16-250-cv

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

PENSION FUNDS,

Plaintiff,

ARKANSAS TEACHERS RETIREMENT SYSTEM, WEST VIRGINIA INVESTMENT MANAGEMENT BOARD, PLUMBERS AND PIPEFITTERS PENSION GROUP,

(Caption Continued on the Reverse)

PURSUANT TO JANUARY 26, 2016 ORDER GRANTING PERMISSION TO APPEAL
FROM AN ORDER GRANTING CERTIFICATION OF CLASS ENTERED ON SEPTEMBER 24, 2015
BY THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK
NO. 10 CIV. 3461 (PAC)
THE HONORABLE PAUL A. CROTTY

BRIEF OF *AMICUS CURIAE* SECURITIES INDUSTRYAND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF DEFENDANTS-APPELLANTS

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Plaintiffs-Appellees,

v.

GOLDMAN SACHS GROUP, INC., LLOYD C. BLANKFEIN, DAVID A. VINIAR, GARY D. COHN,

Defendants-Appellants,

SARAH E. SMITH,

Defendant.

CORPORATE DISCLOSURE STATEMENT

Pursuant to Fed. R. App. P. 26.1, the Securities Industry and Financial Markets Association hereby states that it has no parent corporation and that no publicly held corporation owns 10% of its stock.

TABLE OF CONTENTS

Page

CORPORATE DISCLOSURE STATEMENT i

INTEREST OF *AMICUS CURIAE* 1

INTRODUCTION 1

BACKGROUND AND SUMMARY OF THE ARGUMENT 5

ARGUMENT 10

I. THE DISTRICT COURT PERMITTED PLAINTIFFS TO CIRCUMVENT THE RELIANCE ELEMENT OF 10b-5 LIABILITY 10

A. The District Court Erred by Certifying a Class of Plaintiffs Who, as a Matter of Law, Would Not Have Relied on the Alleged Misstatements 11

B. The District Court Imposed an Excessive Burden of Proof on Defendants 13

C. The District Court Erred in Requiring Defendants to Disprove Plaintiffs' Price Maintenance Theory............................ 15

D. The District Court Erred by Refusing to Consider Evidence Because It Is Relevant to the Merits 17

II. THE CLASS CERTIFICATION ORDER SHOULD BE VACATED BECAUSE PLAINTIFFS' DAMAGES MODEL IS ARBITRARY 19

A. *Comcast* Requires a Non-Arbitrary, Classwide Method of Determining Damages Caused by Actionable Conduct................. 21

B. Plaintiffs' Damages Model Fails to Satisfy the Requirements of *Comcast*.. 23

C. The District Court Improperly Accepted Plaintiffs' Promise to Fix Their Damages Model as Sufficient for Class Certification 25

CONCLUSION 28

TABLE OF AUTHORITIES

Page(s)

Cases

Amgen Inc. v. *Conn. Ret. Plans and Trust Funds*,
133 S. Ct. 1184 (2013)....................2, 18

AT&T Mobility LLC v. *Concepcion*,
563 U.S. 333 (2011)....................18

Basic Inc. v. *Levinson*,
485 U.S. 224 (1988).................... *passim*

In re Blood Reagents Antitrust Litig.,
783 F.3d 183 (3d Cir. 2015) 27

Boca Raton Firefighters & Police Pension Fund v. *Bahash*,
506 F. App'x 32 (2d Cir. 2012) 6

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2013 WL 6388408 (S.D. Tex. Dec. 6, 2013)....................24

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2014 WL 2112823 (S.D. Tex. May 20, 2014)....................25, 26

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394 F.2d 416 (1st Cir. 1968)....................12

Butler v. *Sears, Roebuck & Co.*,
727 F.3d 796 (7th Cir. 2013) 27

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750 F.3d 227 (2d Cir. 2014) 6

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511 U.S. 164 (1994)....................2

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752 F.3d 173 (2d Cir. 2014) 6, 11

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133 S. Ct. 1426 (2013).. *passim*

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437 U.S. 463 (1978)..19

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250 F.R.D. 137 (S.D.N.Y. 2008)...16

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553 F.3d 187 (2d Cir. 2009) 6, 13

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309 F.R.D. 251 (N.D. Tex. 2015)..18

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114 F.3d 1332 (2d Cir. 1997) 14

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2016 WL 1425807 (8th Cir. Apr. 12, 2016)..3, 15, 16

Ind. Pub. Ret. Sys. v. *SAIC, Inc.*,
2016 WL 1211858 (2d Cir. Mar. 29, 2016)...6

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471 F.3d 24 (2d Cir. 2006) 12

Jacob v. *Duane Reade, Inc.*,
293 F.R.D. 578 (S.D.N.Y. 2013)...23

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299 F.R.D. 133 (N.D. Tex. 2014)..27

Ludlow v. *BP, p.l.c.*,
800 F.3d 674 (5th Cir. 2015) 20, 21, 22

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274 F.R.D. 480 (S.D.N.Y. 2011)....................15, 16

