



## **Gutting the Loss Causation Requirement in Securities Class Actions: 5th Circuit Holds that Insufficient Partial Disclosures May Together Sufficiently Plead Loss Causation**

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Reading Time : **4 min**

### **Background**

Amedysis is a home health care services company that assists chronically ill patients. Plaintiffs allege that during the class period, Amedisys defrauded investors by concealing a Medicare fraud scheme. Plaintiffs allege five partial disclosures:

- August 12, 2008, report from a research firm raising questions about Amedysis's Medicare billing practices
- September 3, 2009, announcement of the resignation of the company's CEO and CIO
- April 26, 2010, *Wall Street Journal* article by a professor analyzing publically available Medicare reimbursement data and finding that Amedisys might be "taking advantage of the Medicare reimbursement system"
- May 12, 2010, June 30, 2010, and September 28, 2010, announcements that the Senate Finance Committee, the SEC, and the DOJ were investigating Amedisys
- July 12, 2010, announcement of disappointing operating results.

The district court dismissed plaintiffs' claims, finding that plaintiffs had failed to plead loss causation. The 5th Circuit, in an opinion written by Eastern District of Texas Judge Gilstrap sitting by designation, reversed, finding that the "whole is greater than the sum of its parts" and holding that together these partial disclosures satisfied the pleading requirements for loss causation.

The Court outlined the loss causation requirement: “the plaintiff must allege that when the ‘relevant truth’ about the fraud began to leak out or otherwise make its way into the marketplace, it caused the price of the stock to depreciate and, thereby, proximately caused the plaintiff’s economic harm.” The Court indicates that the “test for ‘relevant truth’ simply means that the truth disclosed must make the existence of the actionable fraud more probable than it would be without that alleged fact, taken as true.”

The Court then analyzed each of the five partial disclosures and found each one lacking by itself, but ultimately held that combined they sufficiently pled loss causation.

**Research Reports** – The Court found that the August 2008 research report, which specifically noted that it had not concluded that Amedisys was committing Medicare fraud, did not make the existence of the actionable fraud more probable than not. But then, the Court held that “it must be considered within the totality of all such partial disclosures.” This is a significant finding because it takes the corrective disclosures back **two years** from the end of the class period, when the stock price was trading at \$66.07. The next disclosure was a year later, when the stock price was trading at \$43.46.

**Corporate Resignations** – More than a year after the August 2008 research report was released, Amedisys’s COO and CIO left to “pursue other interests” and the stock price declined. There is nothing in the press release that links the resignations to the alleged Medicare fraud. The 5th Circuit therefore found that there was nothing in the resignation that revealed the truth behind earlier alleged misstatements and that it “does not in and of itself constitute a corrective disclosure.” Nonetheless, the Court found that it “may constitute a portion of the totality that we must consider.” This holding is somewhat baffling, particularly where the loss causation standard requires them to eliminate other factors unrelated to the fraud. This seems to be precisely the type of other factor that should **disprove** loss causation, but the Court instead opted to include this as part of the alleged corrective disclosures.

**Publicly Available Information** – The April 2010 Wall Street Journal article had an analysis from an expert who used publicly available Medicare information. Defendants argued that since the Medicare information was previously publicly available, it should be considered confirmatory and could not be considered a corrective disclosure. The Court observed that “although a disclosure of mere confirmatory information will not cause a change in the stock price because the current price already reflects the information available, we find it plausible

that this information was not merely confirmatory.” The Court noted that “the raw data itself had little to no probative value in its native state.” This conclusion has implications for defendants on a going-forward basis, as it suggests that even previously publically available information may not be sufficient in certain cases to dispute loss causation.

**Government Investigations** – Securities class action defendants are frequently beset by government investigations. Most courts have held that the disclosure of such investigations are not considered corrective, since the investigation itself is not truth of an alleged fraud. The 5th Circuit in *Amedisys* held that though they do not, standing alone, amount to corrective disclosures, they may be considered “together with the totality of the other alleged partial disclosures.”

In sum, the 5th Circuit appears to have endorsed “leakage theory,” holding that “the truth can be gradually perceived in the marketplace through a series of partial disclosures.” The opinion does not address whether the partial disclosures themselves were statistically significant and whether that bears on the analysis. Instead, the Court combined the entire 63.6 percent decline from the first alleged curative disclosure to the end of the class period, to evaluate loss causation. Although this opinion could have far-reaching impact on securities class actions in the 5th Circuit, defense lawyers can take comfort that the Court made very clear that it was evaluating this under the plausibility standard of Rule 8 and that the evidentiary burden here (as opposed to the merits stage) is “much less stringent.” Regardless, this opinion appears to signal a brave new world for securities class actions.

## Categories

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