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Securities Law - How Strong Is Strong Enough: The Tellabs Court Lacked the Needed Strength for Pleading Scienter in Securities Fraud, Tellabs, Inc. v. Makor Issues & Rights, Ltd., 127 S.Ct. 2499 (2007)

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CASE NOTE

SECURITIES LAW — How Strong is Strong Enough?: The *Tellabs* Court Lacked the Needed Strength for Pleading Scienter in Securities Fraud; *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S. Ct. 2499 (2007).

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Introduction

Tellabs, Inc. (Tellabs), a publicly traded company, manufactures, and markets specialized optical networks, broadband access, and voice-quality enhancement equipment to telecommunications carriers and internet service providers globally.[1] Tellabs became another company of public notoriety when respondents (Shareholders), a group of Tellabs' stockholders, accused Tellabs and its chief executive officer (CEO), Richard Notebaert (Notebaert), of making false statements in an attempt to deceive investors about the actual value of Tellabs stock.[2]

Shareholders claimed Notebaert misled investors in multiple press releases by stating demand for Tellabs' "core optical products . . . remain[ed] strong," and Tellabs was on track to meet its revenue projections.[3] From December 11, 2000 until June 19, 2001, Shareholders alleged Notebaert consciously deluded the public in four ways.[4] First, Notebaert made statements indicating demand for Tellabs' core product, the TITAN 5500 ("5500"), continued to grow when demand actually fell.[5] Second, he made false statements that Tellabs' new product, the TITAN 6500 ("6500"), was available and in strong demand, when it was

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* Candidate for J.D., University of Wyoming, 2009. I would like to thank the entire Wyoming Law Review Board and Professor Gelb for their invaluable assistance with the editing and revising of this case note. I would also like to express my immeasurable love and gratitude to my parents for their unconditional love, support, guidance, and all the opportunities they have provided me. Finally, and most importantly, I would like to thank JC for everything He has provided me in my life. I owe everything to Him.

[1] Tellabs, Inc. v. Makor Issues & Rights, Ltd. (*Tellabs II*), 127 S. Ct. 2499, 2505 (2007); Makor Issues & Rights, Ltd., v. Tellabs, Inc. (*Tellabs I*), 437 F.3d 588, 591 (7th Cir. 2006); Brief for Petitioners at 3, Tellabs, Inc. v. Makor Issues & Rights, Ltd., 127 S. Ct. 2499 (2007) (No. 06-484), 2007 WL 432763; Brief for Respondents at 1, Tellabs, Inc. v. Makor Issues & Rights, Ltd., 127 S. Ct. 2499 (2007) (No. 06-484), 2007 WL 760412.

[2] *Tellabs II*, 127 S. Ct. at 2505; *Tellabs I*, 437 F.3d at 591. Shareholders accused several other executives including Tellabs' chairman and former CEO, Richard Birck (Birck). *Tellabs II*, 127 S. Ct. at 2505; *Tellabs I*, 437 F.3d at 591.

[3] *Tellabs I,* 437 F.3d at 592.

[4] *Tellabs II*, 127 S. Ct. at 2505.

[5] *Tellabs I*, 437 F.3d at 593. Tellabs core business founded itself on the TITAN 5500, Tellabs' flagship networking device. *Id.* at 596. "[I]n Tellabs 2000 Annual Report, published in February, 2001, Notebaert and Birck responded to a frequently asked question ('[A]re you worried that [the

not yet ready for delivery.[6] Third, Notebaert misrepresented Tellabs' financial outlook for the fourth-quarter of 2000 by fraudulently inflating the sales results.[7] Finally, he made multiple overstated earnings and revenue projections.[8] These misrepresentations, contended the Shareholders, resulted in the recommended buying of Tellabs' stock by market analysts.[9]

Evidence of the business struggling did not surface publicly until March 2001, when Tellabs reduced its first-quarter sales projections.[10] Downward projections continued on April 6, 2001, when Tellabs reduced its first-quarter projections for a second time.[11] On June 19, 2001, Notebaert informed investors that sales for the 5500 had dropped dramatically.[12] Once again, Tellabs reduced its sales projections, this time for the second-quarter as a result of the decreased demand for the 5500.[13] The following day, "the price of Tellabs stock, which had reached a high of $67 during the [class] period, plunged to a low of $15.87."[14]

TITAN 5500] has peaked?') by stating flatly, "No . . . . Although we introduced the product nearly 10 years ago, it's still going strong." *Id.* at 597. In addition, on March 8, 2001, a Deutsche Bank analyst asked Notebaert whether Tellabs was experiencing any reduction in TITAN 5500 sales. *Id.* "Notebaert responded: [W]e're still seeing that product continue to *maintain its growth rate*; it's still experiencing strong acceptance." *Id.*

[6] *Id.* The TITAN 6500 is Tellabs' next-generation networking device, designed to replace the TITAN 5500. *Id.* On December 11, 2000, Notebaert stated : "[T]he TITAN 6500 system is available now." *Id.* at 598. Additionally, "[o]n March 8, 2001, Notebaert told analysts, 'Interest in and demand for the 6500 continues to grow . . . . We continue to ship the . . . 6500 through the first quarter. We are satisfying very strong demand and growing customer demand.'" *Id.*

[7] *Tellabs I*, 437 F.3d at 593. Shareholders alleged Tellabs inflated its fourth-quarter results by channel stuffing, a process where the company produces false purchase orders and then sends customers products they never ordered. *Id.* at 598. "This practice . . . creates a short-term illusion of increased demand between the time when the company sends the extra product down the line and the time when the distributors return the unwanted excess." *Id.*

[8] *Id.* Tellabs reduced its first-quarter sales projections of $830 to $865 million to $772 million. *Id.* at 592-93. Tellabs also reduced its second-quarter revenue projection to $500 million from a previous projection of a range between $780 to $820 million. *Id.* at 593.

[9] *Id.* at 592; *see also Tellabs II*, 127 S. Ct. at 2505.

[10] *Tellabs I*, 437 F.3d at 592. Tellabs reduced its first-quarter sales projections from a range of $865 to $890 million to a range of $830 to $865 million. *Id.* Notebaert, however, attributed this reduction to poor growth in another division of the business and still made positive comments regarding demand for its networking products, specifically the TITAN 6500, and his belief that Tellabs would meet the adjusted projections. *Id.*

[11] *Id.* at 593. Tellabs reduced its first-quarter sales projections of $830 to $865 million to $772 million a month later. *Id.* Again, Notebaert reassured investors that demand for the 6500 was still strong, but customers pushing orders from the first-quarter to the second-quarter of 2001 resulted in a decreased projection of Tellabs' results. *Id.*

[12] *Tellabs II*, 127 S. Ct. at 2505.

[13] *Tellabs I*, 437 F.3d at 593. Tellabs reduced its second-quarter sales projections to $500 million from a previous projection of a range between $780 and $820 million. *Id.*

[14] *Tellabs II*, 127 S. Ct. at 2505. The class period is from December 11, 2000 until June 19, 2001. *Id.*

On December 3, 2002, the Shareholders filed their first complaint against Tellabs in the United States District Court for the Northern District of Illinois.[15] The complaint stated Tellabs and Notebaert committed securities fraud, violating § 10(b) of the Securities Exchange Act of 1934 and SEC rule 10b-5.[16] The district court granted Tellabs' motion to dismiss for failure to state a claim, without prejudice.[17] The district court found the Shareholders failed to plead their case with particularity as required by the Private Securities Litigation Reform Act of 1995 (PSLRA).[18] Additionally, the court found the Shareholders failed to meet the scienter requirement for a securities fraud pleading, "which requires that . . . [the defendant] likely intended 'to deceive, manipulate, or defraud.'"[19] On July 2, 2003, the Shareholders filed a second amended complaint; the district court dismissed the complaint with prejudice upon Tellabs' motion.[20] The district court found the Shareholders met the particularity pleading standard with respect to Notebaert's misleading statements.[21] These particular facts, however, failed to establish a "strong inference" of scienter, a requirement in a securities fraud pleading.[22]

The Shareholders appealed to the United States Court of Appeals for the Seventh Circuit claiming the district court erred in its judgment because "(1) some of the statements the court dismissed as 'mere puffery' [were] legally actionable; [and] (2) their complaint provided enough detail to support a strong inference of scienter for each of the defendants . . . ."[23] The Seventh Circuit affirmed in part and reversed in part.[24] The Seventh Circuit agreed with the district court

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[15] Johnson v. Tellabs, Inc., 303 F. Supp. 2d 941 (N.D. Ill. 2004).

[16] *Tellabs II*, 127 S. Ct. at 2505-06.

> Their complaint stated, *inter alia*, that Tellabs and Notebaert had engaged in securities fraud in violation of § 10(b) of the Securities Exchange Act of 1934, and SEC rule 10b-5, also that Notebaert was a 'controlling person' under § 20(a) of the 1934 Act, and therefore derivatively liable for the company's fraudulent acts.

Id. (citations omitted). The complaint also "allege[d] that Brick engaged in illegal insider trading in violation of § 20A of the Act." *Tellabs I*, 437 F.3d at 594 (citation omitted).

[17] *Johnson*, 262 F. Supp. 2d at 959.

[18] *Id.*; *Tellabs I*, 437 F.3d at 593.

[19] *Tellabs I*, 437 F.3d at 593 (quoting Ernst & Ernst v. Hochfelder, 425 U.S. 185, 194 n.12 (1976)).

[20] *Johnson*, 303 F. Supp. 2d at 971; *Tellabs II*, 127 S. Ct. at 2506; *Tellabs I*, 437 F.3d at 594. The district court found that Shareholders pled with particularity that Notebaert's statements were misleading but failed to show he acted with scienter. *Tellabs II*, 127 S. Ct. at 2506; *see also* Johnson v. Tellabs, Inc., 303 F. Supp. 2d 941 (N.D. Ill. 2004).

[21] *Johnson*, 303 F. Supp. 2d at 956-57; *Tellabs II*, 127 S. Ct. at 2506; *Tellabs I*, 437 F.3d at 594.

[22] *Johnson*, 303 F. Supp. 2d at 961, 969; *Tellabs II*, 127 S. Ct. at 2506.

[23] *Tellabs I*, 437 F.3d at 594.

[24] *Id.* at 605.

that the Shareholders had pled with particularity that Notebaert's statements were misleading.[25] The Seventh Circuit, however, used its reasonable person test, and overruled the district court finding the Shareholders adequately alleged a "strong inference" of scienter with respect to Notebaert's actions.[26]

The United States Supreme Court granted certiorari "to resolve the disagreement among the circuits on whether, and to what extent, a court must consider competing inferences in determining whether a securities fraud complaint gives rise to a 'strong inference' of scienter."[27] In an eight-to-one decision delivered by Justice Ginsburg, the Court held "[a] complaint will survive . . . only if a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged."[28] Thus, the Court vacated the Seventh Circuit's judgment, and remanded the case for further proceedings.[29]

This case note examines the evolution of the heightened pleading standard for securities fraud actions and the disagreement among the circuits in interpreting this standard.[30] First, it traces the heightened pleading standard for securities fraud up to *Tellabs*.[31] Next, it argues the Court developed an improper rule.[32] Additionally, it contends Justice Alito and Justice Scalia's concurrences proposed the proper standard for pleading requirements.[33] Finally, this case note discusses the impact the *Tellabs* decision will have on the Tenth Circuit in the future.[34]

BACKGROUND

Reacting to the market crash in 1929, Congress enacted two federal statutes to regulate securities transactions.[35] These securities laws sought to protect investors and to maintain confidence in the securities markets, which seemed to have eroded after the market crash.[36] Congress enacted the Securities Act of

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[25] *Id.* at 596-600.

[26] *Id.* at 603-05. The Seventh Circuit remanded the case to the district court for further proceedings consistent with the Seventh Circuit's opinion. *Id.* at 605.

[27] *Tellabs II*, 127 S. Ct. at 2506.

[28] *Id.* at 2510.

[29] *Id.* at 2513.

[30] *See infra* notes 51-87 and accompanying text.

[31] *See infra* notes 51-87 and accompanying text.

[32] *See infra* notes 197-235 and accompanying text.

[33] *See infra* notes 197-235 and accompanying text.

[34] *See infra* notes 236-250 and accompanying text.

[35] Ernst & Ernst v. Hochfelder, 425 U.S. 185, 194 (1976); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 727 (1975); Securities Act of 1933, 15 U.S.C. § 77l (2006); Securities Exchange Act of 1934, 15 U.S.C. § 78b (2006).