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259 F.3d 154 (3d Cir. 2001)....................19

In re POM Wonderful LLC,
2014 WL 1225184 (C.D. Cal. Mar. 25, 2014)....................23

In re Processed Egg Prods. Antitrust Litig.,
2016 WL 410279 (E.D. Pa. Feb. 3, 2016)....................23, 27

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725 F.3d 244 (D.C. Cir. 2013)....................27

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574 F. App'x 21 (2d Cir. 2014)....................6

Richman v. *Goldman Sachs Grp., Inc.*,
868 F. Supp. 2d 261 (S.D.N.Y. 2012)....................21, 24

Roach v. *T.L. Cannon Mgmt. Corp.*,
778 F.3d 401 (2d Cir. 2015)....................22

Roovers v. *Colvin*,
2015 WL 347749 (E.D. Wis. Jan. 26, 2015)....................14

Scott v. *Gen. Motors Co.*,
605 F. App'x 52 (2d Cir. 2015)....................6

SEC v. *Tambone*,
597 F.3d 436 (1st Cir. 2010)....................4

Sicav v. *James Jun Wang*,
2015 WL 268855 (S.D.N.Y. Jan. 21, 2015)....................22

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552 U.S. 148 (2008)....................1

Strougo v. *Barclays PLC*,
312 F.R.D. 307 (S.D.N.Y. 2016)....................3

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780 F.3d 70 (2d Cir. 2015) 23

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729 F.3d 108 (2d Cir. 2013) 23

Statutes

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INTEREST OF *AMICUS CURIAE*

The Securities Industry and Financial Markets Association ("SIFMA") is a securities industry trade association representing the interests of hundreds of securities firms, banks, and asset managers.[1] Its mission is to support a strong financial industry, while promoting investor opportunity, capital formation, job creation, economic growth, and trust and confidence in the financial markets. SIFMA is the United States regional member of the Global Financial Markets Association. It regularly files *amicus curiae* briefs in cases such as this one that raise issues of vital concern to securities industry participants.[2] This case involves important issues concerning standards for class certification in private securities actions, which are directly relevant to SIFMA's mission of promoting fair and efficient markets and a strong financial services industry.

INTRODUCTION

Recognizing the "practical consequences of an expansion" of liability under the federal securities laws—including "allow[ing] plaintiffs with weak

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[1] The parties have consented to the filing of this brief. Pursuant to Fed. R. App. P. 29(c)(5), the undersigned counsel certify that no party's counsel authored this brief in whole or in part; no party or party's counsel, or any other person, other than *amici* or their counsel, contributed money that was intended to fund the preparation or submission of this brief.

[2] These cases include *Halliburton Co*. v. *Erica P. John Fund, Inc.*, 134 S. Ct. 2398 (2014) and *Comcast Corp.* v. *Behrend*, 133 S. Ct. 1426 (2013).

claims to extort settlements from innocent companies," *Stoneridge Inv. Partners, LLC* v. *Scientific-Atlanta, Inc*., 552 U.S. 148, 163-64 (2008)—the Supreme Court and this Court have, in ruling on claims under Section 10(b), sought a balance between appropriate enforcement of the law and weeding out non-meritorious suits. The District Court's ruling, which certified a sweeping class, disrupts that careful balance in two distinct ways. First, it circumvents the reliance requirement, which is intended to "ensure[] that there is a proper connection between a defendant's misrepresentation and a plaintiff's injury." *Amgen Inc*. v. *Conn. Ret. Plans and Trust Funds*, 133 S. Ct. 1184, 1192 (2013) (quoting *Erica P. John Fund, Inc*. v. *Halliburton Co.*, 131 S. Ct. 2179, 2184-85 (2011) (*Halliburton I*)); *Cent. Bank of Denver, N.A*. v. *First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 180 (1994). Second, it certified a class even though Plaintiffs failed, in contravention of *Comcast Corp.* v. *Behrend*, 133 S. Ct. 1426 (2013), to put forward a non-arbitrary, classwide method of measuring damages; in so doing, the court below eviscerated the predominance requirement of Federal Rule of Civil Procedure 23.

With regard to reliance, all of the statements at issue in this case are general statements about reputation, integrity and conflicts controls. This Court has repeatedly held that such statements are inactionable and have no market impact as a matter of law, because no reasonable investor relies on them. Notwithstanding the Supreme Court's ruling that defendants can rebut the fraud-on-the-market presumption of reliance through "evidence that an alleged misrepresentation did not actually affect the market price of the stock," *Halliburton Co.* v. *Erica P. John Fund, Inc*., 134 S. Ct. 2398, 2417 (2014) (*Halliburton II*), the District Court certified a class based on alleged reliance on these vague, aspirational statements. The District Court compounded its error by subjecting Defendants' rebuttal under *Halliburton II* to a high standard of proof previously unknown in civil litigation, and rejecting admissible evidence of an absence of price impact in favor of unsupported speculation.

