

No. 23-980

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IN THE  
*Supreme Court of the United States*

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FACEBOOK INC., et al.,

*Petitioners,*

v.

AMALGAMATED BANK, et al.,

*Respondents.*

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On Writ of Certiorari to the  
United States Court of Appeals for the Ninth Circuit

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**BRIEF OF FINANCIAL ECONOMISTS AS *AMICI*  
*CURIAE* SUPPORTING RESPONDENTS**

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**INTEREST OF THE AMICI CURIAE<sup>1</sup>**

*Amici curiae* are academic scholars and accomplished practitioners with leading experience and expertise in financial economics. All have contributed to and advanced the study of equities markets and specifically the impact of company disclosures on securities prices. Several provide expert testimony in securities cases and have appeared as *amici* before this Court in securities cases. They have an interest in the proper and efficient development of legal principles in this area and in promoting a legal regime that allows for well-functioning markets, which, as explained below, depend on reliable and complete disclosure and anti-fraud regimes.

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<sup>1</sup> No counsel for any party authored this brief in whole or in part. No person or entity other than *amici* and their counsel funded its preparation or submission.

## INTRODUCTION AND SUMMARY OF THE ARGUMENT

Petitioners in this case argue that statements by public companies about risks “make no implied representations about a company’s past experiences” and, in the alternative, that securities-fraud plaintiffs should be required to show that a warned-of risk *to the company’s business* was “almost certain to materialize” to state a claim based on a risk disclosure. Pet’r Br. 19, 39. Along the way, they argue that because the market, in Petitioners’ telling, already knew about the Cambridge Analytica misappropriation of user data from *The Guardian’s* reporting in 2015 before Facebook filed its 10-K risk disclosures, and because that initial article did not result in a stock-price decline, the full revelation of the truth could not have corrected a misleading disclosure even though the stock plummeted after the second disclosure. *E.g., id.* 28.

These arguments misunderstand how equities markets react to new information, a subject on which *amici* are leading experts. Facebook’s argument that statements about “risk” never imply anything about the past is wrong: Market participants typically interpret risk disclosures made without context and quantification to be addressing risks that may occur with uncertain probability, which some economists call “ambiguity,” not events that have already happened or are certain to occur. Risks to a company’s *business* can have a certain chance of affecting a company’s *stock price*, invalidating Facebook’s argument that investors may be misled only about something nearly certain to harm the company’s bottom line. And major changes in a stock’s price in

reaction to new value-relevant information in the absence of confounding effects are very good evidence that the market did not already know that information, refuting Facebook's continued assertions that the market already knew everything it needed to know before Facebook confirmed the data misappropriation.

Economists have characterized public companies' communications with the capital market as a "communication game with ambiguity-sensitive preferences" and they generally understand most markets incorporating such communications to be "efficient," in the sense that the market promptly incorporates new value-relevant information. Three properties of financial markets are important here: First, management knows more than the market does, a property economists call "information asymmetry." Second, market participants prefer certain outcomes to uncertain ones, a property economists call "risk aversion," and prefer known probabilities of uncertain outcomes to unknown ones, a property economists call "ambiguity aversion." Finally, the objectives of management and investors often do not align perfectly. Management generally wants to keep the company's stock price high, but market participants want as much accurate information as possible with which to value the company's securities. Economists call this mismatch "non-aligned incentives."

The markets for publicly traded equities exhibit these properties. And decades' worth of high-quality, peer-reviewed research shows that in capital markets with these properties accurate communication between participants is not possible without effective disclosure and anti-fraud rules in place. Those rules



thus benefit companies, management, and market participants alike—without them, companies and management could never effectively communicate with the market for their shares.

Petitioners and the dissent below attempt to muddle these concepts. When faced with ambiguity (“something may pose a risk to our business”), reasonable market participants typically distinguish it from risk (“there is a 50% chance a specific thing destroys our business”), and particularly from certainty (“the thing has already happened and is fully known”), and reasonably understand statements like the final two to add information to statements like the first. When faced with risk to a company’s business, market participants will promptly and certainly adjust the stock price in response to that additional information. And when that stock price adjusts in the absence of confounding factors, the adjustment provides very good evidence that market participants did not already know the information they just learned and that they found the new information material.

Petitioners’ arguments do not make economic sense, and this Court should affirm the judgment of the Ninth Circuit.