[36] H.R. REP. NO. 104-369, at 31 (1995) (Conf. Rep.).

1933 (1933 Act) to protect investors against fraud, ensure disclosure of material information concerning public offerings of securities, and to promote honesty and fair dealing in the market.[37] The Securities Exchange Act of 1934 (1934 Act) complemented the 1933 Act by protecting investors in two ways.[38] First, it protected investors from unfair practices by regulating securities exchanges and over-the-counter markets operating in commerce.[39] Second, it protected investors by imposing standardized reporting requirements on publicly traded companies.[40] As part of the 1934 Act, Congress created the Securities Exchange Commission (SEC) and gave it the power to enforce the Acts.[41] Section ten of the 1934 Act (§ 10(b)) makes it

> unlawful for any person . . . [t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.[42]

In 1942, acting under the authority granted by § 10(b) of the 1934 Act, the SEC promulgated rule 10b-5.[43] Rule 10b-5 allows the SEC to regulate

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[37] *Ernst & Ernst*, 425 U.S. at 195 (citing H.R. REP. NO. 73-85, at 1-5 (1933)); *see also Blue Chip Stamps*, 421 U.S. at 728; 15 U.S.C. § 77l.

[38] *Ernst & Ernst*, 425 U.S. at 195; S. REP. NO. 73-792, at 1-5 (1934); *Blue Chip Stamps*, 421 U.S. at 728; 15 U.S.C. § 78b.

[39] *Ernst & Ernst*, 425 U.S. at 195 (stating the 1934 Act intended to protect investors from the manipulation of stock prices in securities markets); S. REP. NO. 73-792, at 1-5 (stating the purpose of the 1934 Act was to protect investors by the regulation of securities exchanges); *Blue Chip Stamps*, 421 U.S. at 728 (stating the 1934 Act intended to protect investors from inequitable and unfair practices by the regulation of securities exchanges); 15 U.S.C. § 78b.

[40] *Ernst & Ernst*, 425 U.S. at 195; S. REP. NO. 73-792, at 1-5; *Blue Chip Stamps*, 421 U.S. at 728; 15 U.S.C. § 78b.

[41] Securities Exchange Act of 1934, 15 U.S.C. 78j (2006); *Ernst & Ernst*, 425 U.S. at 195; *Blue Chip Stamps*, 421 U.S. at 728-29.

[42] 15 U.S.C. § 78j.

[43] *Ernst & Ernst*, 425 U.S. at 195; *Blue Chip Stamps*, 421 U.S. at 729. Allowing standing for securities fraud actions,

Rule 10b-5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) 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 light of the circumstances under which they were made, not misleading, or

securities fraud.[44] Although § 10(b) of the 1934 Act and Rule 10b-5 allow the SEC to regulate securities fraud, neither permits private actions for such fraud.[45] Nevertheless, in 1946, the United States District Court for the Eastern District of Pennsylvania held an implied private right of action existed under the statute.[46] Twenty-five years later the Supreme Court ruled on this issue in *Superintendent of Insurance of the State of New York v. Bankers Life and Casualty Company*.[47] The Supreme Court confirmed the overwhelming opinions of the district courts and the courts of appeals when it established a private right of action is available under § 10(b).[48] In 1976, the Supreme Court clarified another rule when it held, in *Ernst & Ernst v. Hochfelder*, that to establish liability under § 10(b) and 10b-5 negligence was insufficient, and the plaintiff must prove the defendant acted with scienter.[49] The circuits adopted the scienter standard; however, the adoption of a private right of action created a split among the circuits regarding pleading requirements under the Federal Rules of Civil Procedure.[50]

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5 (1951).

[44] 17 C.F.R. § 240.10b-5.

[45] *Ernst & Ernst*, 425 U.S. at 196 ("[Section] 10(b) does not by its terms create an express civil remedy for its violation . . . ."); *Blue Chip Stamps*, 421 U.S. at 729 ("Section 10(b) of the 1934 Act does not by its terms provide an express civil remedy for its violation.").

[46] Kardon v. Nat'l Gypsum Co., 69 F. Supp. 512, 513-14 (E.D. Pa. 1946). The court based its reasoning on the well-established notion that a violation of a statute constitutes a wrongful act and a tort. *Id.* Thus, Congress would have made it clear in the statutory language if it intended to prevent recovery from private parties injured by securities fraud. *Id.* Because Congress did not make it clear in the statutory language, Congress must have intended to follow general tort law, thus allowing civil actions under § 10(b). *Id.*

[47] Superintendent of Ins. of State of N.Y. v. Bankers Life & Cas. Co., 404 U.S. 6, 13 n.9 (1971).

[48] *Id.* at 13 n.9. The Court stated, in its opinion, a private right of action is recognized under Rule 10b-5 as a remedy for securities fraud actions. *Id.* at 13. Then, in footnote 9, the Court acknowledged that a private right of action under § 10(b) of the 1934 Act is "now established." *Id.* at 13 n.9. This decision remained consistent with the Supreme Court's earlier recognition in dictum of *J. I. Case Company v. Borak* that "[p]rivate enforcement of . . . [securities laws] provides a necessary supplement to Commission [(SEC)] action." J. I. Case Co. v. Borak, 377 U.S. 426, 432 (1964).

[49] *Ernst & Ernst*, 425 U.S. at 193. The Court defined scienter as "a mental state embracing intent to deceive, manipulate, or defraud." *Id.* at 193 n.12. Every court of appeals has recognized that the plaintiff may meet the scienter requirement by showing that defendant acted reckless, however, the Supreme Court is yet to rule on this issue. *Tellabs II*, 127 S. Ct. at 2507 n.3; *Ernst & Ernst*, 425 U.S. at 193 n.12.

[50] *Tellabs II*, 127 S. Ct. at 2507; *Ernst & Ernst*, 425 U.S. at 193 n.12; *Superintendent of Ins. of State of N.Y.*, 404 U.S. at 13 n.9.

Pleading Requirements Under The Federal Rules Of Civil Procedure

All of the circuits have consistently recognized that Federal Rule of Civil Procedure "9(b) applies to actions brought under the federal securities laws."[51] Compared to Federal Rule of Civil Procedure 8(a)(2), Federal Rule of Civil Procedure 9(b) is a heightened pleading standard, requiring the circumstances constituting fraud be stated with particularity.[52] However, it provides "[m]alice, intent, knowledge, and other condition of mind of a person, may be averred generally."[53] Although the circuits agreed Rule 9(b) governs pleadings for securities fraud actions, the courts divided on its interpretation.[54] The Ninth Circuit merely required plaintiffs to state scienter existed.[55] The First Circuit's pleading requirement proved more stringent, requiring a plaintiff to state facts that give rise to an inference of scienter.[56] The Second Circuit had the strongest pleading

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[51] *In re* GlenFed, Inc. Securities Litigation, 42 F.3d 1541, 1545 (9th Cir. 1994); *accord* Shields v. Citytrust Bancorp, Inc., 25 F.3d 1124, 1127-28 (2nd Cir 1994) (acknowledging Federal Rule of Civil Procedure 9(b) applies to securities fraud); Greenstone v. Cambex Corp., 975 F.2d 22, 25 (1st Cir. 1992) (holding Federal Rule of Civil Procedure 9b applies to actions brought under the federal securities laws).

[52] FED. R. CIV. P. 9(b). Federal Rule of Civil Procedure 9(b) states that "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally." *Id.* Conversely, Federal Rule of Civil Procedure 8(a)(2) merely requires "a short and plain statement of the claim showing that the pleader is entitled to relief." FED. R. CIV. P. 8(a)(2).

[53] FED. R. CIV. P. 9(b).

[54] *Tellabs II*, 127 S. Ct. at 2507. The Second Circuit required the plaintiff to allege facts that give rise to a "strong inference" that the defendant acted with "fraudulent intent." *E.g., Shields*, 25 F.3d at 1128 (requiring plaintiffs to allege facts that give rise to a "strong inference" that the defendant acted with "fraudulent intent"); Cosmas v. Hassett, 886 F.2d 8, 12-13 (2nd Cir. 1989) (requiring a complaint to allege facts that give rise to a "strong inference" that the defendant "possessed the requisite fraudulent intent"); Ross v. A. H. Robins Co., 607 F.2d 545, 558 (2nd Cir. 1979) (holding plaintiffs must state facts that give rise to a "strong inference" that defendant acted with fraudulent intent). The Ninth Circuit's interpretation was at the opposite end of the spectrum of the Second Circuit. *Compare* In re *GlenFed, Inc. Sec. Litig.*, 42 F.3d at 1547 ("[P]laintiffs may aver scienter generally, just as the rule states-that is, simply by saying that scienter existed."), *with Shields*, 25 F.3d at 1128-29. The First, Fifth and Seventh Circuits choose a middle ground. Brief for the United States as Amicus Curiae Supporting Petitioners at 14, Tellabs, Inc. v. Makor Issues & Rights, Ltd., 127 S. Ct. 2499 (2007) (No. 06-484), 2007 WL 460606. These circuits used different language, but they all required the plaintiff to allege facts that supported a reasonable inference that the defendant acted with the required state of mind. *See Greenstone*, 975 F.2d at 25; Brief for the United States, *supra* note 54, at 14-15 (citing Tuchman v. DSC Comm'cns Corp., 14 F.3d 1061, 1068 (5th Cir. 1994); DiLeo v. Ernst & Young, 901 F.2d 624, 629 (7th Cir. 1990)).

[55] In re *GlenFed, Inc. Sec. Litig.*, 42 F.3d at 1546-47 ("We are not permitted to add new requirements to Rule 9(b) simply because we like the effects of doing so. This is a job for Congress, or for the various legislative, judicial, and advisory bodies involved in the process of amending the Federal Rules.").

[56] *Greenstone*, 975 F.2d at 25 (holding the complaint must "set forth specific facts that make it reasonable to believe that defendant knew that a statement was materially false or misleading.").

requirement, requiring plaintiffs to state, with particularity, facts that give rise to a "strong inference" of scienter.[57] The split between circuits triggered the need for change and established the importance of uniform pleading requirements in securities fraud actions.[58] Thus, following the Ninth Circuit's dicta that stated Congress had the responsibility to develop a uniform standard for pleading requirements in securities fraud actions, Congress enacted the Private Securities Litigation Reform Act of 1995 (PSLRA).[59]

Congress's Enactment of the Private Securities Litigation Reform Act of 1995

In addition to setting a uniform pleading standard among the circuits for § 10(b) actions, Congress enacted the Private Securities Litigation Reform Act in an effort to reduce frivolous securities fraud litigation while allowing meritorious claims to proceed.[60] Congress acknowledged private securities actions provided defrauded investors with a necessary relief for their losses.[61] In addition, Congress noted frivolous lawsuits have run rampant and the PSLRA seeks to maintain confidence in markets while protecting investors.[62] Although the PSLRA provided

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[57] *Shields*, 25 F.3d at 1128; *Ross*, 607 F.2d at 558.

[58] H.R. REP. NO. 104-369, at 31 (1995) (Conf. Rep.); *see also Tellabs II*, 127 S. Ct. at 2504; Ottman v. Hanger Orthopedic Group, Inc., 353 F.3d 338, 344 (4th Cir. 2003); Nathenson v. Zonagen, Inc., 267 F.3d 400, 407 (5th Cir. 2001); Bryant v. Avado Brands, Inc., 187 F.3d 1271, 1282 (11th Cir. 1999).

[59] In re *GlenFed, Inc. Sec. Litig.*, 42 F.3d at 1546; Private Securities Litigation Reform Act (PSLRA), 15 U.S.C. § 78u-4 (2006).

[60] H.R. REP. NO. 104-369, at 31 (Conf. Rep.) (stating that "[t]his legislation implements needed procedural protections to discourage frivolous litigation," while noting the importance of private securities litigation); *Tellabs II*, 127 S. Ct. at 2508; PSLRA, 15 U.S.C. § 78u-4 (2006).

[61] Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit, 126 S. Ct. 1503, 1510 (2006); H.R. REP. NO. 104-369, at 31 (Conf. Rep.).

[62] *See Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 126 S. Ct. at 1510-11 (noting abuses like nuisance filings had run rampant and the PSLRA emerged as an effort to curb these abuses); H.R. REP. NO. 104-369, at 31 (Conf. Rep.). Congress had heard significant evidence of abusive practices in four forms:

> (1) the routine filing of lawsuits against issuers of securities and others whenever there is a significant change in an issuer's stock price, without regard to any underlying culpability of the issuer, and with only faint hope that the discovery process might lead eventually to some plausible cause of action; (2) the targeting of deep-pocket defendants . . . without regard to their culpability; (3) the abuse of the discovery process to impose costs so burdensome that it is often economical for the victimized party to settle; and (4) the manipulation by class action lawyers of the clients whom they purportedly represent.