The impact of the District Court's error on this point is not limited to this one decision; indeed, it has already been cited in support of a similarly erroneous ruling by another District Court in this Circuit, *Strougo* v. *Barclays PLC*, 312 F.R.D. 307, 324 & n.110 (S.D.N.Y. 2016), *motion for review pursuant to Fed. R. Civ. P. 23(f) pending*, No. 16-450 (2d Cir.). The ruling below, if allowed to stand, would render it nearly impossible for defendants to exercise their right under *Halliburton II* to rebut the fraud-on-the-market presumption of reliance. The ruling below also conflicts with a recent ruling of the Eighth Circuit in *IBEW Local 98 Pension Fund* v. *Best Buy Co.*, 2016 WL 1425807 (8th Cir. Apr. 12, 2016). This Court—the foremost authority on federal securities laws—should set litigation applying *Halliburton II* on a path consistent with the language and purpose of that decision. It should firmly reject the standard adopted by the

District Court, which effectively writes the reliance requirement out of Section 10(b) litigation.

The District Court's class certification order also violates the Supreme Court's holding in *Comcast*, where the Supreme Court held that, before certification of a liability and damages class like this one, plaintiffs must put forward a classwide method of measuring damages. Here, Plaintiffs did not introduce a damages model that predicts the prices at which the stock of The Goldman Sachs Group, Inc. ("Goldman") allegedly would have traded but for the alleged misrepresentations on which Plaintiffs rely. Rather, Plaintiffs' expert merely promised such a damages calculation at some future time. This is insufficient. If followed, this ruling would effectively eliminate the predominance requirement of Rule 23, and would turn companies into insurers of losses arising out of inactionable events that coincide with alleged securities law violations.

"No one sophisticated about markets believes that multiplying liability is free of cost." *SEC* v. *Tambone*, 597 F.3d 436, 452 (1st Cir. 2010) (Boudin, J., concurring). The cost of abusive class actions inevitably "gets passed along to the public." *Id.* This is especially the case in securities class actions, where if classes survive dismissal and are certified, even weak cases can result in "blackmail settlements" induced by a small probability of an immense judgment. *Cf.* Henry J. Friendly, *Federal Jurisdiction: A General View* 120 (1973) (noting that class actions risk "recoveries that would ruin innocent shareholders or, what is more likely . . . blackmail settlements").[3] We respectfully submit that this Court should preserve the careful limits that the Supreme Court and this Court have imposed on securities litigation.

BACKGROUND AND SUMMARY OF THE ARGUMENT

Plaintiffs' Complaint alleged that on four dates during the spring of 2010, the price of Goldman Sachs' stock dropped in response to announcements about government investigations and enforcement actions concerning Goldman's marketing of four collateralized debt obligations ("CDOs"), including allegations that Goldman had conflicts of interests with customers for those CDOs. Plaintiffs, investors in Goldman common stock, contend that share price declines following news of government enforcement activity reflected the market's realization that

[3] *See also* Tom Baker & Sean J. Griffith, *How the Merits Matter: Directors' and Officers' Insurance and Securities Settlements*, 157 U. Pa. L. Rev. 755, 757-58 (2009) (observing that it is widely believed that the merits of securities fraud claims are essentially irrelevant to settlement of securities class actions); Geoffrey Rapp, *Rewiring the DNA of Securities Fraud Litigation:* Amgen*'s Missed Opportunity*, 44 Loy. U. Chi. L.J. 1475, 1478 (2013) ("[B]ecause securities litigation is so high risk for defendants, these cases—should they survive motions to dismiss and obtain class certification—will almost always settle."); Denise N. Martin et al., *Recent Trends IV: What Explains Filings and Settlements in Shareholder Class Actions*, 5 Stan. J.L. Bus. & Fin. 121, 156 (1999) ("Generally, we find that the merits do not have much, if any, explanatory power on settlement size."); Janet Cooper Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 Stan. L. Rev. 497, 523 (1991) (study of securities class action settlements concluding that "the merits did not affect the settlement amounts").

disclosure of alleged conflicts demonstrated the falsity of Goldman's prior general representations about its ethical principles, integrity, and commitment to putting client interests first.

After the District Court refused to dismiss the claims as non-actionable under this Court's precedents,[4] Plaintiffs supported their class certification request by relying on the fraud-on-the-market presumption of reliance created by *Basic Inc.* v. *Levinson*, 485 U.S. 224 (1988). Defendants, in accordance with *Halliburton II*, rebutted the *Basic* presumption by showing that the alleged misstatements did not affect the price of Goldman's shares. Defendants established that:

- The alleged misstatements—vague aspirational statements about Goldman's business principles and conflicts-of-interest controls[5]—could not have impacted the price of Goldman's stock in light of this Court's