## ARGUMENT

### **I. Efficient Equities Markets React to Communications About Probabilistic Information.**

This Court has long recognized that “in an open and developed securities market, the price of a company’s stock is determined by the available material information regarding the company and its business.” *Basic Inc. v. Levinson*, 485 U.S. 224, 241

(1988) (quoting *Peil v. Speiser*, 806 F.2d 1154, 1160–61 (3rd Cir. 1986)). Information is “material” if it adds to the “total mix of information . . . made available” to the market. *Id.* at 231; see also *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 38 (2011). The Court chose this materiality standard to balance two competing goals: If, on the one hand, the materiality threshold were too low, then “management would ‘bury the shareholders in an avalanche of trivial information.’” *Id.* (quoting *Basic*, 485 U.S. at 231). If, on the other hand, the materiality threshold were too high, management would be free to withhold information that would “otherwise be considered significant to the trading decision of a reasonable investor.” *Basic*, 485 U.S. at 236.

The “total mix” standard requires that management disclose only information that would reasonably alter participants’ investment decisions. *Id.* And this Court’s caselaw thus incorporates the “efficient capital market hypothesis,” *id.* at 247 n.24, under which all information affecting the market’s judgment of the value of the company is promptly incorporated into the market prices of the company’s securities. See *Basic*, 485 U.S. at 247 n.24 (citing Roger J. Dennis, *Materiality And The Efficient Capital Market Model: A Recipe for The Total Mix*, 25 Wm. & Mary L. Rev. 373, 379 (1984)); see also *Halliburton Co. v. Erica P. John Fund, Inc.*, 573 U.S. 258, 272 (2014) (“Even the foremost critics of the efficient-capital-markets hypothesis acknowledge that public information generally affects stock prices.” (citing Robert J. Shiller, *We’ll Share the Honors, and Agree to Disagree*, N.Y. Times, Oct. 27, 2013, p. BU6 (“Of course, prices reflect available information.”))).

For equities markets to function properly, management must have a strong incentive to be truthful. The canonical illustration of what happens when participants in asymmetric-information markets are not required to make truthful disclosures is the market for used cars, as described in Nobel-prize-winning economist George Akerlof's *The Market For "Lemons."* See George Akerlof, *The Market For "Lemons": Quality Uncertainty And The Market Mechanism*, 84 Q.J. Econ. 488 (1970). In an unregulated market where sellers know information about goods that buyers do not know and cannot discover, both communication and trading may break down. Buyers begin with the background assumption that all goods are of average quality, and so they will offer only an average price. They then will reason that any seller who would accept an offer at the average price must be selling below-average goods, and so buyers do not buy at that price. Any seller who would sell at a lower price, of course, must be assumed to have even worse goods, and so on until no one buys or sells anything. *Id.* at 500. This market failure harms buyers and sellers alike—if buyers cannot safely credit sellers' representations about the quality of goods (cars, among other examples, in Akerlof's model) only those who own truly awful goods will be able to sell them, and at rock-bottom prices, harming all other would-be buyers and sellers.

Public-company shares differ from used cars and goods like them because the information relevant to their value is ever-changing and complex. But just like in the market for most goods, in the market for public-company stock, the buyers and sellers are often at cross purposes: Market participants want complete and accurate disclosures, but management wants to

keep prices up. *E.g.*, *Matrixx*, 563 U.S. at 49 (noting that management may withhold adverse documents because it “under[stands] their likely effect on the market”).

Unlike in many other markets, however, investors in public-company stock care not only about the current state of the company in which they are investing but also about its plans for the future. And so public-company executives often communicate with the market through probabilistic statements. *E.g.*, *Asher v. Baxter Int’l Inc.*, 377 F.3d 727, 733 (7th Cir. 2004) (Easterbrook, J.) (explaining forward-looking management statements and rejecting conclusion that “any issuer could list its lines of business, say ‘we could have problems in any of these,’ and avoid liability for statements implying that no such problems were on the horizon even if a precipice was in sight”).

Economists generally distinguish between two sorts of uncertainty that may exist about a statement. First, the speaker may be unsure whether something is true but has a good way of estimating whether it is or will be, as when someone says “there’s a one-in-36 chance of rolling boxcars” when playing dice. The speaker does not know whether boxcars—that is, a pair of sixes—will be rolled but does know the probability that this will happen. This is an example of “risk.” Risk does not exist absent uncertainty—where something is certain to happen or has already happened and is known, “risk” does not obtain. No one says “there is a one-in-36 chance I will have rolled boxcars” when two dice are currently showing sixes *and the speaker knows the result*. At that point, probabilistic language implies that the speaker is ignorant of the result and so knows only probabilities.

