff’s claim); cf. Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 324 (2007) (requiring that properly pleading the element of scienter must be “strong in light of other explanations . . . and at least as compelling as any [plausible] opposing inference one could draw from the facts alleged”).


234. *See Bone, supra* note 67, at 870–79 (disapproving of equating *Iqbal* and *Twombly* where *Iqbal*’s thick-screening approach eliminates weak suits while *Twombly*’s thin-screening approach accepts weaker suits that at least suggest that “something fishy might be going on”); *Spencer, supra* note 27, at 473–74 (equating plausibility pleading and heightened particularity pleading).


236. *Iqbal*, 129 S. Ct. at 1952 (internal quotations omitted).
particularity does not ensure plausibility as a matter of logic.\textsuperscript{237} Accordingly, it may be difficult to isolate a material misstatement or omission as the cause of an economic loss if other economic factors also contributed to that loss.\textsuperscript{238} Thus, even if a plaintiff could satisfy both particularity and initial plausibility, the claim still may not be plausible in light of alternative explanations.\textsuperscript{239}

Looking at the Supreme Court’s reasoning in a securities fraud case dealing with the element of scienter, \textit{Tellabs Inc. v. Makor Issues and Rights, Ltd.},\textsuperscript{240} it may be that a plaintiff’s pleading of loss causation must not only be plausible, but at least as plausible as reasonable alternatives.\textsuperscript{241} Indeed, there is support for this approach in both \textit{Twombly} and \textit{Iqbal}.\textsuperscript{242} While the \textit{Iqbal} Court does not go so far as to hold that “plausibility” must be determined in light of plausible alternatives, in dismissing his complaint, the Court relied heavily on the notion that Iqbal’s claim was unlikely, and certainly not plausible in light of “obvious alternative explanations.”\textsuperscript{243}

\textsuperscript{237} See Fisch, \textit{supra} note 30, at 820–21, 845–46 (noting that a loss causation analysis is particularly difficult in the securities fraud context because of the myriad factors that can affect the valuation of a security).

\textsuperscript{238} See, e.g., Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 342–43 (2005) (observing that the link between share purchase price and consequent economic loss is not always strong because there are a “tangle of factors affecting price”); see also Fisch, \textit{supra} note 30, at 821 (noting that loss causation analysis can depend on how a plaintiff’s loss is measured, testimony of expert witnesses, and timing of price changes).

\textsuperscript{239} The concept of “negative causation” provides some guidance here. It does not go to a defendant’s liability, but it provides the defendant with an affirmative defense in the assessment of damages where the defendant can point to other factors that contributed to a plaintiff’s loss. It is a mitigation of damages scheme, and although it does not go to liability, it shows that the idea that “alternative” causes can factor into a plaintiff’s loss and that a defendant should not bear the full burden of liability in such circumstances is a well-understood concept in securities law. See Securities Act of 1933 § 11, 15 U.S.C. § 77k (2006) (allowing, for the purposes of mitigation of damages, a “negative causation” affirmative defense in which a defendant offers alternative explanations for the plaintiff’s loss).

\textsuperscript{240} 551 U.S. 308 (2007).

\textsuperscript{241} See \textit{id.} at 323–24 (“To determine whether the plaintiff has alleged facts that give rise to the requisite ‘strong inference’ of scienter, a court must consider plausible, nonculpable explanations . . . as well as inferences favoring the plaintiff . . . [that] must be more than merely ‘reasonable’ or ‘permissible’—it must be cogent and compelling, thus strong in light of other explanations.”).

\textsuperscript{242} See Ashcroft v. Iqbal, 129 S. Ct. 1937, 1951–52 (2009) (stating that “[a]s between that ‘obvious alternative explanation’ for the arrests [that the plaintiff had been arrested not because of his religion or race, but because he was part of a class of individuals who made an attack on the United States], and the purposeful, invidious discrimination respondent asks us to infer, discrimination is not a plausible conclusion.” (citing Bell Atl. Corp. v. Twombly, 550 U.S. 544, 567(2007))). This suggests that the Court may be willing to look to its seminal pleading case to find support for transporting a “plausible in light of alternatives,” \textit{Tellabs}-type of analysis into the Rule 8(a)(2) plausibility test.