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4 *See City of Pontiac Policemen's & Firemen's Ret. Sys.* v. *UBS AG*, 752 F.3d 173, 185-86 (2d Cir. 2014); *ECA & Local 134 IBEW Joint Pension Trust of Chi.* v. *JP Morgan Chase Co.*, 553 F.3d 187, 205-06 (2d Cir. 2009); *Boca Raton Firefighters & Police Pension Fund* v. *Bahash*, 506 F. App'x 32, 37 (2d Cir. 2012) (summary order); *Reese* v. *Bahash*, 574 F. App'x 21, 23 (2d Cir. 2014) (summary order); *Carpenters Pension Trust Fund of St. Louis* v. *Barclays PLC*, 750 F.3d 227, 235-36 (2d Cir. 2014); *Scott* v. *Gen. Motors Co*., 605 F. App'x 52, 54 (2d Cir. 2015) (summary order); *Ind. Pub. Ret. Sys.* v. *SAIC, Inc.*, 2016 WL 1211858, at *10 (2d Cir. Mar. 29, 2016).

5 The alleged misstatements at issue included: "We have extensive procedures and controls that are designed to . . . address conflicts of interest[,]" "we increasingly have to address potential conflicts of interest . . ." and "[o]ur clients' interests always come first." (SPA2.)

repeated rulings that reasonable investors do not as a matter of law rely upon such statements.

- None of the alleged misstatements caused an increase in the price of Goldman's shares when made.
- The magnitude of each price drop associated with the alleged corrective disclosures was attributable to the news that Goldman was the subject of enforcement actions, rather than to the alleged falsity of earlier general representations concerning the integrity of the firm.
- On 34 dates before the date of the first alleged corrective disclosure, revelations that Goldman purportedly acted contrary to its clients' interests caused zero movement in the price of its shares.

The District Court nonetheless adhered to its view that the statements at issue were actionable, held that Defendants had not successfully rebutted the *Basic* presumption by showing an absence of price impact, and certified the class.

The Court's ruling was based on several errors of law: First, the Court committed an overarching error in imposing upon Defendants the burden of coming forward with "conclusive evidence" that is "inconsistent" with any inference of price impact. (SPA12-13.) The Court's demand for such conclusive evidence effectively required Defendants to rebut the presumption by at least proof beyond a reasonable doubt—a standard that is unknown in civil litigation.

Second, the District Court characterized Defendants' showing that the alleged misstatements failed to move the stock price as "insignificant," accepting Plaintiffs' speculation that on the date of each alleged misstatement, the price of Goldman's shares would have dropped but for the statement. (SPA11.) But requiring Defendants to disprove the speculative "price maintenance" theory renders *Halliburton II* a nullity. Some degree of price maintenance can be asserted in every case if unsupported speculation is treated as good currency; one can always imagine that the stock price might have dropped, or dropped more, had the alleged truth been disclosed.

Third, the District Court erroneously rejected Defendants' showing that the magnitude of each price drop was fully explained by news about enforcement activity. This showing was based on an empirical study of market reactions to such news in other cases. The District Court held this evidence insufficient because it did not "conclusively" exclude the possibility that, in this case, the correction of earlier alleged misstatements caused some portion of each price drop. (SPA12-13.) The District Court thus appears to have unfairly tested Defendants' evidence against a standard even higher than reasonable doubt, which far exceeds Defendants' burden under Federal Rule of Evidence 301.

Fourth, the District Court discarded Defendants' undisputed showing that news about conflicts of interests between Goldman and its clients has historically not been associated with share price declines. The District Court excluded this evidence based on its misunderstanding that the evidence could be relevant only to a truth-on-the-market defense on the element of materiality, which the District Court deemed inappropriate for consideration at the class certification stage. The point of the evidence, however, was to show that news concerning conflicts of interests did not contribute to decreases in the price of Goldman's stock. The District Court's holding is directly contrary to *Halliburton II*, which expressly acknowledged that direct evidence of price impact will always be "highly relevant at the merits stage," but held that defendants must also be afforded a price impact rebuttal at class certification. 134 S. Ct. at 2416-17.

The District Court's reasoning, in conflict with *Halliburton II*, is a recipe for the automatic certification of a class in every securities law case involving a government enforcement action that is followed by a stock-price drop—regardless of how the price moves at other relevant times. It would render rebuttal of the fraud-on-the-market presumption virtually impossible, by elevating speculation above evidence. Nearly all enforcement actions are associated with significant stock-price drops, and nearly all companies have made general statements about integrity or ethical compliance that could be deemed "corrected" by such enforcement actions. Under the District Court's reasoning, so long as the stock price drops after the regulatory action is announced, the class will be certified—regardless of (1) the lack of price impact when the statements were made, (2) the lack of price impact when disclosures of allegedly concealed facts were made, and (3) whether the price movement is consistent with the price impact of news of an enforcement action.

The District Court also certified the class in contravention of the Supreme Court's holdings in *Comcast*. Instead of requiring Plaintiffs to come forward with a non-arbitrary, classwide method of measuring damages in order to satisfy the predominance requirement in Rule 23, the Court certified the class based on Plaintiffs' promise to do so, eventually. That is not a sufficient basis for class certification.