H.R. REP. NO. 104-369, at 31 (Conf. Rep.).

both "substantive and procedural controls," one of the most notable additions was Congress's attempt to standardize the PSLRA pleading requirements.[63] Section 1 of the PSLRA states in relevant part that:

> [i]n any private right of action . . . the complaint shall specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed.[64]

Section 2 of the PSLRA states in relevant part that "[i]n any private action . . . the complaint shall, with respect to each act or omission alleged to violate this chapter, state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind."[65]

Although Federal Rule of Civil Procedure 9(b) and § 78u-4(b)(1) of the PSLRA both require pleading the circumstances constituting fraud with particularity, there exists a notable difference between the pleading requirements of the two.[66] Rule 9(b) has a weaker standard with regard to the pleading requirements pertaining to the defendant's state of mind, allowing it to be "averred generally."[67] Conversely, § 78u-4(b)(2) of the PSLRA has a stringent requirement, demanding the plaintiff to "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind."[68]

Congress had great intentions in enacting the PSLRA.[69] However, Congress's failure to codify the Second Circuit's case law or "throw much light on what facts

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[63] 15 U.S.C. § 78u-4(b)(1)-(2); *Tellabs II*, 127 S. Ct. at 2508. In addition to pleading requirements, "Congress prescribed new procedures for the appointment of lead plaintiffs and lead counsel. This innovation aimed to increase the likelihood that institutional investors—parties more likely to balance the interests of the class with the long-term interests of the company—would serve as lead plaintiffs." *Id.* Additionally, Congress provided "provisions limit[ing] recoverable damages and attorney's fees, provide[d] a 'safe harbor' for forward-looking statements, . . . mandate[d] imposition of sanctions for frivolous litigation, and authorize[d] a stay of discovery pending resolution of any motion to dismiss." *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 126 S. Ct. at 1511; *see also* 15 U.S.C. § 78u-4.

[64] 15 U.S.C. § 78u-4(b)(1).

[65] 15 U.S.C. § 78u-4(b)(2).

[66] 15 U.S.C. § 78u-4(b)(1)-(2); FED. R. CIV. P. 9(b).

[67] FED. R. CIV. P. 9(b). "Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally." *Id.*

[68] 15 U.S.C. § 78u-4(b)(1)-(2).

[69] H.R. REP. NO. 104-369, at 31 (1995) (Conf. Rep.).

will suffice to create [a strong] inference" has left the circuits divided again, this time in defining the term "strong inference."[70]

Three different approaches developed among the circuits in determining the facts a plaintiff must plead to meet the required "strong inference" of scienter.[71] The Second and Third Circuits reasoned Congress intended to adopt the Second Circuit's pleading standard.[72] In the case of *In re Advanta Corp. Securities Litigation*, the Third Circuit reasoned Congress's use of the Second Circuit's language in enacting the PSLRA indicated that Congress intended to adopt the Second Circuit's pleading standard.[73] Additionally, the court argued that adoption of the Second Circuit's restrictive pleading standard in most jurisdictions would be consistent with Congress's intentions in strengthening the pleading standards and reducing frivolous litigation.[74] Thus, under the Second Circuit's standard, a plaintiff would succeed if he or she stated a claim that "establish[ed] a motive and an opportunity to commit fraud, or by setting forth facts that constitute[d] circumstantial evidence of either reckless or conscious behavior."[75]

Turning to the other extreme, the Ninth and Eleventh Circuit rejected the Second Circuit's standard and opted instead for an even stricter standard, requiring "strong circumstantial evidence of deliberately reckless or conscious misconduct."[76] The Ninth Circuit in *In re Silicon Graphics Inc. Securities Litigation*, reasoned that rejection of the Second Circuit's standard was proper because Congress intended

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[70] *See Tellabs I*, 437 F.3d at 601 (stating "Congress did not . . . throw much light on what facts will suffice to create [a strong] inference"); *Tellabs II*, 127 S. Ct. at 2509.

[71] *Tellabs I*, 437 F.3d at 601; *In re* Silicon Graphics Inc. Securities Litigation, 183 F.3d 970, 974 (9th Cir. 1999).

[72] *See, e.g.,* Novak v. Kasaks, 216 F.3d 300, 309-10 (2nd Cir. 2000) ("The statute effectively adopts the Second Circuit's pleading standard for scienter wholesale, and thus plaintiffs may continue to state a claim by pleading either motive and opportunity or strong circumstantial evidence of recklessness or conscious misbehavior."); *In re* Advanta Corp. Sec. Litig., 180 F.3d 525, 534-35 (3rd Cir. 1999) (holding plaintiffs may "plead scienter by alleging facts establishing a motive and an opportunity to commit fraud").

[73] In re *Advanta Corp. Sec. Litig.*, 180 F.3d at 533-34; *accord Novak*, 216 F.3d at 309-10 (Congress's use of the Second Circuit's language in the PSLRA indicates a standard equal to the Second Circuit's standard.).

[74] In re *Advanta Corp. Sec. Litig.*, 180 F.3d at 534; *accord Novak*, 216 F.3d at 309-10. The Second Circuit had the most stringent pleading standard, and therefore, the adoption of the Second Circuit's standard would be consistent with Congress's intentions in strengthening the pleading standards. *Novak*, 216 F.3d at 309-10.

[75] In re *Advanta Corp. Sec. Litig.*, 180 F.3d at 534-35; *see also Novak*, 216 F.3d at 309-10 (stating a plaintiff may succeed by "pleading either motive and opportunity or strong circumstantial evidence of reckless or conscious misbehavior").

[76] In re *Silicon Graphics Inc. Sec. Litig.*, 183 F.3d at 974; *see also Bryant*, 187 F.3d at 1285-87 (rejecting the Second Circuit's standard and instead requiring a strong showing of severe recklessness).

to elevate the pleading requirement above any standards in existence at the time of the PSLRA's enactment.[77] Furthermore, the court stated its reasoning best explains Congress's adoption of the Second Circuit's "strong inference standard" for the PSLRA while expressly refusing to codify the Second Circuit's case law interpreting that standard.[78]

Finally, the First, Fourth, Fifth, Sixth, Eighth, and Tenth Circuits interpreted the PSLRA by creating a middle ground.[79] These circuits adopted a case-by-case approach, requiring courts to look at the totality of the facts to determine if the allegations gave rise to a strong inference of fraudulent intent.[80] The cases that follow the middle ground approach argued Congress did not intend to adopt the Second Circuit's pleading standard.[81] In addition, these cases stated that the Act's language indicated, "Congress plainly contemplated that scienter could be proven by inference, thus acknowledging the role of indirect and circumstantial evidence."[82] Furthermore, the courts held the PSLRA's language does not require "nor prohibit the use of any particular method to establish an inference of

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[77] In re *Silicon Graphics Inc. Sec. Litig.*, 183 F.3d at 974.

[78] *Id.*

[79] City of Philadelphia v. Fleming Companies, Inc., 264 F.3d 1245, 1261-62 (10th Cir 2001).

[80] *Id*. at 1261; *accord Ottmann*, 353 F.3d at 345 (agreeing a case-by-case approach is appropriate); Florida State Bd. of Admin. v. Green Tree Financial Corp., 270 F.3d 645, 659-60 (8th Cir. 2001) (holding the Eighth Circuit will follow the middle ground approach); Helwig v. Vencor, Inc., 251 F.3d 540, 550-52 (6th Cir. 2001) (holding the case-by-case approach best reflects Congress's intent); Greebel v. FTP Software, Inc., 194 F.3d 185, 195-97 (1st Cir. 1999) (holding the First Circuit analyzes the facts of each case to determine whether those facts alleged support a "strong inference" of scienter); Nathenson v. Zonagen, Inc., 267 F.3d 400, 410-12 (5th Cir. 2001) (stating it followed the approach taken by the Sixth Circuit).

[81] *Greebel*, 194 F.3d at 195-97; *accord City of Philadelphia*, 264 F.3d at 1261-62 (holding a fact-specific approach best reflects Congress's intent); *Ottmann*, 353 F.3d at 345 (holding the legislative history regarding the adoption of the Second Circuit standard inconclusive); *Florida State Bd. of Admin.*, 270 F.3d at 659-60 (holding the PSLRA "adopted only the strong-inference-of-scienter standard, without codifying the particular methods of satisfying the standard."); *Helwig*, 251 F.3d at 550-52 (stating the PSLRA never refers to motive and opportunity); *Nathenson*, 267 F.3d at 410-12 (holding the legislative history on whether Congress intended to adopt the motive and opportunity approach is ambiguous).

[82] *Greebel*, 194 F.3d at 195; *accord City of Philadelphia*, 264 F.3d at 1261-62 (holding the Act's language indicates Congress's belief that scienter could be proven by inference); *Ottmann*, 353 F.3d at 345 (holding the court must examine all of the allegations to determine if they give rise to a "strong inference" of scienter); *Florida State Bd. of Admin.*, 270 F.3d at 659-60 (holding the primary effect of the PSLRA "is to require a pleading to state facts giving rise to a 'strong inference of scienter.'"); *Helwig*, 251 F.3d at 551 (quoting *Greebel* that "Congress plainly contemplated that scienter could be proven by inference, thus acknowledging the role of indirect and circumstantial evidence."); *Nathenson*, 267 F.3d at 410 (quoting *Greebel* that "Congress plainly contemplated that scienter could be proven by inference, thus acknowledging the role of indirect and circumstantial evidence.").

scienter."[83] Finally, the courts argued Congress mandated inferences of scienter only survive if both reasonable and "strong."[84] Considering the "strong" aspect of the PSLRA, the First Circuit and the Sixth Circuit raised its middle ground standard to a higher level.[85] In *In re Credit Suisse First Boston Corp.*, the First Circuit held that when considering the complaint as a whole, a plaintiff has not met the "strong inference" standard where "there are legitimate explanations for the behavior that are equally convincing."[86] In *Helwig v. Vencor, Inc.*, the Sixth Circuit held "plaintiffs are entitled only to the most plausible of competing inferences," but the inference does not have to be "irrefutable."[87] The circuit splits regarding the interpretation of the PSLRA's "strong inference" standard led the United States Supreme Court's decision to grant certiorari in the *Tellabs* case.[88]

PRINCIPAL CASE

In *Tellabs I*, the Seventh Circuit adopted the middle ground standard, requiring an examination of all the complaint's allegations to decide whether they gave rise to a "strong inference" of scienter.[89] However, the Seventh Circuit failed to adopt the Sixth Circuit's standard for the survival of a complaint.[90] According to the Sixth Circuit's standard, "plaintiffs are entitled only to the most plausible of competing inferences," but the inference does not have to be "irrefutable."[91] Worried the Sixth Circuit's standard might infringe on the plaintiff's Seventh Amendment rights to a jury trial, the Seventh Circuit adopted its own standard for the survival of a complaint.[92] Reversing the decision of the district court, the

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[83] *Greebel*, 194 F.3d at 195-96; *accord Ottmann*, 353 F.3d at 345 (holding the Act's language does not specify any particular method to establish an inference of scienter); *Florida State Bd. of Admin.*, 270 F.3d at 659-60 (holding Congress did not mandate a particular method of satisfying the "strong inference" standard); *Helwig*, 251 F.3d at 551 (quoting *Greebel* that "'the words of the act neither mandate nor prohibit the use of any particular method to establish an inference of scienter.'"); *Nathenson*, 267 F.3d at 411 (citing *Greebel* that the "PSLRA neither mandated nor prohibited *any* particular method of establishing a strong inference of scienter.").

[84] *Greebel*, 194 F.3d at 195; *accord Florida State Bd. of Admin.*, 270 F.3d at 660 (holding inferences only survive if they are both strong and reasonable); *Helwig*, 251 F.3d at 553 (holding inferences must be reasonable and strong).

[85] *See In re* Credit Suisse First Boston Corp., 431 F.3d 36, 49 (1st Cir. 2005) (holding plaintiff fails to meet the "strong inference" standard where "there are legitimate explanations for the behavior that are equally convincing."; *Helwig*, 251 F.3d at 553 (holding "the 'strong inference' requirement means plaintiffs are entitled only to the most plausible of competing inferences.").