\textsuperscript{243} See \textit{Iqbal}, 129 S. Ct. at 1951–52 (rejecting the plaintiffs’ allegations of discrimination in light of the Court’s conclusion that a national security policy of detaining individuals with suspected links to terrorism would naturally have a disparate effect on Arab Muslims and therefore provides a more plausible explanation for plaintiff’s detention).
This at least opens the door for a “plausibility in light of the alternative” style of analysis. The Fourth Circuit’s decision in *In re Mutual Funds Investment Litigation* (a case decided under the particularity standard of Rule 9(b)) provides an apt example.244 There, the plaintiffs provided detailed factual allegations regarding: (1) misstatements in the prospectuses of defendant Janus Capital Group, Inc.; (2) subsequent disclosure that the statements were false; (3) the payment of fines for the false statements, and; (4) the ensuing decline in share price.245 The court concluded that these allegations were a “substantial cause” in the decrease in share price and allowed the plaintiff to clear the particularity hurdle of Rule 9(b)’s heightened pleading.246 While these facts were sufficiently particular for the court to find them to be a “substantial cause” of the plaintiffs’ injury, a “substantial cause” of some injury does not necessarily mean that it is the *most plausible* cause of the injury in light of alternate plausible explanations.247 As the *Dura* Court alluded to, in a typical securities fraud context, it is plausible that a myriad of other factors such as lower earnings than expected, poor performance in a particular market sector, a decrease in general consumer demand in China, or an act of God halfway across the world could provide *more* plausible explanations for what “caused” a given loss.248 As discussed earlier, determining the exact cause of some event is a difficult endeavor, but even determining an event’s most plausible cause is not much easier, particularly in the securities fraud context.249 In such a situation, a plaintiff may be able to plead sufficient factual particularity to meet the requirements of Rule 9(b)’s particularity standard and even the first prong of *Iqbal*’s conclusory analysis under Rule 8(a)(2), yet still fail to meet the second prong of *Iqbal*’s analysis either because the factual pleading is not plausible, or is not plausible in light of alternate plausible explanations.250

244. *In re Mutual Funds Investment Litigation* 566 F.3d 111, 119 (4th Cir. 2009).
245. *Id.* at 128–29.
246. *Id.* at 128.
247. *See id.* (maintaining that allegations do not have to conclusively show that an injury is caused solely by one action, only that it was a substantial cause).
248. *See Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 342–43 (2005) (noting that in a loss causation context, a loss is susceptible to multiple and intervening factors); *Law v. Medco Research, Inc.*, 113 F.3d 781, 786–87 (7th Cir. 1997) (dismissing for failure to state loss causation after finding no ground to doubt causation when plaintiffs failed to respond to defendant’s studies showing that because defendant’s share price moved in tandem with competitors’ share price, market forces created plaintiff’s loss); *see also* Fisch, *supra* note 30, at 840 (highlighting the difficulty of showing loss causation because of the many factors that can affect the value of a securities investment).
249. *See supra* note 237 and accompanying text.
250. *See supra* notes 240–43 and accompanying text.
C. As a Policy Matter, Pleading Loss Causation under Iqbal’s Construction of Rule 8(a)(2), Combined with the Strict Pleading Requirements for the other Elements of a Private Securities Fraud Claim, Suggests that a Plaintiff Will Face a Substantial Barrier in Accessing Judicial Redress

As a matter of congressional intent, requiring the element of loss causation to be pled under a heightened standard is in line with Congress’s desire to curb abusive litigation practices in private securities fraud claims.251 Pleading under Iqbal’s plausibility standard, however, may present policy concerns about a plaintiff’s access to judicial remedy for loss resulting from securities fraud.252 Placing the issue of pleading loss causation within the broader context of pleading a private securities fraud claim suggests that the heightened pleading standard may be too strong.