ARGUMENT

I. THE DISTRICT COURT PERMITTED PLAINTIFFS TO CIRCUMVENT THE RELIANCE ELEMENT OF 10b-5 LIABILITY

In *Halliburton II*, the Supreme Court, consistent with its long-standing insistence upon "a proper connection between a defendant's misrepresentation and a plaintiff's injury" in order to respect the careful limits on Rule 10b-5 liability, held that a defendant may rebut the *Basic* presumption before class certification with "[a]ny showing that severs the link between the alleged misrepresentation and . . . the price received (or paid) by the plaintiff." *Halliburton II*, 134 S. Ct. at 2407, 2415. Such a showing, the Court said, would eliminate "the basis for finding that the fraud had been transmitted through market price." *Id.* at 2415-16. Here, Defendants severed the link by showing that the alleged misrepresentations on which Plaintiffs claimed to have relied had no impact on the price of Goldman's shares as a matter of law or fact. The District Court, however, imposed an erroneous and onerous burden of proof and made other errors of law. The aggregate effect of these errors was effectively to nullify *Halliburton II*, upsetting the careful balance established by the Supreme Court and this Court to uphold the securities laws while at the same time protecting defendants from frivolous suits.

A. The District Court Erred by Certifying a Class of Plaintiffs Who, as a Matter of Law, Would Not Have Relied on the Alleged Misstatements

Defendants "severed the link" as a matter of law by showing under this Court's precedents that the alleged misrepresentations—general aspirational disclosures about Defendants' business principles, policies and procedures for dealing with conflicts of interest—are the types of "general statements about reputation, integrity, and compliance with ethical norms [that] are inactionable puffery, meaning that they are too general to cause a reasonable investor to rely upon them." *City of Pontiac Policemen's & Firemen's Ret. Sys.* v. *UBS AG*, 752 F.3d 173, 183 (2d Cir. 2014) (internal quotation marks omitted). This showing alone rebutted Plaintiffs' claim of classwide reliance because by definition, such inactionable statements could not have affected the stock price. If, however, Defendants' general business statements are deemed actionable and somehow capable of affecting stock price, then virtually any statements by companies, no matter how imprecise or aspirational, could serve as the predicate for certification of a securities class action. Such a result would have the unfortunate effect of magnifying the burden on the economy of non-meritorious securities lawsuits.

The District Court erroneously rejected Defendants' showing because (1) the Court had previously rejected it at the motion to dismiss stage; and (2) Defendants' showing overlaps with materiality, a merits issue. (SPA12 n.5.) But the District Court is not bound to its previous erroneous rulings,[6] particularly in light of this Court's intervening rulings on the inactionability of puffery. And courts cannot disregard arguments against certification because they overlap with merits issues. *Comcast*, 133 S. Ct. at 1432; *In re Initial Pub. Offerings Sec. Litig.*, 471 F.3d 24, 27 (2d Cir. 2006). Goldman's showing speaks directly to Plaintiffs' inability to establish reliance as a matter of law; any overlap with materiality does not diminish Defendants' right under *Hallburton II* to rebut the presumption on reliance grounds.

Indeed, the District Court's error, if uncorrected, would undermine the objectives of federal securities laws and contravene clear Supreme Court precedent. If the scope of securities laws is expanded so that puffery statements may serve as the basis for securities class actions, the reliance requirement will have been effectively written out of Section 10(b) litigation, rendering defendants'

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[6] *See Burns* v. *Mass. Inst. of Tech.*, 394 F.2d 416, 418 (1st Cir. 1968) ("[A] court [is] not bound to perpetuate error if it later believed it had committed such.").

rebuttal rights under *Hallburton II* a nullity. *See ECA*, 553 F.3d at 206 ("declin[ing] to broaden the scope of securities laws" to include statements of puffery and "many routine representations made by investments institutions" because such statements, as a matter of law, "are too general to cause a reasonable investor to rely").[7]

B. The District Court Imposed an Excessive Burden of Proof on Defendants

The District Court noted that a defendant may rebut the *Basic* presumption by establishing, by a preponderance of the evidence, that the alleged misstatements on which a plaintiff relies did not affect the price of the securities at issue. (SPA6 n.3.) However, it then proceeded to impose a much higher and virtually unachievable evidentiary burden on Goldman.

Defendants rebutted the *Basic* presumption by showing that (1) the stock price did not react when the statements at issue were made, (2) the price did not react when the news regarding Goldman's alleged conflicts of interest was previously and repeatedly disclosed, and (3) the subsequent price reactions that occurred years later were attributable to other causes. The District Court found

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[7] "Completely eliminating the requirement of reliance, however, would mark a radical departure from rule 10b-5's traditional underpinnings and should not be undertaken by the judiciary." Barbara Black, *Fraud on the Market: A Criticism of Dispensing with Reliance Requirements in Certain Open Market Transactions*, 62 N.C. L. Rev. 435, 472 (1984).