[86] In re *Credit Suisse First Boston Corp.*, 431 F.3d at 49; *see also Helwig*, 251 F.3d at 553 (holding "the 'strong inference' requirement means that plaintiffs are entitled only to the most plausible of competing inferences.").

[87] *Helwig*, 251 F.3d at 553.

[88] *Tellabs II*, 127 S. Ct. 2499, 2506 (2007).

[89] *Tellabs I*, 437 F.3d 588, 601 (7th Cir. 2006).

[90] *Id.* at 601-02.

[91] *Helwig*, 251 F.3d at 553.

[92] *Tellabs I*, 437 F.3d at 602.

Seventh Circuit found the complaint survived because "it allege[d] facts from which, if true, a reasonable person could infer that the defendant acted with the required intent."[93] Consequently, Tellabs appealed the decision of the Seventh Circuit and the United States Supreme Court granted certiorari "to resolve the disagreement among circuits on whether, and to what extent, a court must consider competing inferences in determining whether a securities fraud complaint gives rise to a 'strong inference' of scienter."[94]

In *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, the United States Supreme Court acknowledged it must develop a more workable PSLRA "strong inference" pleading standard while still maintaining the PSLRA's goals of reducing frivolous claims but allowing meritorious ones to proceed.[95] The Court held the determination of whether a complaint survives a motion to dismiss is not whether an individual allegation, viewed in isolation, meets the "strong inference" standard.[96] Rather, courts must look at all of the facts alleged to determine if those facts give rise to a "strong inference" of scienter.[97]

Because of the circuit split and Congress's failure to provide an explanation as to the facts needed to meet the "strong inference" standard, the *Tellabs* Court settled the disagreement.[98] The Court decided that in determining whether the pled facts met the "strong inference" requirement, a court must look at reasonable opposing inferences.[99] The Court noted the Seventh Circuit failed to take this step when it determined the Shareholders met the "strong inference" requirement.[100] The Seventh Circuit mistakenly held a complaint could survive if it "allege[d] facts from which, if true, a reasonable person could infer that the defendant acted with the required intent . . . ."[101] Conversely, when Congress enacted the PSLRA, one of the Act's main purposes involved heightening the pleading standards required in a securities fraud action.[102] Congress determined it insufficient to allege facts from which a reasonable person could find an inference of scienter.[103] Thus, the

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[93] *Id.*

[94] *Tellabs II*, 127 S. Ct. at 2506.

[95] *Id.* at 2509.

[96] *Id.* The Court first reiterated that when dealing with a Rule 12(b)(6) motion to dismiss a § 10(b) action, a court must accept all the factual allegations in the complaint as true. *Id.*

[97] *Id.*

[98] *Id.*

[99] *Tellabs II*, 127 S. Ct. at 2509.

[100] *Id.*

[101] *Id.* (quoting *Tellabs I*, 437 F.3d at 602).

[102] *Tellabs II*, 127 S. Ct. at 2508.

[103] *Id.* at 2510. *See also In re* Cerner Corp. Sec. Litig., 425 F.3d 1079, 1084, 1085 (8th Cir. 2005) (holding inferences of scienter do not survive a motion to dismiss unless the inferences are both reasonable and strong).

Court stated, "Congress required plaintiffs to plead with particularity facts that give rise to a 'strong' *i.e.*, a powerful or cogent-inference."[104]

In evaluating the strength of an inference, the Court stated, "it cannot be decided in a vacuum."[105] Furthermore, the Court determined that in addition to looking at inferences that favor the plaintiff, a court must also consider possible explanations for the defendant's conduct.[106] However, the Court noted "[t]he inference that the defendant acted with scienter need not be irrefutable, *i.e.*, of the 'smoking-gun' genre, or even the 'most plausible of competing inferences.'"[107] The Court determined this because the PSLRA pleading standards contained only one constraint among many that heightened the requirements in instituting a securities fraud action.[108] Despite this reasoning, the Court again noted the importance that "the inference of scienter must be more than merely 'reasonable' or 'permissible'—it must be cogent and compelling, thus strong in light of other explanations."[109] As a result, the Court held a plaintiff will succeed only if a reasonable person would find the inference of scienter "cogent and at least as compelling" as any inference favoring the defendant.[110]

In other words, the Court held in addition to looking at inferences that favor the plaintiff, a court must weigh the plaintiff's deductions against other possible inferences favoring the defendant's conduct.[111] The Court acknowledged, however, the inferences favoring the plaintiff do not need to be a dead give away, nor do they even need to be the most realistic of the competing inferences.[112] But, the Court highlighted the importance the inference of scienter must be more than "permissible," it must be convincing to a reasonable person.[113] Therefore, for a complaint to survive, a reasonable person must find the inference of scienter at least as convincing as any inference favoring the defendant.[114]

Before concluding its discussion on scienter, the Court addressed two of Tellabs' contentions.[115] First, Tellabs contended when considering competing

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[104] *Tellabs II*, 127 S. Ct. at 2510.

[105] *Id.*

[106] *Id.*

[107] *Id.* (quoting Fidel v. Farley, 392 F.3d 220, 227 (6th Cir. 2004)).

[108] *Tellabs II*, 127 S. Ct. at 2510.

[109] *Id.*

[110] *Id.*

[111] *Id.*

[112] *Id.* ("The inference that defendant acted with scienter need not be irrefutable, *i.e.*, of the 'smoking-gun' genre, or even the 'most plausible of competing inferences.'").

[113] *Tellabs II*, 127 S. Ct. at 2510.

[114] *Id.*

[115] *Id.* at 2511.

inferences, Notebaert's lack of personal financial gain proved dispositive.[116] The Court noted the defendant's motive is an important consideration and proof of defendant's financial gain might "weigh heavily in favor of a scienter inference."[117] However, in agreeing with the Seventh Circuit, the Court held the absence of allegations proving a motive is not dispositive.[118] The Court noted the presence or absence of motive accounts for only one allegation, and it reiterated the importance of taking all of the allegations, as a whole, to determine if the plaintiff met the "strong inference" of scienter.[119]

Next, Tellabs argued four claims in the Shareholders' complaint proved too vague to give rise to a "strong inference" of scienter with respect to Notebaert's actions.[120] First, regarding the false inflation of fourth-quarter results for 2000, the Shareholders failed to allege whether Notebaert knew about the illegal channel stuffing as opposed to the legal channel stuffing.[121] Second, the Shareholders failed to state particular dates proving Notebaert knew about the dropping demand for the 5500 when he made multiple statements about the strong demand.[122] Third, the Shareholders failed to prove the weekly or monthly reports, reviewed by Notebaert, mentioned the TITAN 6500 was not ready for delivery.[123] Thus, the Shareholders failed to prove Notebaert knew the falsity of his statement that the product was ready for delivery and demand was strong.[124] Finally, because the Shareholders failed to prove that Notebaert or the company benefited from the alleged fraud, both Tellabs and Notebaert lacked motive.[125] The Court agreed with Tellabs that vague and ambiguous statements would weigh against the Shareholders in their attempt to meet the "strong inference" requirement.[126]

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[116] *Id.* S*ee also* Brief for Petitioners, *supra* note 1, at 50. Tellabs stated that the complaint failed to identify any motive on the part of Notebaert to commit fraud because he never sold any stock during the class period which would have personally benefited him. *Id.*

[117] *Tellabs II*, 127 S. Ct. at 2511.

[118] *Id.*

[119] *Id.*

[120] *Id.* S*ee also* Brief for Petitioners at, *supra* note 1, at 43-50.

[121] Brief for Petitioners, *supra* note 1, at 43-50. Legal channel stuffing includes offering customers discounts in an attempt to increase sales. *Id.* at 44. Writing purchase orders for products customers never ordered, and then shipping the customers those products in an attempt to increase sales fraudulently exemplifies illegal channel stuffing. *Id.*

[122] *Id.* at 46-48.

[123] *Id.* at 48-49.

[124] *Id.*

[125] *Id.* at 49-50.

[126] *Tellabs II*, 127 S. Ct. at 2511. Vague and ambiguous statements would count against Shareholders in inferring scienter because 15 U.S.C. § 78u-4(b)(2) requires plaintiffs to "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2) (2006). Again, the court reiterated the importance of reviewing all of the allegations collectively and not viewing each allegation individually. *Tellabs II*, 127 S. Ct. at 2511.

The Court, however, summarized by stating the reviewing court must weigh all allegations and determine if a reasonable person would find the inference of scienter at least as strong as any opposing inference.[127]

Before concluding its opinion, the Court addressed the Seventh Circuit's constitutional argument.[128] Justifying its ruling on the "strong inference" standard, the Seventh Circuit stated that weighing opposing inferences and making a decision is a role for the jury.[129] It also noted that failing to allow jury review would impinge upon the Shareholders' Seventh Amendment right to a trial by jury.[130] The Court disagreed with the Seventh Circuit, stating it lies within Congress's power to determine what the plaintiff must plead to state a claim, and the Court has never questioned that power.[131] Furthermore, the Court has never held the Seventh Amendment prohibits Congress from establishing heightened pleading requirements for particular claims.[132] The Court stated the Seventh Amendment is not violated because the "heightened pleading rule simply 'prescribes the means of making an issue,' and that, when '[t]he issue [was] made as prescribed, the right of trial by jury accrues.'"[133]

The Court concluded by overruling the Seventh Circuit's scienter test.[134] The Court did not determine, however, whether the Shareholders' allegations met the scienter requirement pursuant to the new rule handed down in its decision.[135] Instead, the Court remanded the case back to the Seventh Circuit for further proceedings consistent with the new rule.[136]

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[127] *Tellabs II*, 127 S. Ct. at 2511. The Seventh Circuit held allegations of scienter must be made with respect to each defendant individually. *Tellabs I*, 437 F.3d at 602-03. The Court did not address whether allegations of scienter made against one defendant can be imputed to all the other individual defendants. *Tellabs II*, 127 S. Ct. at 2511, n.6.

[128] *Tellabs II*, 127 S. Ct. at 2511-12. The Supreme Court stated the Seventh Circuit unnecessarily raised this issue on its own accord since Shareholders never raised it. *Id.* at 2512 n.7.

[129] *Id.* at 2511-12.

[130] *Id.*

[131] *Id.* at 2512.

[132] *Id.*

[133] *Tellabs II*, 127 S. Ct. at 2512 (quoting Fidelity & Deposit Co. of Md. v. United States, 187 U.S. 315, 320 (1902)). *Fidelity & Deposit Co.* dealt with a similar Seventh Amendment contention regarding the Supreme Court of the District of Columbia's rule established pursuant to the rulemaking power Congress delegated that required defendants to state with particularity their grounds for defense. *Id.* The Court entered judgment for the plaintiff because of the defendant's affidavit lacked sufficiency. *Id.* The United States Supreme Court upheld the District of Columbia's holding that the rule did not violate the Seventh Amendment. *Id.* The Court stated the right to a trial by jury would begin once the defendant properly stated his grounds for defense. *Id.*

[134] *Id.* at 2512.

[135] *Id.*

[136] *Id.*

Justice Scalia's Concurrence

Unhappy with the new rule the Court developed, Justice Scalia concurred.[137] In his concurring opinion, Justice Scalia disagreed with the Court's opinion that an inference "'at least as compelling as any opposing inference,'" can be considered a "strong inference."[138] Justice Scalia reasoned the Court must give the phrase "strong inference" its normal meaning.[139] The proper test, therefore, "should be whether the inference of scienter (if any) is *more plausible* than the inference of innocence."[140] He argued the Court's rejection of his test fell on two erroneous lines of reasoning.[141] First, irrefutable facts are not required to prove a "strong inference" of scienter.[142] Justice Scalia began his analysis by noting that Congress should determine the proper pleading standard, and Congress did so by using the phrase "strong inference."[143] According to Justice Scalia, it is now the Court's job to give that phrase its normal meaning.[144] Justice Scalia noted the Court abandoned the statutory text in favor of judicial inference when the Court enacted a test allowing a tie to go to the plaintiff.[145] Justice Scalia concluded by stating that enacting the PSLRA's heightened pleading standards Congress did not intend to allow plaintiffs to win in a close case.[146]

Justice Scalia stated the second erroneous reason the Court rejected his test lies in the contention that "the inference of scienter . . . [must be] at least as compelling as any opposing inference."[147] The effect of this rule would allow a tie to go to the plaintiff, an outcome contrary to the ordinary rule of tort law.[148] Justice Scalia argued that if Congress meant to depart from the ordinary rule in which a tie goes to the defendant, the statute would have indicated it.[149] He concluded by noting that the contrary proves true because Congress "explicitly strengthen[ed] [the] rule by extending it to the pleading stage of a case."[150]

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[137] *Id.* (Scalia, J., concurring).