Second, the speaker may be unsure of whether something is true and also lack a good way to estimate whether it is or will be, as when someone says “humans may someday walk on Mars”: The speaker knows that the probability of humans walking on Mars is greater than zero and lower than one but does not know anything about where it falls in that range. This is an example of what is often called “ambiguity.” Most rational market participants are both risk- and ambiguity-averse, preferring certain outcomes to uncertain ones (most would prefer a certain payment of \$.027 over a one-in-thirty-six chance of winning a dollar for rolling boxcars), and preferring known probabilities to unknown ones (most would prefer to play dice in a regulated casino over playing a sidewalk shell game with unclear rules and odds).

When management speaks to the market it does so in the context of asymmetric information, ambiguous information, and non-aligned interests. Economic scholarship has shown that communication will break down in markets like this if there is not a strong disclosure and accuracy regime. *E.g.*, Phillippe Colo, *Communicating About Confidence: Cheap Talk With an Ambiguity-Averse Receiver*, *Am. Econ. J.: Microeconomics*, Aug. 2023, at 45; Vincent P. Crawford & Joel Sobel, *Strategic Information Transmission*, 50 *Econometrica* 1431 (1982). Just like in the market for used cars, where only lemons get sold without assurances of truthfulness and disclosure, trading in public markets will break down absent assurances of truthfulness and disclosure.

Two legal mechanisms prevent a market failure caused by asymmetric information and unaligned incentives from happening in the public-capital

markets: disclosure rules and anti-fraud rules. Although anti-fraud rules alone “do not create an affirmative duty to disclose any and all material information,” *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, 601 U.S. 257, 264 (2024) (citation omitted), mandatory disclosure rules create an obligation periodically to communicate with the market, *e.g.*, 17 C.F.R. § 229.105 (requiring “under the caption ‘Risk Factors’ a discussion of the material factors that make an investment in the registrant or offering speculative or risky”). And all communications, mandatory or otherwise, must be genuinely accurate—both literally true and free from materially misleading elements and omissions. *E.g.*, 17 C.F.R. § 240.10b-5 (making it unlawful to “make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading”).

Although these legal rules may prompt short-term unhappiness among company management, the rules are essential to management’s long-term functioning. Without the rules, management would be stuck in a market for corporate lemons. If the market cannot trust what management says, the market would rationally assume the worst, foreclosing investment and capital raising. *See, e.g.*, Colo, *supra*, at 48. Temporary incidents of such communication breakdowns in which markets cease to function are sometimes referred to by economists as “asymmetric information-induced financial crises.” *See, e.g.*, Charles W. Calomiris & Joseph R. Mason, *Contagion And Bank Failures During The Great Depression: The June 1932 Chicago Banking Panic*, 87 *Am. Econ. Rev.* 863 (1997).

The Chicago banking panic of 1932, discussed in *amici*'s scholarship, provides a “quintessential example of an asymmetric-information-induced panic.” *Id.* at 865. By 1932, many Chicago banks held as assets a substantial amount of municipal “tax warrants,” which were essentially City of Chicago IOUs, that banks had received as deposits because the city could not otherwise pay its bills in cash. As the city's economic situation worsened, so did its banks'. *Id.* Depositors thus began to worry about the safety of their funds and withdrew *en masse*. *Id.* at 866. But—and this is the crucial point—because depositors could not tell which banks had large balances of the distressed IOUs and which did not, depositors ran on nearly *all* Chicago's banks, *id.* at 867, even those that were later revealed to be solvent, *id.* The market for bank stocks plummeted across the board. *Id.*

In the absence of an effective disclosure and anti-fraud regime, if a Chicago banker in 1932 said “don't worry, we're not exposed to the City's credit risk,” no one could credibly rely on that statement. *See, e.g.,* Colo, *supra* at 48. And because the market would therefore have no way to distinguish the solvent banks from the insolvent ones, all banks would suffer. This is why the securities laws do not allow insiders to say whatever they wish without consequence. Instead, they are forbidden to mislead the market, *e.g.,* 17 C.F.R. § 240.10b-5, and required periodically to disclose all “material factors that make an investment . . . speculative or risky,” 17 C.F.R. § 229.105.