Defendants' showing insufficient on the ground that it did not include "conclusive evidence" logically "inconsistent" with any possibility that the statements caused a portion of each price drop: "Defendants' attempt to demonstrate a lack of price impact . . . does not provide conclusive evidence that no link exists between the price decline and the misrepresentation." (SPA12-13 (citing *Aranaz* v. *Catalyst Pharm Partners Inc.*, 302 F.R.D. 657, 672 (S.D. Fla. 2014)) (Defendants "must show that price impact is *inconsistent* with the results of their analysis").)

By demanding "conclusive evidence," the District Court erroneously applied a standard even higher than the "beyond a reasonable doubt" standard applicable in criminal cases. *See Roovers* v. *Colvin*, 2015 WL 347749, at *5 (E.D. Wis. Jan. 26, 2015) ("Even in criminal cases where the burden of proof is beyond a reasonable doubt, conclusive evidence is not required to sustain the verdict."). This demand is inconsistent with Federal Rule of Evidence 301. That Rule provides: "In a civil case, unless a federal statute or these rules provide otherwise, the party against whom a presumption is directed has the burden of producing evidence to rebut the presumption. But this rule does not shift the burden of persuasion, which remains on the party who had it originally." A party produces sufficient evidence to rebut a presumption when it provides "[a]ny legitimate . . . reason" for the contested event. *Fisher* v. *Vassar Coll.*, 114 F.3d 1332, 1335-36

(2d Cir. 1997), *abrogated on other grounds by Reeves* v. *Sanderson Plumbing Prods., Inc.*, 530 U.S. 133 (2000).

C. The District Court Erred in Requiring Defendants To Disprove Plaintiffs' Price Maintenance Theory

An additional basis for vacating the District Court's order is its rejection of evidence in favor of unsupported conjecture that, but for the alleged misstatements, the price of Goldman Sachs' shares would have declined on each of the dates those statements were made. The District Court's holding would enable plaintiffs to circumvent *Halliburton II* simply by uttering the words "price maintenance" in every case.

The Eighth Circuit recently held that lack of price movement is enough to "sever the link." *Best Buy*, 2016 WL 1425807, at *7 ("Here, defendants rebutted the Basic presumption by submitting direct evidence . . . that severed any link between the alleged . . . misrepresentations and the stock price at which plaintiffs purchased."). The highly respected author of a leading treatise on class actions agrees: "Speculation that . . . statements maintained or slowed the rate of decline should give way to an evidentiary showing of no price impact of the challenged statement when made." 1 Joseph M. McLaughlin, *McLaughlin on Class Actions* § 5:26 (12th ed. 2015); *see also In re Moody's Corp. Sec. Litig.*, 274 F.R.D. 480, 492 (S.D.N.Y. 2011) (holding that an event study showing "no statistically significant change in Moody's value when any alleged misrepresentation was made . . . would rebut the presumption").

Courts in this Circuit have recognized that the price maintenance theory—and certainly its mere unsupported invocation—cannot alone be the basis for class certification because, by its nature, "there is no way to test" it and "it is based not on facts but on speculation." *In re Credit Suisse First Boston Corp. (Lantronix, Inc.) Analyst Sec. Litig.*, 250 F.R.D. 137, 145 (S.D.N.Y. 2008). Thus, courts have properly held that the *Basic* presumption is sufficiently rebutted by proof that alleged misstatements caused no price change.

Moreover, the "fraud on the market presumption is based upon the notion that the market was [fed] misinformation, absorbed that information and the stock price increased because of that misinformation." *Moody's*, 274 F.R.D. at 493; *see also Best Buy*, 2016 WL 1425807, at *6. If a misstatement does not cause a price increase, then an investor who relies upon price integrity would have made the same assumption about the value of the stock had the defendant made no misstatement. In such a case, if the statement had not been made, the "more plausible counterfactual" is one where "the issuer chose (lawfully) to stay silent," which also would have resulted in price maintenance.[8]

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[8] Donald C. Langevoort, *Judgement Day for Fraud-on-the-Market: Reflections on* Amgen *and the Second Coming of* Halliburton, 57 Ariz. L. Rev. 37, 57

In any case, to the extent that Defendants were required to disprove price maintenance, they amply did so. That proof reduces the price maintenance theory here to implausible and baseless speculation.

D. The District Court Erred by Refusing to Consider Evidence Because It Is Relevant to the Merits

The District Court mistook Defendants' evidence of the lack of price impact on 34 dates with public allegations of Goldman Sachs' conflicts of interest for a "truth on the market" defense, which the Court deemed inappropriate "at the current stage of the litigation." (SPA11.) The evidence, however, was not offered to show "truth on the market." That affirmative defense requires proof that the truth "credibly entered the market *and dissipated the effects of the misstatements*," thus providing a defense against "those who traded . . . after the corrective statements." *Basic*, 485 U.S. at 249 (emphasis added). Here, Defendants were not arguing that the prior disclosures undid the effects of the prior alleged misstatements by deflating Goldman's stock price. Instead, Defendants showed that the 34 other disclosures had no effect on share price to support the inference that the statements at issue and alleged corrective disclosures also had no price impact. On remand in *Halliburton II*, the Court expressly distinguished between a "truth on the market" defense, which that Court refused to consider at this stage,

(2015); *see also Basic*, 485 U.S. at 239 n.17 ("Silence, absent a duty to disclose, is not misleading under Rule 10b-5.").

