Securities Regulation Daily Wrap Up, FRAUD AND MANIPULATION—2d Cir.: Injection of damages testimony revives Celebrex suit against Pfizer, (Apr. 12, 2016)

Securities Regulation Daily Wrap Up

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By John M. Jascob, J.D., LL.M.

The Second Circuit has reversed a grant of summary judgment to Pfizer, Inc. and several officers and directors for alleged misrepresentations concerning the risks posed by the company's anti-inflammatory drugs, Celebrex and Bextra. The district court erred by entirely excluding testimony by the plaintiffs' expert concerning loss causation and damages on the grounds that the expert failed to disaggregate the impact of Pfizer's misrepresentations from those of two other companies. In addition, the expert's failure to account for his methodology in making offsetting adjustments for two disclosure events previously excluded by the court did not render the remainder of his testimony unreliable (*In re Pfizer Inc. Securities Litigation*, April 12, 2016, Livingston, D.).

Loss causation and damages. In 2004, the plaintiffs filed a purported class action suit against Pfizer, claiming that the company violated the anti-fraud provisions of the Exchange Act by misrepresenting the cardiovascular risks associated with Celebrex and Bextra. After nearly a decade of litigation, the Southern District of New York granted the defendants' motion to exclude testimony on loss causation and damages by the plaintiffs' expert, renowned former law professor Daniel R. Fischel. The district court ruled that Fischel's report concerning the stock price inflation caused by the alleged misrepresentations would not be helpful to the jury because it failed to isolate the effects of Pfizer's conduct from the effects of certain allegedly fraudulent statements made by G.D. Searle & Co. and Pharmacia Corporation, the two companies that had manufactured and owned Celebrex and Bextra prior to Pfizer.

In addition, Fischel had calculated the alleged price inflation by means of an event study which identified days on which Pfizer's stock price fell when the market discovered allegedly concealed information about Celebrex and Bextra and days on which Pfizer's stock price rose in reaction to new information about the drugs. When the district court determined that the stock price declines on two days in Fischel's event study could not reasonably be attributed to Pfizer's alleged fraud, Fischel removed those days from his analysis and adjusted his calculations. The court concluded, however, that Fischel's methodology for adjusting the amount of price increases attributable to Pfizer was not "the product of reliable principles and methods reliably applied." The exclusion of Fischel's testimony left the plaintiffs unable to sustain the loss causation and damages elements of their claims, and the district court granted Pfizer's motion for summary judgment.

Inflation maintenance. On appeal, however, the Second Circuit held that the district court abused its discretion by excluding Fischel's testimony in its entirety on the grounds that he failed to disaggregate the impact of Pfizer's misrepresentations. Under the plaintiffs' "inflation-maintenance" theory of the case, all three companies engaged in fraudulent misrepresentations and omissions that concealed the same information concerning the increased risk of cardiovascular problems. By fraudulently concealing the same risks that Pharmacia and Searle hid, the plaintiffs argued, Pfizer perpetuated the market's misperceptions about Celebrex and Bextra, thus maintaining the company's stock price at an artificially high level.

Even assuming that Pfizer lacked sufficient authority over several of the Searle and Pharmacia statements, this would not require Fischel to disaggregate the effects of Pfizer's conduct from that of the other companies in order to help the jury calculate the amount of losses that Pfizer allegedly caused, the appellate court reasoned. Rather, Pfizer would be liable for all of the artificial inflation related to Celebrex and Bextra under the inflation-maintenance theory because, through its own fraudulent conduct, Pfizer concealed the same information as its

predecessors. In the context of that theory, Fischel's testimony could be helpful to the jury because it showed that the discovery of information Pfizer allegedly concealed caused shareholders to lose money and calculated the amount of money they lost.

The Second Circuit emphasized that it was not deciding whether the plaintiffs' inflation-maintenance theory was either legally or factually sustainable. The panel observed that the inflation-maintenance theory may prove to be legally deficient under Rule 10b-5 or that, even under such a theory, the plaintiffs cannot establish that Pfizer concealed the same information as Searle and Pharmacia hid. Nevertheless, this would not provide a justification for concluding that, in the context of the plaintiffs' theory of the case, Fischel's testimony would be unreliable or unhelpful.

Proportional reduction. Next, the appellate court turned to the district court's holding that Fischel's report concerning the stock price inflation caused by the alleged misrepresentations failed to account for his methodology in making offsetting adjustments for two disclosure events previously excluded by the court. Although the district court did not abuse its discretion in concluding that Fischel failed to adequately explain his proportional adjustment, that failure was not a basis for excluding his testimony in its entirety. Instead, the district court should have prevented Fischel from testifying about the proportional reduction while still permitting him to offer his opinion about loss causation and damages, the appellate court stated.

Fischel's proportional reduction was but one small part of an extensive economic analysis, the panel noted. Eliminating the proportional reduction did not render the remainder of his analysis useless, but instead merely insured the adoption of the most conservative estimate of the losses Pfizer allegedly caused. As the remainder of Fischel's testimony rested on a reliable foundation and was relevant, excluding his testimony in the entirety was an abuse of discretion.

The case is No. 14-2853-cv.

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Companies: Teachers' Retirement System of Louisiana; Pfizer, Inc.

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