## **II. Reasonable Market Participants Understand “Risks” To Be *Uncertain* Harms.**

Petitioners and the dissent below mix up certainty,

risk, and ambiguity and misunderstand how investors typically process ambiguous, risky, and certain information. According to Petitioners

A reasonable investor reading a risk disclosure required by Item 105 would understand the statement to advise only about the possibility of a risk that may affect the company in the future. The reasonable investor would not interpret such a statement as implicitly asserting that the triggering event identified had not occurred in the past and that no such occurrence created a present risk of harm to the company.

Pet'r Br. at 21. Similarly, the dissent below reasoned that Facebook's statements regarding "risk" of "harm" that may befall the company if "the public or government learn about improper access to its data" "do not represent that Facebook was free of significant breaches at the time of the filing." Pet'r App'x at 44a. Not so.

As economic scholarship shows, reasonable market participants distinguish among events that are known to have occurred, known risks, and unknown risks—that is between "certainties," "risks," and "ambiguities." *See Colo, supra*. This is because reasonable market participants care a great deal about the difference between risks, which they may be able to easily evaluate and hedge against, and ambiguities, whose effects are generally harder to evaluate. *See, e.g., Asher, 377 F.3d at 733* (rejecting conclusion that "any issuer could list its lines of business, say 'we could have problems in any of these,' and avoid liability for statements implying that no such problems were on



the horizon even if a precipice was in sight”). The distinction market participants draw between risks and ambiguities is stronger still with respect to incidents that have already happened and are known, as is the case here.

Consider again the Chicago panic of 1932. If a bank relied on City of Chicago IOUs for its solvency, in a regime with strong anti-fraud rules the statement “we may be subject to counterparty credit risk” would have a dramatically different effect on the market for bank stocks than “City of Chicago IOUs represent 60% of the assets on our balance sheet.” *See generally*, Calormiris & Mason, *supra*. This is all the more true where, as here, the “risk” underlying those IOUs had *already materialized*, as would be the case if the City had just declared its intent to default on the notes. Petitioners and the dissent below are thus incorrect to suggest that statements about “risk” never imply that the “risk” has not materialized in the past and presents only a risk of future harm.

Partially in response to this point, Petitioners argue that the Ninth Circuit’s rule threatens to require firms to issue prolix reports, ultimately harming price discovery, falsely worrying that “[t]he Ninth Circuit’s approach would cause risk disclosures to balloon in length” and therefore ultimately harm market participants. Pet’r Br. at 33. Petitioners misunderstand the resources market participants deploy to analyze public-company statements and overlook economic research on the subject. Economic research has shown that for actively traded securities like Facebook stock a very large and very diligent system of analysts at “sell side” investment firms can facilitate the market’s processing of a large amount of

information. See, e.g., Reuven Lehavy, *et al.*, *The Effect of Annual Report Readability on Analyst Following And The Properties of Their Earnings Forecasts*, 86 *Accounting Rev.* 1087, 1089 (2011) (testing and validating the hypothesis that where firms' 10K reports become more difficult to read by standard measures of readability analyst coverage at sell-side firms increases, which the authors conclude to be "consistent with a greater collective effort by analysts for firms with less readable disclosures"). The infrastructure of well-developed capital markets is capable of processing copious and complex information. In fact, equity analysts and investors regularly request more information from companies, and rarely, if ever, ask for less. Petitioners' protestations to the contrary are without merit.

### **III. Petitioners Mistake "Business Harm" for Investor Loss.**

Petitioners and the dissent below conflate "business harm," which they seem to equate with harm to the company's cash flows, with harm to the company's *stock price*, which is closely related to the legal concept of materiality. Petitioners argue in the alternative (when discussing the "virtually certain" standard) that "the only way that [Facebook]'s risk disclosures could be misleading under the 'virtual certainty' standard is if [Facebook] knew that Cambridge Analytica's misuse of Facebook user data in 2015 in support of the Cruz campaign was virtually certain *to cause business harm* after February 2017." Pet'r Br. at 41 (emphasis added). Similarly, the dissent below reasoned that even if "Facebook . . . knew about breaches of its data—even potentially serious breaches—when it gave its risk statements, . . .