Erica P. John Fund, Inc. v. *Halliburton Co.*, 309 F.R.D. 251, 261 (N.D. Tex. 2015), and this type of price impact rebuttal, which that Court accepted, *id.* at 273.

Even if the District Court were correct that the evidence supporting Defendants' rebuttal might also be relevant to the merits, it still should have considered it. In *Halliburton II*, the Supreme Court specifically acknowledged that price impact will be "highly relevant at the merits stage," but ruled that defendants must be afforded such a rebuttal nonetheless. 134 S. Ct. at 2417-18.[9]

Defendants' right to rebut price impact is critical since "[t]he fact that a misrepresentation . . . had price impact . . . is *Basic*'s fundamental premise." *Halliburton II*, 134 S. Ct. at 2416 (citation omitted). The *Halliburton II* right of rebuttal provides a defendant with an important "opportunity to show that plaintiffs' fraud allegations had no impact on the stock's price before that defendant is forced to make the difficult trade-off of yielding to settlement pressures if the proposed class is certified or potentially expending substantial resources in defense of the claim at the merits stage."[10] *Halliburton II* and its right

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9 *See also* Langevoort, *supra*, at 47 ("[*Halliburton II*] concedes that [price impact] is a class-wide issue . . . . In this sense, the Court is clearly backtracking on both *Amgen* and *Halliburton I*.").

10 Victor E. Schwartz & Christopher E. Appel, *Rebutting the Fraud on the Market Presumption in Securities Fraud Class Actions:* Halliburton II *Opens the Door*, 5 Mich. Bus. & Entrepreneurial L. Rev. 33, 58 (2015). *See also AT&T Mobility LLC* v. *Concepcion*, 563 U.S. 333, 350 (2011) ("[W]hen damages allegedly owed to tens of thousands of potential claimants are aggregated and decided at

of rebuttal serve an essential gatekeeping function in weeding out meritless claims.[11]

II. THE CLASS CERTIFICATION ORDER SHOULD BE VACATED BECAUSE PLAINTIFFS' DAMAGES MODEL IS ARBITRARY

The District Court also certified the class in conflict with another important limitation on class actions, the Supreme Court's decision in *Comcast*. In that case, the Court held that prior to class certification, in order to establish the predominance element in Rule 23, a plaintiff must show that damages can be proven on a classwide basis in a manner consistent with the plaintiffs' theory of liability. This requirement appropriately protects defendants from becoming insurers of losses caused by inactionable events, such as unexpected announcements of government enforcement activity, which often coincide with

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once, the risk of an error will often become unacceptable. Faced with even a small chance of a devastating loss, defendants will be pressured into settling questionable claims."); *Coopers & Lybrand* v. *Livesay*, 437 U.S. 463, 476 (1978) ("Certification of a large class may so increase the defendant's potential damages liability and litigation costs that he may find it economically prudent to settle and to abandon a meritorious defense."); *Newton* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 259 F.3d 154, 165 (3d Cir. 2001).

[11] *See* Geoffrey Miller, *The Problem of Reliance in Securities Fraud Class Actions*, 57 Ariz. L. Rev. 61, 68-69 (2015) (noting that *Halliburton II* reflects "concerns about the too-ready certification of securities class actions" and that the "mood of the majority opinion was one of caution, especially in marginal cases involving weak claims").

alleged corrective disclosures.[12] Here, *Comcast* requires Plaintiffs to come forward with a method for measuring class damages resulting solely from the alleged falsity of Goldman Sachs' general statements about conflicts of interest and business principles, as distinct from the disclosure of government enforcement activity.

Plaintiffs failed to come forward with any such method. Indeed, Plaintiffs do not even claim to have such a method. The damages model they presented to the District Court purports only to measure the price decline attributable to the *entire* mixture of news in the alleged corrective disclosures, including news of government enforcement activity. This is indistinguishable from the situation in *Comcast*, where plaintiffs sought to recover the full price increases due to reductions in competition, rather than disaggregating the price increases caused by violations of the antitrust laws.