[138] *Tellabs II*, 127 S. Ct. at 2513 (Scalia, J., concurring) (quoting *Tellabs II*, 127 S. Ct. at 2505).

[139] *Id.* at 2513-14 (Scalia, J., concurring).

[140] *Id.* (Scalia, J., concurring). Justice Scalia stated that his test and the Court's test will seldom produce different results because two opposing inferences rarely prove exactly equal. *Id.* at 2514.

[141] *Id.* at 2513 (Scalia, J., concurring).

[142] *Id.* (Scalia, J., concurring).

[143] *Tellabs II*, 127 S. Ct. at 2513-14 (Scalia, J., concurring).

[144] *Id.* at 2514 (Scalia, J., concurring).

[145] *Id.* (Scalia, J., concurring).

[146] *Id.* (Scalia, J., concurring).

[147] *Id.* at 2510; *Id.* at 2513 (Scalia, J., concurring).

[148] *Tellabs II*, 127 S. Ct. at 2510; *Id.* at 2513 (Scalia, J., concurring).

[149] *Id.* at 2514 (Scalia, J., concurring).

[150] *Id.* (Scalia, J., concurring).

Justice Alito's Concurrence

Justice Alito agreed with Justice Scalia that the proper test for pleading requirements would demand an inference slightly stronger than no inference of scienter.[151] Justice Alito stated Justice Scalia's test for the pleading requirements acts similar to the test used at the summary-judgment and judgment-as-a-matter-of-law stages.[152] Differing from the Court, Justice Alito believed Congress did not intend to develop a new test.[153] Rather, Justice Alito thought the test should run consistent with the one used at the summary-judgment stage, one with which the courts remain familiar.[154]

Additionally, Justice Alito disagreed with the Court's decision that all of the facts must be taken into consideration when determining whether the plaintiff met the "strong inference" of scienter.[155] Instead, Justice Alito concluded only those facts pled with particularity should determine the sufficiency of the inference of scienter.[156] He stated that because the clear language requires the inference of scienter to arise from facts stated with particularity, "[i]t follows that facts not stated with the requisite particularity cannot be considered in determining whether the strong-inference test is met."[157] Justice Alito criticized the Court for stating non-particularized facts should determine whether the plaintiff met the scienter requirement.[158] In addition to contradicting the statute's clear language, Justice Alito stated the Court's holding would allow plaintiffs to benefit from alleging facts that do not meet the particularity requirement.[159] Finally, he criticized the Court for its interpretation of the particularity requirement.[160] Justice Alito reasoned the Court stripped the word "of all meaning" because its particularity requirement equaled a normal pleading review.[161] Consistent with the Court's interpretation, under a normal pleading review the court gives more weight to particularly pled facts than those pled ambiguously.[162] Thus, there existed no distinction between

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[151] *Id.* at 2516 (Alito, J., concurring).

[152] *Id.* (Alito, J., concurring). Justice Alito's test examines the pleadings to determine whether "no genuine issue" exists "as to any material fact" that the defendant possessed the required strong inference of scienter. FED. R. CIV. P. 56(c); *Tellabs II*, 127 S. Ct. at 2510 n.5.

[153] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring).

[154] *Id.* (Alito, J., concurring).

[155] *Id.* at 2515-16.

[156] *Id.* (Alito, J., concurring).

[157] *Id.* at 2516 (Alito, J., concurring). Section 78u-4(b)(2) states that "the complaint shall . . . state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. 78u-4(b)(2) (2006).

[158] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring).

[159] *Id.* (Alito, J., concurring).

[160] *Id.* (Alito, J., concurring).

[161] *Id.* (Alito, J., concurring).

[162] *Id.* (Alito, J., concurring).

the Court's interpretation of the particularity requirement and a normal pleading review.[163]

In conclusion, Justice Alito stated, "Questions certainly may arise as to whether certain allegations meet the statutory particularity requirement, but where that requirement is violated, the offending allegations cannot be taken into account."[164] Thus, a court may only use those facts pled with particularity to meet the "strong inference" standard.[165]

Justice Stevens's Dissent

Justice Stevens began his dissent by stating that since Congress left the phrase "strong inference" undefined, it would follow implicitly that Congress gave the judiciary lawmaking authority to determine its meaning.[166] He acknowledged the Court developed a workable definition of the phrase, however, his "probable-cause" standard would prove less complicated in application and more consistent with statutory interpretation."[167] Under Justice Stevens's test, the facts must show probable cause that the defendant acted with a "strong inference" of scienter.[168] Justice Stevens admitted that his definition does not have an exact measurement, but the concept is familiar to judges.[169] Furthermore, the meaning is similar to that of "strong inference."[170] He criticized Justice Scalia's test by stating Congress would not have intended the Court to adopt a standard that would make it more difficult to bring a civil case than a criminal one.[171] Justice Stevens noted his definition would beneficially omit the weighing of opposing inferences when easily deemed a strong inference.[172] Justice Stevens gave this example to illustrate his point:

> [I]f a known drug dealer exits a building immediately after a confirmed drug transaction, carrying a suspicious package, a judge could draw a strong inference that the individual was involved in the aforementioned drug transaction without debating whether the suspect might have been leaving the building at that exact time for another unrelated reason.[173]

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[163] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring).

[164] *Id.* (Alito, J., concurring).

[165] *Id.* (Alito, J., concurring).

[166] *Id.* at 2516-17 (Stevens, J., dissenting).

[167] *Tellabs II*, 127 S. Ct. at 2517 (Stevens, J., dissenting).

[168] *Id.* (Stevens, J., dissenting).

[169] *Id.* (Stevens, J., dissenting).

[170] *Id.* (Stevens, J., dissenting).

[171] *Id.* (Stevens, J., dissenting).

[172] *Tellabs II*, 127 S. Ct. at 2517 (Stevens, J., dissenting).

[173] *Id.* (Stevens, J., dissenting).

Justice Stevens applied this example to the channel stuffing allegations in the *Tellabs* case and decided taking the facts as true, they clearly established "probable cause to believe" Notebaert acted with the necessary intent.[174] Thus, he would have affirmed the judgment of the Seventh Circuit.[175]

ANALYSIS

In deciding *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, the United States Supreme Court correctly overruled the Seventh Circuit's test for a complaint's survival.[176] In addition, the Court correctly determined the need for considering plausible opposing inferences when determining if the plaintiff met the "strong inference" of scienter.[177] The Court erred, however, in the new test it developed for determining whether the facts alleged have met the required "strong inference" of scienter.[178] The new test merely requires the plaintiff to allege facts that support an inference of scienter "at least as likely as" any credible opposing inference in favor of the defendant.[179] The Court erred by allowing a tie in inferences to go to the plaintiff, instead of adopting a test like the one proposed by Justice Scalia.[180]

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[174] *Id.* (Stevens, J., dissenting). Justice Stevens found that taking the channel stuffing allegations as true, they are proof that Notebaert had knowledge of illegal practices occurring. *Id.* at 2517 n.2. For example, Notebaert worked directly with the sales personnel to channel stuff its customer, SBC. *Id.* In addition, customers returned orders they did not want, and because of the high returns, Tellabs had to rent storage space to accommodate all the returns. *Id.*

[175] *Id.* at 2518 (Stevens, J., dissenting).

[176] Supreme Court Clarifies Standards for Stock-Fraud Plaintiffs, 23 No. 2 ANCODLLR 3 (2007); David Stras, A Lingering Thought on *Tellabs*, http://www.scotusblog.com/movabletype/archives/2007/06/a_lingering_tho.html (June 23, 2007, 10:08 EST) (David Stras, a former United States Supreme Court clerk for The Honorable Clarence Thomas, currently works as a professor of law at the University of Minnesota Law School).

[177] *See* Supreme Court Clarifies Standards for Stock-Fraud Plaintiffs, *supra* note 176; A Lingering Thought on Tellabs, *supra* note 176.

[178] *See infra* notes 197-212, 217-235 and accompanying text.

[179] *Tellabs II*, 127 S. Ct. at 2513.

[180] John C. Coffee, Jr., *Federal Pleading Standards after* 'Tellabs,' *Bell Atlantic*', 7/19/2007 N.Y.L.J. 5, (col.1), 4 (2007); Posting of Joe Grundfest to WSJ Law Blog, Tellabs: Securities Lawyers React, http://blogs.wsj.com/law (June 21, 2007, 13:03 EST). Joe Grundfest posted the blog on The Wall Street Journal Online. Joe Grundfest, a Securities Law Professor at Stanford Law School and a former SEC Commissioner acknowledged that the decision constituted a clear victory for the defendants but proved not as "thorough a thrashing of the plaintiffs as some plaintiff lawyers had feared." S*ee* Grundfest, *supra* note 180. Professor Grundfest acknowledged the downfall of the opinion, leaving room for lower courts to determine that the inference of scienter, is equally in favor of plaintiff, allowing a tie to go to the plaintiff. *Id.* Professor Grundfest acknowledged this approach would ignore the Court's holding that the inference of scienter "must be cogent and compelling, thus strong in light of other explanations." *Id.* He concluded the Court's decision would lead to a new split of the lower courts over the proper interpretation of *Tellabs'* pleading standard. *Id.* Justice Scalia's test is "whether the inference of scienter (if any) proves *more plausible* than the inference of innocence." *Tellabs II*, 127 S. Ct. at 2513 (Scalia, J., concurring).

The second error pertains to the facts used to determine if the plaintiff met the "strong inference" of scienter.[181]

Where the Court Correctly Ruled

Although uncertain whether the Supreme Court's test will provide a workable outcome to the "strong inference" standard, the Court correctly held the Seventh Circuit's rule did not meet the heightened pleading standards Congress intended when it enacted the PSLRA.[182] The Seventh Circuit's test "contradicts both the language and the purpose of the PSLRA."[183] The Seventh Circuit required the complaint allege facts that "a reasonable person could infer that the defendant acted with the required intent."[184] The statute's plain language, however, requires a "strong inference," not a "reasonable" or "permissible" inference as required by the Seventh Circuit.[185] The Seventh Circuit's test reflects the approach taken prior to the PSLRA where any reasonable inference of fraud would support a claim.[186] This standard previously proved unworkable, and resulted in Congress

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[181] *See* A Lingering Thought on *Tellabs*, *supra* note 176.

[182] In re *Silicon Graphics Inc, Sec. Litig.*, 183 F.3d at 978-79 (explaining Congress intended to adopt a standard higher than the Second Circuit's, the highest standard at the time of enacting the PSLRA). This means the Seventh Circuit's standard which is lower than the Second Circuit's does not meet the heightened pleading standards intended by Congress. S*ee also Tellabs II*, 127 S. Ct. at 2504 (acknowledging that the Seventh Circuit's standard does not meet the stricter intent of Congress in enacting the PSLRA); *supra* notes 89-104 and accompanying text.

[183] *See* Coffee, *supra* note 180, at 4; In re *Silicon Graphics Inc, Sec. Litig.*, 183 F.3d at 978-79; Brief for New England Legal Found. as Amicus Curiae in Support of Pet'rs at 11, Tellabs, Inc. v. Makor Issues & Rights, Ltd., 127 S. Ct. 2499 (2007) (No. 06-484), 2007 WL 445337; *see also In re* Credit Suisse First Boston Corp., 431 F.3d 36, 49 (1st Cir. 2005) ("Scienter allegations do not pass the 'strong inference' test when . . . there are legitimate explanations for the behavior that are equally convincing."); Gompper v. VISX, Inc., 298 F.3d 893, 896-97 (9th Cir. 2002) (holding a consideration of inferences only favorable to the plaintiff would undermine the PSLRA's strong inference requirement); Helwig v. Vencor, Inc., 251 F.3d 540, 553 (6th Cir. 2001) (holding "plaintiffs are entitled only to the most plausible of competing inferences").

[184] *Tellabs I*, 437 F.3d 588, 602 (7th Cir. 2006).

