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## In Victory for WLF, First Circuit Cracks Down on “Fraud by Hindsight” Securities Law Claims

*(In re: Genzyme Corp. Securities Litigation)*

**“Frivolous securities litigation will plague the business community unless courts are willing to weed out lawsuits like this one before defendants must respond to expensive and time-consuming discovery requests.”**

**—Rich Samp, WLF Chief Counsel**

WASHINGTON, DC—The U.S. Court of Appeals for the First Circuit yesterday dismissed a securities fraud lawsuit against a biologics manufacturer alleged to have defrauded investors by failing to disclose potentially unfavorable business developments. The decision handed a victory to Washington Legal Foundation (WLF), which filed a brief urging the court to crack down on “fraud by hindsight”—claims inferring early knowledge of adverse events based on a mere allegation that a company “must have known” in advance those events were bound to happen.

The First Circuit said a § 10(b) securities fraud complaint must include allegations that give rise to a “strong inference” of scienter (*i.e.*, an intent to deceive). The appeals court agreed with WLF that a complaint cannot reach that “strong inference” threshold by alleging the defendant did not disclose every piece of potentially adverse information, particularly where, as here, there was little reason to conclude the information would materially impact company earnings.

The lawsuit alleged Genzyme Corp. failed to alert shareholders in time that Food and Drug Administration employees, during an October 2008 inspection, had observed 16 deficiencies in Genzyme’s manufacturing practices at its largest facility. The company’s share price dropped after it timely disclosed a Warning Letter (in March 2009) and then a significant enforcement action (in late 2009) based on alleged noncompliance with “good manufacturing practices.” The appeals court affirmed dismissal of the complaint, concluding the most reasonable inference was that Genzyme delayed disclosing the earlier observations for five months because it reasonably believed they would not lead to an enforcement action materially affecting company earnings.

In response to the decision, WLF issued the following statement by Chief Counsel Rich Samp: “The appeals court’s decision is faithful to Congress’s 1995 law designed to encourage early dismissal of insubstantial securities fraud lawsuits. Frivolous securities litigation will plague the business community unless the courts are willing to weed out lawsuits like this one before defendants must respond to expensive and time-consuming discovery requests. Public companies should not be held liable for good-faith, forward-looking statements solely because their predictions of future events ultimately prove to be inaccurate.”

*WLF is a public interest law firm and policy center that regularly litigates in support of civil justice reform, to ensure that unwarranted lawsuits do not drive up costs for all consumers.*

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