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Southern District of New York Rejects 1933 Act Claims Based on Events Post-Dating an Issuer's Financial Statements

Issuer in April 2008 Offering Had No Duty To Disclose Additional Information Concerning Events of the First Quarter of 2008.

District Court Also Holds that Defendants Carried Their Burden of Proving that Class Period Share Price Declines Were Not Caused by Alleged Misrepresentations.

SUMMARY

In *In re Barclays Bank PLC Securities Litigation*, the U.S. District Court for the Southern District of New York (Crotty, J.) granted summary judgment to Barclays and the other defendants in a 1933 Act class action arising out of Barclays' April 8, 2008 offering of $2.5 billion of American Depositary Shares (ADS). Plaintiff's claims rested largely on purported omissions from the offering materials, which included Barclays' 2007 year-end financial statements. Specifically, plaintiff contended that Barclays had a duty to disclose additional information concerning (i) the valuations and writedowns of Barclays' mortgage-related assets; (ii) Barclays' exposure to monoline insurance counterparties; and (iii) changes in Barclays' capital ratios during the first quarter of 2008, just prior to the offering. The Court rejected these claims, holding that Barclays satisfied its disclosure obligations.

In the alternative, the Court held that Barclays had carried its burden of proving "negative causation," that is, that the ADS price declines during the class period were caused by factors other than the alleged misstatements and omissions.

BACKGROUND TO THE *BARCLAYS* DECISION

Lead Plaintiff's Section 11 claims in *In re Barclays Bank PLC Securities Litigation*, No. 09 Civ. 1989 (S.D.N.Y.), arose out of his purchase of American Depositary Shares (Series 5) issued by Barclays Bank PLC in April 2008. The offering materials consisted of (i) an August 31, 2007 shelf registration statement; and (ii) an April 8, 2008 prospectus supplement, which incorporated by reference (iii) Barclays' Form 20-F, dated March 26, 2008, containing the bank's consolidated financial statements for the fiscal year ended December 31, 2007.

Plaintiff purchased his shares in the offering at a price of $25 per share, and the price of the Series 5 ADS declined to a class period low of $4.95 on March 9, 2009. The first complaint challenging the offering was filed against Barclays on April 8, 2009.

No Duty To Disclose Additional Information

The April 2008 offering materials for the Series 5 ADS reflected significant writedowns (over £1.6 billion) that Barclays recorded as at December 31, 2007 on mortgage-related assets that had been impacted by turbulence in the credit markets. The offering materials also itemized Barclays' remaining exposure to vulnerable credit market assets (such as CDOs, subprime whole loans, Alt-A loans, and contracts with monoline insurer counterparties).

Nevertheless, plaintiff claimed that the Series 5 ADS offering materials omitted "critical information" in violation of Regulation S-K (Items 303 and 503) and applicable accounting rules (such as International Accounting Standard 10) governing disclosure of events post-dating Barclays' balance sheet date (December 31, 2007). With respect to each purported omission, Judge Crotty held that Barclays had no duty to disclose additional information.

First, plaintiff claimed that, in addition to the fair value of the monoline insurance (which was disclosed in the offering materials), Barclays was also required to disclose the "notional" amount of its monoline insurance contracts (i.e., the value of the underlying insured credit market assets). The Court rejected this theory holding that, under Second Circuit precedent, Barclays was under "no duty as a matter of law to disclose the notional amount of monoline exposure." In addition, a reasonable investor would have understood from the offering materials that Barclays was *not* disclosing the notional amount of monoline insurance. Even if the additional information "would have provided [investors with] a more complete assessment of Barclays' exposure to monoline insurers," Barclays was "not required to disclose a fact merely because a reasonable investor would very much like to know that fact."

Second, plaintiff claimed that Barclays' reported year-end 2007 valuations on its credit market assets were materially misleading by April 2008 because certain of those assets were written down (by approximately £1 billion) during the first quarter of 2008, just before the offering. The Court disagreed and, applying the Second Circuit's recent decision in *Stadnick* v. *Vivint Solar, Inc.*, 861 F.3d 31 (2d Cir.

2017), held that Regulation S-K Item 303's requirement of disclosing "known trends or uncertainties" did not require disclosure of Barclays' interim writedowns. The Court held that, even assuming Barclays had a duty to disclose the trend of deteriorating credit market positions (or of general market dislocation), Barclays satisfied that duty by identifying the trend and "specifically identifying different types and amount of assets as of 6/30/07 and 12/31/07. Given these disclosures, a reasonable investor would infer how continued credit market dislocation "might reasonably be expected to have a material impact on future revenues: the investor would conclude that these assets would be vulnerable to additional write-downs."

Judge Crotty also held that the purported omission of interim writedowns on certain of its assets (specifically, subprime and Alt-A positions) was immaterial in any event. A reasonable investor would look to the performance of the bank as a whole, and Barclays reported a pre-tax profit of £1.194 billion in the first quarter of 2008, which is a "more accurate indicator of Barclays' overall performance."

Finally, plaintiff claimed that Barclays was required, but failed, to disclose conversations between Barclays and its regulator (the FSA) concerning the bank's capital position during the first quarter of 2008. The Court held that Barclays had no duty to disclose its "continuous discussions" with regulators "regarding capital and contingency plans," particularly where there had been "no official regulatory action."

Negative Loss Causation

Alternatively, the Court granted Barclays summary judgment because, even assuming some or all of the alleged misrepresentations were actionable, Barclays had carried its burden on the affirmative defense of negative loss causation. Barclays showed that the declines in the Series 5 ADS over the course of the class period were not caused by the alleged misrepresentations in two ways.

First, on the dates the supposedly misstated or concealed information was disclosed, the Series 5 ADS price either increased or, on one date, decreased by an immaterial amount. The Court found that the market reaction showed "minimal materiality" and that the market "failed to react in any discernible way to the corrective revelations."

Second, Barclays offered an "event study" by an expert in finance proving—through regression analysis—that there was no statistically significant market reaction to the revelation of any "corrective" information. The Court found that Barclays' expert's methodology was consistent with industry standards and "convincingly illustrate[d]" the absence of loss causation. Noting that the class period included landmark events such as the collapse of Lehman Brothers, the Court also observed that the Series 5 ADS share price declines coincided with a "marketwide phenomenon causing comparable losses to other investors."

IMPLICATIONS

The District Court's decision granting summary judgment shows that courts will carefully analyze whether information purportedly "omitted" from offering materials was required to be disclosed under applicable standards and regulations. The decision also shows that courts will grant summary judgment on the issue of causation where there was no discernible market reaction to the revelation of the alleged misrepresentations, and the usefulness of an event study methodology in proving the absence of causation.

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