The entire pleading scheme for a private securities fraud claim operates under a heightened standard. For example, section 21D(b)(2) of the Exchange Act sets out the heightened pleading standard for the state of mind element of scienter.253 A plaintiff must state factual particularity that creates a strong inference that the defendant acted with scienter.254 The Supreme Court has since interpreted “strong inference” to be more than simply what is reasonable; it must be at least as likely as reasonable alternative inferences.255

When considering the combination of the PSLRA particularity pleading requirements for the misstatement or material omission elements,256 the Tellabs “strong inference” requirement for scienter257, and the application of Iqbal’s formulation of plausibility to the remaining elements, including loss causation,258 the plaintiff faces a significant burden in putting forward


252. See supra note 199 and accompanying text (discussing the challenges presented by a heightened pleading standard).


254. Id.


257. Id.

258. See Ashcroft v. Iqbal, 129 S. Ct. 1937, 1949–50 (2009) (clarifying that while Rule 8(a)(2) might have relaxed the older system of code-pleading, it did not loosen the standard so much as to allow a plaintiff to proceed only on conclusions, and further, that plausibility is required to survive a motion to dismiss).
facts that can clear all of these procedural hurdles. Ultimately, there may be legitimate concerns regarding system accessibility. The more difficult that it becomes to adequately plead a private securities fraud claim, the less likely an investor with a meritorious claim will be able to recover his losses absent a clearly compelling case and the financial means to weather a storm of motions to dismiss.\footnote{259}{See Spencer, supra note 27, at 471 (recognizing the irony that a plaintiff will often be unable to plead a plausible claim absent discovery to key information necessary to do so).} Pleading loss causation under the \textit{Iqbal} plausibility gloss on Rule 8(a)(2), while perhaps jurisprudentially consistent with the intentions of the PSLRA, only serves to augment the concern about system accessibility.

\section*{Conclusion}

The current economic climate suggests that a steady stream of private securities fraud claims should enter the court system in the near term. Understanding the proper pleading standard for the element of loss causation will be pivotal for a plaintiff bringing a claim if he is to avoid dismissal. Although the general pleading standard under Rule 8(a)(2) is the proper pleading standard for the element of loss causation, it is likely a difficult standard for a plaintiff to meet in light of \textit{Iqbal}’s new, formal two-prong approach.\footnote{260}{See discussion supra Part II.B.}

Several factors suggest that Rule 8(a)(2) is the proper pleading standard for loss causation. While the Supreme Court did not formally adopt Rule 8(a)(2) as the pleading standard to govern loss causation in \textit{Dura}, it clearly assumed it as the standard in dismissing a claim for insufficiently pleading the element of loss causation. Additionally, \textit{Dura} begins a fairly clear line of progression in the development of the plausibility pleading under Rule 8(a)(2) that is further refined in \textit{Twombly} and \textit{Iqbal}. The fact that the Supreme Court cited \textit{Dura}, a loss causation case, in \textit{Twombly} and \textit{Iqbal} as a source of the current plausibility standard shows that \textit{Dura} was an integral case in the development of the Court’s plausibility pleading jurisprudence and strongly suggests that the Court would apply Rule 8(a)(2) to future loss causation cases. Moreover, analogies to the elements of common law fraud and the element of proximate cause in the tort context reinforce the conclusion that, notwithstanding the fact that Rule 9(b) generally governs the pleading standard for elements of a fraud claim, Rule 8(a)(2) is the proper pleading standard.

However, properly pleading the element of loss causation may prove to be particularly difficult under the \textit{Iqbal} plausibility construction of Rule...
8(a)(2). *Iqbal*’s formal two-prong approach entails requirements of both particularity and plausibility, and possibly even “plausibility in light of other reasonable alternatives.” To meet *Iqbal*’s first prong—avoiding conclusory statements—a plaintiff will need to plead factual particularity. To meet *Iqbal*’s second prong, the plausibility requirement, a plaintiff will need to plead a factual description of events that are not only sufficiently particular to satisfy the first prong, but also sufficiently plausible, and perhaps even the most plausible description of events among reasonable alternatives. This pleading scheme suggests a substantial burden for the plaintiff to carry at the pleadings stage. Moreover, considering pleading the element of loss causation within the context of the broader private securities fraud claim and the heightened requirements therein, policy concerns arise regarding a plaintiff’s ability to access judicial remedy for loss. The cumulative effect is that there will likely be many cases where a plaintiff with a meritorious, detailed, but not clear-cut private securities fraud claim, will ultimately find himself pleading a lost cause.

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261. *See discussion supra* Part II.B.


263. *See supra* Part II.B.2.