[Respondents] do not allege that Facebook knew that those breaches would lead to immediate harm *to its business or reputation*,” Pet’r App’x at 48a, and that their claims must be dismissed for this reason, *id.*

This conflation is a serious and fundamental mistake: Efficient equities markets promptly adjust to probabilistic information about cash flows. Even if the exact effect of the Cambridge Analytica scandal on Facebook’s future business was not both certain and prompt, the harm to Facebook’s *stock price* was certain and prompt.

This Court has long accepted the efficient capital-market principle, which “posits that the price of a security reflects all publicly available information about a firm.” Dennis, *supra*, at 379, *cited in Basic*, 485 U.S. at 247 n.24. This is true whether the information is deterministic (“an earthquake destroyed our plant”), probabilistic (“there is a 50% chance an earthquake will destroy our plant”), or ambiguous (“an earthquake may harm our business”). In an efficient market, when new *potential* harm to a company is revealed, the revelation is promptly incorporated into the company’s stock price. *See, e.g., Dennis, supra.*

Petitioners and the dissent below rely on a series of cases articulating what Petitioners call the “virtually certain” standard, under which a risk statement is false only if the risk was in fact a certainty or close to it. *See Indiana Public Retirement System v. Pluralsight, Inc.*, 45 F.4th 1236, 1256 (10th Cir. 2022); *Karth v. Keryx Biopharmaceuticals, Inc.*, 6 F.4th 123, 139 (1st Cir. 2021); *Set Capital LLC v. Credit Suisse Group AG*, 996 F.3d 64, 85–86 (2d Cir. 2021). Petitioners’ standard mistakes the likelihood of harm to a company’s business with the likelihood of harm to

its stock price. Although there is surely a relationship between these two concepts—a company whose business is harmed is worth less—they are not the same. As economic and legal scholarship shows, information can have a certain and immediately quantifiable effect on stock price while having a far-from-certain effect on the company’s business. *See generally, e.g.*, Matthew L. Mustokoff & Margaret E. Mazzeo, *Loss Causation on Trial in Rule 10b-5 Litigation a Decade After Dura*, 70 Rutgers L. Rev. 175 (2017). The risks to a company are material information that impacts the company’s stock price even if the adverse outcome of the risks may not materialize.

Accordingly, it does not make sense to distinguish between certain and uncertain harms to a company’s business when assessing the falsehood of a risk framed as a merely hypothetical prospect. Petitioners of course concede that they are forbidden to mislead the market, but seem to think the market simply cannot be misled about anything other than that which would be virtually certain to harm its cash flows. But a piece of information can be certain to harm a company’s stock price even if the effect on its cash flows is uncertain, and it is stock price that concerns investors, as this Court’s materiality cases make clear. *E.g.*, *Matrixx*, 563 U.S. at 42–44 (rejecting argument that pharmaceutical companies need only disclose “adverse event” reports that have reached a threshold of statistical significance because “[g]iven that medical professionals and regulators act on the basis of evidence of causation that is not statistically significant, it stands to reason that in certain cases reasonable investors would as well”). Even on Petitioners’ alternative argument this Court should

affirm the judgment of the Ninth Circuit.

#### **IV. The Impact of The Corrective Disclosure on Price Is Strong Evidence.**

Finally, Petitioners argue that “[t]he notion that [Facebook]’s statements were misleading is even more implausible in light of public reporting about . . . [t]he misuse of Facebook user data by Cambridge Analytica and the Cruz campaign [that] was publicly reported in 2015” because Facebook “experienced no drop in stock price or other material business harm” when this happened. Pet’r Br. 28.

This argument makes a simple but fundamental mistake about the efficient-capital-market principle, which this Court’s cases have long embraced. That Facebook’s stock price did not appear to drop after the first disclosures in 2015 but cratered after the revelation of the complete scandal in 2018 in the absence of any likely confounding factors proves the opposite of what Facebook argues. That is because in an efficient capital market, which the market for Facebook shares likely is, a large stock-price change after the revelation of information that cannot be explained by other factors is very strong—indeed nearly conclusive—evidence that the revealed information is new to the market. Dennis, *supra*, at 379, *cited in Basic*, 485 U.S. at 247 n.24. Petitioners’ argument that the market must have known the important part of the Cambridge Analytica scandal in 2015 appears belied by the subsequent change in its stock price.

**CONCLUSION**

This Court should affirm the judgment of the Ninth Circuit.

Respectfully submitted,

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