[185] *Helwig*, 251 F.3d at 551, 553 ("[T]he 'strong inference' requirement means that plaintiffs are entitled only to the most plausible of competing inferences. This represents a significant strengthening of the pre-PSLRA standard under Rule 12(b)(6), which gave the plaintiff 'the benefit of all reasonable inferences . . . .'"); *In re* Cabletron Systems, Inc. 311 F.3d 11, 38 (1st Cir. 2002) ("Under the PSLRA, the complaint must state with particularity facts that give rise to a 'strong inference' of scienter, rather than merely a reasonable inference."); Brief for the United States, *supra* note 54, at 20-21; 15 U.S.C. § 78u-4(b)(2) (2006); *see* In re *Credit Suisse First Boston Corp*., 431 F.3d at 48 (holding "[t]hat the statute, by its terms, requires a 'strong,' rather than merely a 'reasonable,' inference that the defendant acted with scienter is more than an odd linguistic quirk.").

[186] Brief of Technet, The Info. Tech. Ass'n of Am., The Semiconductor Indus. Ass'n, Aea, Baybio, The Cal. Healthcare Inst. and The Nat'l Venture Capital Ass'n as Amici Curiae in Support of Pet'r at 12, Tellabs, Inc. v. Makor Issues & Rights, Ltd., 127 S. Ct. 2499 (2007) (No. 06-484), 2007 WL 445338; *see also* H.R. REP. NO. 104-369, at 31 (1995) (Conf. Rep.); S. REP. NO. 104-98, at 15 (1995).

enacting the PSLRA.[187] Furthermore, a "reasonable" inference is inconsistent with Congress's intent in requiring heightened pleading standards under the PSLRA because a reasonable inference is less than a "strong inference."[188] Therefore, the Court correctly rejected the Seventh Circuit's test.[189]

Additionally, the Court correctly determined "[t]he strength of an inference cannot be decided in a vacuum" and requires a consideration of "plausible nonculpable explanations for the defendant's conduct, as well as inferences favoring the plaintiff."[190] The Court's decision follows many of the circuits on this issue requiring an inquiry into possible opposing inferences of the defendant's conduct.[191] Moreover, the Court's ruling remains consistent with the PSLRA's plain language, which requires a "strong inference" of scienter.[192] "Strong" means "striking or superior of its kind . . . ."[193] Thus, a "strong inference" reigns "superior" to other possible inferences.[194] Since a "strong inference" holds superior to other inferences, determining whether an inference proves "strong" would require a

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[187] H.R. Rep. No. 104-369, at 31 (Conf. Rep.); S. REP. NO. 104-98, at 15.

[188] Brief of Technet, *supra* note 186, at 15; H.R. REP. NO. 104-369, at 31 (Conf. Rep.) (stating the PSLRA has implemented needed procedural protections to reduce frivolous litigation); In re *Silicon Graphics Inc, Sec. Litig.*, 183 F.3d at 979. The *In re Silicon* court noted that Congress adopted the Second Circuit's language of strong inference because it held a higher standard than the reasonable standard of other circuits. *Id.* However, Congress did not adopt the Second Circuit's two-prong test because it did not meet the heightened pleading standards the PSLRA intended. *Id.* Thus, a reasonable inference proves less convincing than a "strong inference," and therefore, not in-line with Congress's intent in enacting the PSLRA. *See Id.*

[189] *See* Supreme Court Clarifies Standards for Stock-Fraud Plaintiffs, *supra* note 176; *see also* In re *Credit Suisse First Boston Corp.*, 431 F.3d at 48 (holding "that the statute, by its terms, requires a 'strong,' rather than merely a 'reasonable,' inference that the defendant acted with scienter is more than an odd linguistic quirk."); *Tellabs II*, 127 S. Ct. at 2504 (acknowledging that the Seventh Circuit's standard does not meet the stricter intent of Congress in enacting the PSLRA).

[190] *Tellabs II*, 127 S. Ct. at 2510; *accord Helwig*, 251 F.3d at 553; Pirraglia v. Novell, Inc., 339 F.3d 1182, 1187-88 (10th Cir. 2003).

[191] *See, e.g.*, In re *Credit Suisse First Boston Corp.*, 431 F.3d at 51 (holding the court should not "turn a blind eye" to other possible conclusion arising from the facts alleged); *Pirraglia*, 339 F.3d at 1187 (holding a court must consider all reasonable inferences, even those inferences which are not favorable to the plaintiff); *Gompper*, 298 F.3d at 896-97 (holding a consideration of inferences only favorable to the plaintiff would undermine the PSLRA's strong inference requirement); *Helwig*, 251 F.3d at 553 (holding "plaintiffs are entitled only to the most plausible of competing inferences").

[192] Brief for New England Legal Found., *supra* note 183, at 12; 15 U.S.C. 78u-4(b)(2) (2006).

[193] WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 2265 (Una Dlx ed 1986).

[194] Brief for New England Legal Found., *supra* note 183, at 12; *see Helwig*, 251 F.3d at 553 ("'Strong inferences' nonetheless involve deductive reasoning; their strength depends on how closely a conclusion of misconduct follows from a plaintiff's proposition of fact. [T]he 'strong inference' requirement means that plaintiffs are entitled only to the most plausible of competing inferences.").

comparison of other possible opposing inferences.[195] Therefore, the Court correctly held the determination of whether an inference is strong requires a comparison of the plaintiff's inferences with competing inferences relating to the defendant's conduct.[196]

Justice Scalia's Test, the Proper Interpretation

Although the Court's test reflects the heightened pleading standard Congress intended in enacting the PSLRA, Justice Scalia's test remains the most "workable construction of the 'strong inference' standard."[197] Justice Scalia's test properly follows the statute's "natural reading" and provides more guidance.[198]

The Court's test requires the "inference of scienter must be more than merely plausible or reasonable—it must be cogent and at least as compelling as any opposing inference of nonfraudulent intent."[199] This rule proves flawed because it "leaves room for lower courts to reason 'gee, the story in support of scienter seems as cogent as the story in opposition to scienter, and that's good enough.'"[200] This

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[195] Brief for New England Legal Found., *supra* note 183, at 12; *see also Helwig*, 251 F.3d at 553 ("'Strong inferences' nonetheless involve deductive reasoning; their strength depends on how closely a conclusion of misconduct follows from a plaintiff's proposition of fact. [T]he 'strong inference' requirement means that plaintiffs are entitled only to the most plausible of competing inferences."); *Gompper*, 298 F.3d at 896-97 (holding a consideration of inferences only favorable to the plaintiff would undermine the PSLRA's strong inference requirement).

[196] *See Helwig*, 251 F.3d at 553; *Gompper*, 298 F.3d at 896-97 (holding that consideration of an "equally if not more plausible" inference of the defendant's innocence "clearly impedes the plaintiffs' progress toward building the requisite strong inference of scienter."); Brief for New England Legal Found., *supra* note 183, at 12 (stating a strong inference is superior to other inferences); *Tellabs II*, 127 S. Ct. at 2509-10 (holding the determination of whether plaintiff meets the strong inference standard requires consideration of opposing inferences).

[197] *See* Darquea v. Jarden Corp., 2007 WL 2584744, 1-2, 2 n.2 (S.D.N.Y. 2007) (stating that the court agrees with the "persuasive" reasoning of Justice Scalia).

[198] *See Darquea*, 2007 WL 2584744, 1-2, 2 n.2 (noting the persuasiveness of Justice Scalia's reasoning because it follows the natural statutory language); Communications Workers of Am. Plan for Employees' Pensions and Death Benefits v. CSK Auto Corp., 525 F. Supp 2d 1116, 1120 n.2 (D. Ariz. 2007) (stating an inference cannot be strong if it is equal to an innocent explanation, it is the same).

[199] *Tellabs II*, 127 S. Ct. at 2504-05.

[200] Grundfest, *supra* note 180 (quoting *Tellabs II*, 127 S.Ct. at 2502); *see also* Transit Rail, LLC v. Marsala, 2007 WL 2089273, 13 (W.D.N.Y. 2007) (reasoning that a reasonable person could just as easily infer facts in favor of the defendant as the plaintiff); Sherrie R. Savett, *Plaintiffs' Vision of Securities Litigation: Trends/Strategies in 2005-2007*, 1620 PLI/Corp 57, 97 (2007) ("[C]ourts will no doubt continue to grapple with major issues relating to the 'strong inference' language, including the manner in which allegations sufficient to give rise to a 'strong inference' of scienter may be pleaded."); Thomas O. Gorman, Tellabs Inc. v. Makor Issues & Rights, Ltd.: *Pleading a Strong Inference of Scienter*, 1620 PLI/Corp 151, 184 ("The standard gives the District Court significant discretion in construing the allegations contained in a plaintiff's securities law complaint."); F. Hodge O'Neal & Robert B. Thompson, *Resisting Squeeze-outs and Oppression:Remedies Under Federal Law*, OPPMINSH S 8:14 (stating the Court's test "leaves open multiple outcomes").

reasoning would allow a tie to go to the plaintiff, ultimately ignoring the Court's warning that "'the inference of scienter must be more than merely 'reasonable' or 'permissible' it must be cogent and compelling, thus strong in light of other explanations.'"[201] Therefore, it seems likely this rule will lead to another split between the circuits on the interpretation of *Tellabs's* pleading standard.[202]

Conversely, Justice Scalia's test requires the inference of scienter to be slightly stronger than the inference of no scienter.[203] A test that demands an inference slightly stronger than any opposing inference would eliminate the possibility of a tie between inferences.[204] This would resolve potential splits in the circuits on their interpretation of the inferences.[205] The way the rule currently stands, some courts might interpret the inferences in favor of plaintiffs while other courts would interpret those same inferences in favor of defendants.[206]

Not only does Justice Scalia's test resolve potential disputes between the circuits, it also is consistent with a natural reading of the statute.[207] "Courts . . . *must* give the statute its single, most plausible, reading."[208] In analyzing Justice

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[201] *See* Grundfest, *supra* note 180; Coffee, *supra* note 180, at 4; *Tellabs II*, 127 S. Ct. at 2510.

[202] *Compare* Ross v. Abercrombie & Fitch Co., 501 F. Supp. 2d 1102, 1117 (S.D. OH. 2007) (ruling in favor of the plaintiff because "the plaintiff's allegations are at least as compelling" as defendant's), *with* Frank v. Dana Corp., 525 F. Supp. 2d 922, 927-28, 930, 932-33 (N.D. OH. 2007) (ruling in favor of defendant because plaintiff's inferences were not "more plausible and powerful" than competing inferences or the "most plausible" of competing inferences); *see* Savett, *supra* note 200, at 97 (stating courts continue to struggle with what allegations give rise to a "strong inference"); Gorman, *supra* note 200, at 184 (stating the Court's test gives the lower courts great discretion); O'Neal & Thompson, *supra* note 200 (stating the Court's test "leaves open multiple outcomes"); Grundfest, *supra* note 180.

[203] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring).

[204] *Id.* at 2513-14 (Scalia, J., concurring); s*ee* Coffee, *supra* note 180, at 4.

[205] *See* Coffee, *supra* note 180, at 4; *see Darquea*, 2007 WL 2584744, 1-2, 2 n.2 (stating this is a case where Justice Scalia's test would make a difference in the outcome of the case).

[206] *See* Coffee, *supra* note 180, at 4; Savett, *supra* note 200, at 97 ("[C]ourts will no doubt continue to grapple with major issues relating to the 'strong inference' language, including the manner in which allegations sufficient to give rise to a 'strong inference' of scienter may be pleaded."); Gorman, *supra* note 200, at 184 ("The standard gives the District Court significant discretion in construing the allegations contained in a plaintiff's securities law complaint."); O'Neal & Thompson, *supra* note 200 (stating the Court's test "leaves open multiple outcomes").

[207] Benefits v. CSK Auto Corp., 525 F. Supp 2d 1116, 1120 n.2 (D. Ariz. 2007) (explaining an inference cannot be strong unless it is greater than a competing inference).

[208] *Tellabs II*, 127 S. Ct. at 2515 (Scalia, J., concurring); *see, e.g.,* State of N.J. v. State of N.Y. 1997 WL 291594, 23 (U.S. 1997) ("The most important and well-established [rule of statutory construction] is that, if possible, the Court will undertake a plain-language reading of the terms of [the statute]."); U.S. v. Granderson, 511 U.S. 39, 74 (1994) (stating an elementary canon of construction requires the plain statutory language to control); Mukaddam v. Permanent Mission of Saudi Arabia to United Nations, 111 F. Supp. 2d 457, 467 n.65 (S.D.N.Y. 2000) ("[T]he Court follows basic principles of statutory construction and looks first to the plain language of the statute.").

Scalia's test, § 21D(b) of the PSLRA requires the plaintiff to plead facts which give rise to a "strong inference."[209] The Supreme Court defines "strong" as "cogent," "persuasive," and "powerful."[210] Accordingly, a strong inference outweighs, by power or persuasion, an opposing inference.[211] Thus, the normal reading of the statute would demand a test like Justice Scalia's which requires that the inference of scienter prove slightly stronger than the inference of no scienter.[212]

Additionally, Justice Scalia's test equates with many circuits that hold a "strong inference" of scienter is not met if a competing inference is just as plausible.[213] In

[209] 15 U.S.C. § 78u-4(b)(1)-(2) (2006); *see also Darquea*, 2007 WL 2584744, 1-2, 2 n.2 (noting the persuasiveness of Justice Scalia's test because the language of the statute requires a "strong inference," thus the test should require a more plausible inference than one of innocence).

[210] *Tellabs II*, 127 S. Ct. at 2510.

[211] *CSK Auto Corp.*, 525 F. Supp 2d at 1120 n.2 (explaining an inference cannot be considered strong unless proven greater than an opposing inference); Brief for New England Legal Found., *supra* note 183, at 12; *see also Tellabs II*, 127 S. Ct. at 2513 n.* (Scalia, J., concurring) (stating a possibility "that B is responsible is not a strong *inference* that B is responsible"); *Helwig*, 251 F.3d at 553 (holding plaintiff's inferences must be compared to opposing inferences and plaintiff is entitled only to the strongest of opposing inferences); In re *Credit Suisse First Boston Corp.*, 431 F.3d at 49 ("[S]cienter allegations do not pass the 'strong inference' test when . . . there are legitimate explanations for the behavior that are equally convincing."); *Gompper*, 298 F.3d at 896-97 (holding that consideration of an "equally if not more plausible" inference of the defendant's innocence "clearly impedes the plaintiffs' progress toward building the requisite strong inference of scienter."); *Ottman*, 353 F.3d at 350 (holding a plaintiff has failed to meet the "strong inference" standard where a misstatement "was just as likely the result of an overgeneralization as it was the product of intentional deception or recklessness.").

[212] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring); *see also Tellabs II*, 127 S. Ct. at 2513 n.* (Scalia, J., concurring) (stating a possibility "that B is responsible is not a strong *inference* that B is responsible"); *Helwig*, 251 F.3d at 553 (holding "plaintiffs are entitled only to the most plausible of competing inferences. This represents a significant strengthening of the pre-PSLRA standard under Rule 12(b)(6), which gave the plaintiff 'the benefit of all reasonable inferences . . . .'"); In re *Credit Suisse First Boston Corp.*, 431 F.3d at 49 (holding an inference is not strong if there are equally legitimate explanations); *Gompper*, 298 F.3d at 896-97 (holding consideration of an equal inference of the defendant's innocence impedes plaintiff's meeting the "strong inference" requirement); *Ottman*, 353 F.3d 350 (holding a plaintiff has failed to meet the "strong inference" standard where a misstatement "was just as likely the result of an overgeneralization as it was the product of intentional deception or recklessness."); Brief for New England Legal Found., *supra* note 183, at 12 (stating a "strong inference" is superior to other inferences). Additionally, Justice Stevens criticized Justice Scalia's test by stating that Congress would not have intended the Court to adopt a standard that would make it more difficult to bring a civil case than a criminal one. *Tellabs II*, 127 S. Ct. at 2517 (Stevens, J., dissenting).

[213] *See, e.g.*, In re *Credit Suisse First Boston Corp.*, 431 F.3d at 49 (holding "scienter allegations do not pass the 'strong inference' test when . . . there are legitimate explanations for the behavior that are equally convincing."); *Gompper*, 298 F.3d at 896-97 (holding that consideration of an "equally if not more plausible" inference of the defendant's innocence "clearly impedes the plaintiffs' progress toward building the requisite strong inference of scienter."); *Ottman*, 353 F.3d 350 (holding a plaintiff has failed to meet the "strong inference" standard where a misstatement "was just as likely the result of an overgeneralization as it was the product of intentional deception or recklessness."); Fidel v. Farley, 392 F.3d 220, 227 (6th Cir. 2004) (holding the "strong inference" requirement only entitles the plaintiff to the "most plausible of competing inferences"); *CSK Auto Corp.*, 525 F. Supp 2d at 1120 n.2 (explaining an inference equal to an opposing inference is not strong, it is equal).

the case of *In re Credit Suisse First Boston Corp.*, the court noted the PSLRA meant to establish a strict standard for pleading in a securities fraud action to meet the "strong inference" requirement.[214] Following the strict standard of the PSLRA, the First Circuit in *In re Credit Suisse First Boston Corp.* held when considering the complaint as a whole, a "strong inference" is not met where "there are legitimate explanations for the behavior that are equally convincing."[215] The Court's opinion should have followed the lead of these circuits that gave the statute its normal reading, and therefore, used Justice Scalia's test.[216]

Justice Alito's Particularity Requirement, the Correct One

In addition to making an erroneous ruling by not following Justice Scalia's test, the Court erred again when it failed to utilize Justice Alito's particularity requirement.[217] Justice Alito's requirement only allowed consideration of those facts stated "with particularity" in determining if the "strong inference" standard was met.[218] Unfortunately, the Court developed a flawed rule by failing to recognize the PSLRA's "particularity" requirement.[219] First, although the Court reiterated that the PSLRA requires facts to be pled with "particularity," the Court's opinion weakened this standard.[220] This was evidenced when the Court stated, "omissions and ambiguities [only] count against inferring scienter," but stressed "that a court should consider all allegations of scienter, even nonparticularized ones, when considering whether a complaint meets the 'strong inference' requirement."[221]

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[214] In re *Credit Suisse First Boston Corp.*, 431 F.3d at 48.

[215] *Id.* at 49.

[216] *See Darquea*, 2007 WL 2584744, 1-2, 2 n.2 (agreeing with the reasoning of Justice Scalia and Justice Alito).

[217] *See In re* K-tel Int'l, Inc. Sec. Litig., 300 F.3d 881, 889 (8th Cir. 2002) (noting that ambiguous facts which do not live up to the particularity requirement are discarded); *In re* Trex Co., Inc. Sec. Litig., 454 F. Supp. 2d 560, 572 (W.D. Va. 2006) (stating plaintiffs may not benefit from facts not pled with the requisite particularity).

[218] *Tellabs II*, 127 S. Ct. at 2515-16 (Alito, J., concurring).

[219] *Gompper*, 298 F.3d at 896-97 (Congress made it clear that the PSLRA requires facts pled with particularity to give rise to a "strong inference" of scienter); In re *K-tel Int'l, Inc. Sec. Litig.*, 300 F.3d at 889 (stating the PSLRA requires the court to disregard those facts which are not pled with particularity); Brief of Technet, *supra* note 186, at 12; Brief for the United States, *supra* note 54, at 21; *see* A Lingering Thought on *Tellabs*, *supra* note 176 (stating the language of the statute implies that only facts pled with particularity can be used to meet the strong inference standard).

[220] *See* In re *Credit Suisse First Boston Corp.*, 431 F.3d at 49 (holding the PSLRA requires that the plaintiff plead facts with particularity); *Gompper*, 298 F.3d at 897 (holding only complaints with particularized facts that meet the strong inference standard survive a motion to dismiss); *Helwig*, 251 F.3d at 548 (holding under the PSLRA the plaintiff must plead facts with particularity); *Ottman*, 353 F.3d 350 (holding the PSLRA requires the plaintiff to plead the facts in the complaint with particularity).

[221] *Tellabs II*, 127 S. Ct. at 2515-16 (Alito, J., concurring); *see also Tellabs II*, 127 S. Ct. at 2511 (The Court allowed consideration of ambiguous facts in the determination of a "strong inference" of scienter when the Court "agree[d] that omissions and ambiguities count against inferring scienter . . . .").

Congress used the "particularity" requirement to prevent plaintiffs from defeating a motion to dismiss for failure to state a claim by merely pleading vague or ambiguous facts.[222] Considering non-particularized facts in determining whether plaintiff met the "strong inference" standard undermines Congress's purpose, thus allowing the plaintiff to evade the "particularity" requirement altogether.[223] Conversely, Justice Alito's standard enforces Congress's purpose and upholds the particularity requirement by allowing only those facts pled with particularity in determining whether the plaintiff met the "strong inference" requirement.[224]

Additionally, the Court's interpretation is flawed because it contradicts the plain statutory language.[225] Before Congress enacted the PSLRA, Rule 9(b) governed the pleading requirements for fraud demanding that facts be pled with

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[222] *See Gompper*, 298 F.3d at 897 ("Congress made it crystal clear that the [PSLRA's] pleading requirements were put in place so that only complaints with particularized facts giving rise to a strong inference of wrongdoing survive a motion to dismiss . . . ."); Bryant v. Avado Brands, Inc., 187 F.3d 1271, 1278 (11th Cir. 1999) (Congress "structur[ed] the [PSLRA] to permit the dismissal of frivolous cases at the earliest feasible stage of litigation . . . ."); H.R. REP. NO. 104-369, at 31 (1995) (Conf. Rep.) (stating Congress has enacted needed procedural protections to reduce the amount of frivolous lawsuits); S. REP. NO. 104-98, at 15 (1995) (stating Congress developed the PSLRA to enact stringent pleading requirements to deter frivolous suits); Brief of Technet, *supra* note 186, at 12; Brief for the United States, *supra* note 54, at 21-22; A Lingering Thought on Tellabs, *supra* note 176.

[223] S*ee* H.R. REP. NO. 104-369, at 31 (Conf. Rep.) (Congress recognized a need to strengthen pleading standards to reduce frivolous litigation); S. REP. NO. 104-98, at 15 (Congress enacted the PSLRA to establish a stringent pleading requirement); Winer Family Trust v. Queen, 503 F.3d 319, 327 (3rd Cir. 2007) (stating "Congress did not merely require plaintiffs to 'provide a factual basis for [their] scienter allegations'. . . . Congress required plaintiffs to plead with particularity facts that give rise to a 'strong—*i.e.,* a powerful or cogent-inference."); *Gompper*, 298 F.3d at 897 (stating the PSLRA only allows complaints pled with particular facts that give rise to a "strong inference" of scienter to survive a motion to dismiss); In re *K-tel Int'l, Inc. Sec. Litig.*, 300 F.3d at 889 (stating the PSLRA requires the court to disregard those facts not pled with particularity); *Bryant*, 187 F.3d at 1278 (stating the PSLRA is meant to dismiss those complaints at the earliest possible stage which have not pled particular facts that rise to a "strong inference" of scienter); Brief of Technet, *supra* note 186, at 12; Brief for the United States, *supra* note 54, at 21-22; A Lingering Thought on Tellabs, *supra* note 176.

[224] S*ee* H.R. REP. NO. 104-369, at 31 (Conf. Rep.) (stating the PSLRA has strengthened pleading requirements to reduce frivolous litigation); *Gompper*, 298 F.3d at 896-97 (stating the PSLRA requires facts pled with particularity to give rise to a "strong inference" of scienter); In re *Trex Co., Inc. Sec. Litig.*, 454 F. Supp. 2d at 572 (stating plaintiffs may not benefit from vague or ambiguous facts); *In re* Rockefeller Ctr. Properties, Inc. Sec. Litig., 311 F.3d 198, 224 (3d Cir. 2002) (stating according to the PSLRA plaintiffs may not benefit from vague or ambiguous facts).

[225] S*ee also Gompper*, 298 F.3d at 896-97 (Congress made it clear the PSLRA requires facts pled with particularity to give rise to a "strong inference" of scienter); In re *K-tel Int'l, Inc. Sec. Litig.*, 300 F.3d at 889 (stating the PSLRA requires the court to disregard those facts not pled with particularity); Brief of Technet, *supra* note 186, at 12; Brief for the United States, *supra* note 54, at 21; A Lingering Thought on Tellabs, *supra* note 176.

"particularity."[226] Congress enacted the PSLRA in an attempt to curb frivolous litigation by making the pleading standards higher.[227] With this purpose in mind, Congress kept the "particularity" requirement of Rule 9 in the PSLRA.[228] Section 78u-4(b)(2) of the PSLRA states "the complaint shall, with respect to each act or omission alleged to violate this chapter, state with particularity facts giving rise to a strong inference the defendant acted with the required state of mind."[229] According to the statutory language, the plaintiff may only meet the "strong inference" standard by those facts stated in the complaint with particularity.[230] Therefore, "[i]t follows that facts not stated with the requisite particularity cannot be considered in determining whether the strong-inference test is met."[231] However, the Court allowed the use of nonparticularized facts when it held that a court must consider all of the facts in determining whether a complaint meets

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[226] In re *GlenFed, Inc. Sec. Litig.*, 42 F.3d at 1545; *accord* Greenstone v. Cambex Corp., 975 F.2d 22, 25 (1st Cir. 1992) (according to Federal Rule of Civil Procedure Rule 9(b) the facts constituting fraud must be pled with particularity); Shields v. Citytrust Bancorp, Inc., 25 F.3d 1124, 1127-28 (2nd Cir 1994) (holding when fraud is asserted the complaint must meet the requirements of Federal Rule of Civil Procedure 9(b)); FED. R. CIV. P. 9(b).

[227] H.R. REP. NO. 104-369, at 31 (Conf. Rep.).

[228] H.R. REP. NO. 104-369, at 31 (Conf. Rep.).

[229] 15 U.S.C. § 78u-4(b)(2) (2006).

[230] *See* A Lingering Thought on Tellabs, *supra* note 176 (stating the language of the statute implies that only facts pled with particularity can be used to meet the strong inference standard); *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring); *see also Winer Family Trust*, 503 F.3d at 327 (stating "Congress did not merely require plaintiffs to 'provide a factual basis for [their] scienter allegations'. . . . Congress required plaintiffs to plead with particularity facts that give rise to a 'strong'—*i.e.,* a powerful or cogent-inference."); Key Equity Investors, Inc. v. SEL-LEB Mktg., Inc., 246 Fed. Appx. 780, 785 (3d Cir. 2007) (holding plaintiff may not benefit from vague or ambiguous facts that do not live up to the PSLRA's particularity requirement); *Gompper*, 298 F.3d at 896-97 (stating the PSLRA clearly states that only those facts pled with particularity must give rise to a "strong inference" of scienter); In re *K-tel Int'l, Inc. Sec. Litig.*, 300 F.3d at 889 (stating the PSLRA only allows those facts pled with particularity to be used in determining if the plaintiff met the "strong inference" standard); In re *Rockefeller Ctr. Properties, Inc. Sec. Litig.*, 311 F.3d at 224 (stating according to the PSLRA the "strong inference" standard must be met by those facts pled with particularity); Brief of Technet, *supra* note 186, at 12; Brief for the United States, *supra* note 54, at 21.

[231] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring); *see Key Equity Investors, Inc.*, 246 Fed. Appx. at 785 (holding plaintiff may not benefit from vague or ambiguous facts that do not live up to the PSLRA's particularity requirement); California Pub. Employees' Ret. Sys. v. Chubb Corp., 394 F.3d 126, 145 (3d Cir. 2004) (holding plaintiff may only benefit from particular facts and cannot benefit from vague facts in meeting the PSLRA's "strong inference" standard); *Gompper*, 298 F.3d at 896-97 (stating the PSLRA requires facts pled with particularity to give rise to a "strong inference" of scienter, thus facts not pled with the requisite particularity will not suffice) *In re* Navarre Corp. Sec. Litig., 299 F.3d 735, 741 (8th Cir. 2002) (holding the court must disregard ambiguous facts that do not live up to the PSLRA's "particularity" requirement); Brief of Technet, *supra* note 186, at 12; Brief for the United States, *supra* note 54, at 21-22; A Lingering Thought on *Tellabs*, *supra* note 176.

the "strong inference" standard.[232] Thus, the Court's interpretation did not follow the statute's plain language because it did not limit the consideration of facts to only those facts pled with particularity.[233] Conversely, Justice Alito's interpretation correctly followed the plain language of the statute by only allowing those facts pled "with particularity" to be viewed in determining whether the "strong inference" had been met.[234] Therefore, Justice Alito's interpretation proved proper.[235]

The Tellabs *Impact on the Tenth Circuit*

The *Tellabs* decision received mixed reactions; some articles announced a win for corporate America, while others proclaimed no clear win for either side.[236] Although the overall impact may not materialize for some time, the potential influence of *Tellabs* on the Tenth Circuit deserves discussion.

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[232] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring); *Id*. at 2511. After the Court noted that ambiguities count against inferring scienter, the Court "reiterate[d], however, that the court's job is not to scrutinize each allegation in isolation but to assess all the allegations holistically." *Id.* at 2511; *see* A Lingering Thought on *Tellabs*, *supra* note 176 (stating the Court ignored the particularity requirement); Gregg L. Weiner, Esq., *Supreme Court Raises The Bar For Securities Fraud Plaintiffs, But Questions Remain*, 18 No. 1 ANMALAR 12, 4 (2007) (stating the Court allows the use of ambiguous facts in determining if plaintiff met the strong inference requirement).

[233] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring); *see* A Lingering Thought on *Tellabs*, *supra* note 176, (stating the statutory language implies that only facts pled with particularity can be used to meet the strong inference standard, which the Court failed to follow); *see also Key Equity Investors, Inc.*, 246 Fed. Appx. at 785 (holding plaintiff may not benefit from vague or ambiguous facts that do not live up to the PSLRA's particularity requirement); *Gompper*, 298 F.3d at 896-97 (stating the PSLRA clearly requires that facts must be pled with particularity to give rise to a "strong inference" of scienter); In re *K-tel Int'l, Inc. Sec. Litig.*, 300 F.3d at 889 (stating the PSLRA only allows facts pled with particularity to determine if the plaintiff met the "strong inference" standard); In re *Rockefeller Ctr. Properties, Inc. Sec. Litig.*, 311 F.3d at 224 (stating that according to the PSLRA the plaintiff must meet the "strong inference" standard by those facts pled with particularity).

[234] *Tellabs II*, 127 S. Ct. at 2516 (Alito, J., concurring); *see supra* note 233 and accompanying text; *California Pub. Employees' Ret. Sys.*, 394 F.3d at 145 (holding plaintiff may only benefit from particular facts and cannot benefit from vague facts in meeting the PSLRA's "strong inference" standard); *Florida State Bd. of Admin.*, 270 F.3d at 660 (holding the court must disregard ambiguous facts that do not live up to the PSLRA's "particularity" requirement).

[235] S*ee* A Lingering Thought on Tellabs, *supra* note 176 (stating Justice Alito's particularity argument follows the plain language of the statute which implies that only facts pled with particularity can be used to meet the strong inference standard); *see also Key Equity Investors, Inc.*, 246 Fed. Appx. at 785 (holding plaintiff may not benefit from vague or ambiguous facts that do not live up to the PSLRA's particularity requirement); *California Pub. Employees' Ret. Sys.*, 394 F.3d at 145 (holding plaintiff may only benefit from particular facts and cannot benefit from vague facts in meeting the PSLRA's "strong inference" standard); *Gompper*, 298 F.3d at 896-97(Congress was clear the language of the PSLRA requires facts to be pled with particularity); *Florida State Bd. of Admin.*, 270 F.3d at 660 (holding the court must disregard ambiguous facts that do not live up to the PSLRA's "particularity" requirement).

[236] *See, e.g.,* Weiner, *supra* note 232, at 4; Tellabs: *Securities Lawyers React*, http://blogs.wsj.com/law (June 21, 2007, 13:03 EST); Tony Mauro*, High Court Raises the Bar for Investors Alleging Securities Fraud* (June 22, 2007), http://biz.yahoo.com/law; Greg Stohr*, Top U.S. Court*

City of Philadelphia v. Fleming Companies, Inc., was the first securities fraud case the Tenth Circuit ruled on after the passage of the PSLRA.[237] The court began by rejecting the arguments upheld by the Second and Third Circuits; these arguments held "pleading motive and opportunity, without more, provides an alternative method to establish scienter."[238] Instead, the Tenth Circuit followed the middle ground approach of the First and Sixth Circuits that required the court to "look to the totality of the pleadings to determine whether the plaintiffs' allegations permit a strong inference of fraudulent intent."[239] The court also noted plaintiffs could plead scienter by "setting forth facts raising a 'strong inference' of intentional *or* reckless misconduct."[240]

Pleading scienter in securities fraud continued to evolve in the Tenth Circuit.[241] Following the Tenth Circuit's decision in *Pirraglia v. Novell, Inc.*, the Tenth Circuit took a notable step in considering whether the plaintiffs met the scienter requirement.[242] The court held that in determining whether plaintiffs established scienter, it "'must consider *all* reasonable inferences to be drawn from the allegations, including inferences unfavorable to the plaintiffs.'"[243] However, the court rejected the Sixth Circuit's standard that "'plaintiffs are entitled only to the most plausible of competing inferences.'"[244] The court reasoned the Sixth Circuit's standard would "invade the traditional role of the fact finder."[245]

Major adjustments by the Tenth Circuit prove unnecessary to align with the pleading standards set forth in the *Tellabs* decision.[246] The Tenth Circuit currently looks at inferences unfavorable to the plaintiff to determine whether he or she met the scienter standard, but it does not weigh competing inferences.[247] Following the *Tellabs* decision, the Tenth Circuit must "consider all competing inferences

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Tightens Limits on Shareholder Suits (June 21, 2007), http://bloomberg.com; *Supreme Court Issues* Tellabs *Opinion,* http://dandodiary.blogspot.com/2007/06/supreme-court-issues-tellabs-opinion.html (June 22, 2007, 8:17 EST).

[237] City of Philadelphia v. Fleming Companies, Inc., 264 F.3d 1245, 1249 (10th Cir 2001).

[238] *Id.*

[239] *Id.* at 1261-62.

[240] *Id.* at 1259.

[241] *See* Pirraglia v. Novell, Inc., 339 F.3d 1182, 1187 (10th Cir. 2003) (holding the court must consider all reasonable inferences, including inferences favoring the defendant).

[242] *Id.*

[243] *Id.* (quoting *Gommper*, 298 F.3d at 897).

[244] *Pirraglia*, 339 F.3d at 1188 (quoting *Helwig*, 251 F.3d at 553).

[245] *Pirraglia*, 339 F.3d at 1188.

[246] *More* Tellabs *Thoughts: Does it Change D & O Exposure?,* http://dandodiary.blogspot.com (July 2, 2007 10:23 EST) (the author, Kevin LaCroix, has nearly 25 years of experience counseling clients concerning director and officer liability issues).

[247] *Pirraglia*, 339 F.3d at 1187-88.

of scienter which can be drawn from the complaint's factual allegations, and determine whether the inference suggested by the plaintiff is cogent and 'at least as compelling as any opposing inference of nonfraudulent intent.'"[248] Formerly, the Tenth Circuit felt this step would "invade the traditional role of the fact finder."[249] The Tenth Circuit's rule permitting the pleading of scienter through recklessness, however, will remain unchanged unless and until the Supreme Court takes a stance.[250]

CONCLUSION

When the United States Supreme Court developed a new test for determining whether the facts alleged have met the "strong inference" of scienter, the Court failed to follow the statute's plain language, thus frustrating Congress's intentions in enacting the statute.[251] The Court should have followed the strict test developed by many circuits and argued for by Justice Scalia in his dissent.[252] This test required the inference of scienter to be slightly stronger than the inference of no scienter.[253] Adopting Justice Scalia's test compared to the Court's test would eliminate a tie going to the plaintiff, thereby eliminating the potential for a future split in circuits on the application of the Court's test.[254] Furthermore, the Court's failure in only considering those facts pled with particularity, as argued for by Justice Alito, directly contradicts the statute's natural language.[255] This failure reduced the heightened pleading standard Congress intended in enacting the PSLRA by allowing plaintiffs to benefit from facts not pled with particularity.[256] Although the outcome of this test is currently unknown, time will likely prove that the Court's failures lead to another split among circuits.[257]

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[248] Britton v. Parker, 2007 WL 2871003, *4 (D. Colo. 2007) (quoting *Tellabs II*, 127 S. Ct. 2499, 2504-05 (2007)).

[249] *Pirraglia*, 339 F.3d at 1188.

[250] City of Philadelphia v. Fleming Companies, Inc., 264 F.3d 1245, 1259 (10th Cir 2001); *Tellabs II*, 127 S. Ct. at 2507 n.3; Ernst & Ernst v. Hochfelder, 425 U.S. 185, 194 n.12 (1976); *see supra* note 49.

[251] *See supra* notes 199-212, 217-223 and accompanying text.

[252] *See supra* notes 203-216 and accompanying text.

[253] *See supra* notes 203-212 and accompanying text.

[254] *See supra* notes 203-206 and accompanying text.

[255] *See supra* notes 225-234 and accompanying text.

[256] *See supra* notes 219-223 and accompanying text.

[257] *See supra* notes 199-202 and accompanying text.