Plaintiffs' model cannot measure what is actually at issue: the supposed effect of the alleged misstatements concerning Goldman's efforts to avoid conflicts of interest, as distinguished from the effect of the market learning that Goldman had received an SEC Wells notice (which Goldman had no duty to

[12] *See Ludlow* v. *BP, p.l.c.*, 800 F.3d 674, 690 (5th Cir. 2015) (quoting *Dura Pharm., Inc.* v. *Broudo*, 544 U.S. 336, 345 (2005)) (explaining that the securities laws protect investors only "against those economic losses that misrepresentations actually cause" and do not provide "broad insurance against market losses").

disclose).[13] By certifying a class based on a methodology that cannot disaggregate the price impact, if any, of the alleged misstatements about Goldman's efforts to avoid conflicts from the news of government enforcement activity, the District Court "travel[led] to a place forbidden by *Comcast*." *Ludlow* v. *BP, p.l.c.*, 800 F.3d 674, 688 (5th Cir. 2015). If followed, this ruling would allow plaintiffs to require companies to compensate them for losses due to events that did not violate the securities laws simply because those events happened to coincide with alleged securities law violations.

A. *Comcast* Requires a Non-Arbitrary, Classwide Method of Determining Damages Caused by Actionable Conduct

Comcast was a case in which the plaintiffs alleged four different antitrust injuries. The District Court in that case found that three of the alleged injuries could not be determined on a classwide basis, but certified a class regarding the fourth. Comcast argued that the class should not be certified because the plaintiffs' damages model failed to separate damages caused by the sole remaining theory of injury from losses caused by the other three injuries for which class certification had been denied. The Supreme Court agreed, holding that, in order to satisfy the predominance requirement in Rule 23(b)(3) with respect to a

[13] *See Richman* v. *Goldman Sachs Grp., Inc.*, 868 F. Supp. 2d 261, 272-75 (S.D.N.Y. 2012) (JA365-368) (holding that Goldman had no duty to disclose the SEC Wells Notices regarding its alleged conflicts of interest).

liability and damages class, a plaintiff must present a classwide damages theory that separates recoverable damages from other losses. 133 S. Ct. at 1433.[14]

As the Court noted in *Comcast*, "a model purporting to serve as evidence of damages in this class action must measure only those damages attributable" to the plaintiffs' liability theory. 133 S. Ct. at 1433. "If the model does not even attempt to do that, it cannot possibly establish that damages are susceptible of measurement across the entire class for purposes of Rule 23(b)(3)." *Id*. And, the Court added, for purposes of Rule 23, courts must "conduct a rigorous analysis to determine whether that is so." *Id.* (citations omitted).[15]

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[14] In *Roach* v. *T.L. Cannon Mgmt. Corp.*, 778 F.3d 401, 409 (2d Cir. 2015), this Court rejected a *per se* rule that "individualized damages determinations alone" always preclude class certification, while acknowledging that "damages questions should be considered at the certification stage when weighing predominance issues." In *Roach* it was clear that each class member's damages would be calculated based on the number of times that class member was the subject of the alleged classwide wage-and-hour violations, thus tying directly to the classwide theory of injury. By contrast, in *Comcast* and this case, the problem is not merely that a diversity of individual class member characteristics requires some individualized proof and separate damages calculations. The more fundamental flaw here is that Plaintiffs' damages model fails to connect to the theories of liability and injury, because Plaintiffs have no classwide method for disaggregating recoverable damages from losses not caused by Defendants' alleged misconduct. Thus, here, *Comcast*, rather than *Roach*, is the relevant controlling authority.

[15] *Comcast* applies in securities fraud cases. *See Ludlow*, 800 F.3d at 690; *Sicav* v. *James Jun Wang*, 2015 WL 268855, at *6 (S.D.N.Y. Jan. 21, 2015).

B. Plaintiffs' Damages Model Fails to Satisfy the Requirements of *Comcast*

Comcast requires that a plaintiff's alleged damages model be consistent with its liability case.[16] Accordingly, plaintiffs must disaggregate losses attributable to the actionable theory of liability from, for example, non-recoverable losses flowing from the announcement of enforcement activity.[17] The damages model that Plaintiffs offered in the District Court was arbitrary in at least three respects.

First, Plaintiffs did not propose a method to disaggregate the effect of the alleged "correction" of Defendants' statements concerning conflicts of interest

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[16] *See, e.g.*, *Sykes* v. *Mel S. Harris & Assocs. LLC*, 780 F.3d 70, 82 (2d Cir. 2015) (quoting *Comcast*, 133 S. Ct. at 1434) (affirming class certification but noting that "[f]or the purposes of class certification . . . plaintiffs cannot 'identify damages that are not the result of the wrong'"); *In re U.S. Foodservice Inc. Pricing Litig.*, 729 F.3d 108, 123 n.8 (2d Cir. 2013) ("In *Comcast*, the Supreme Court held that courts should examine the proposed damages methodology at the certification stage to ensure that it is consistent with the classwide theory of liability and capable of measurement on a classwide basis."); *Jacob* v. *Duane Reade, Inc.*, 293 F.R.D. 578, 587 (S.D.N.Y. 2013) ("*Comcast* . . . require[s] a baseline inquiry into damages at the certification phase—meaning that the putative class's theory of liability must track its theory of damages."), *aff'd*, 602 F. App'x 3 (2d Cir. 2015).

[17] *See, e.g.*, *In re Processed Egg Prods. Antitrust Litig.*, 2016 WL 410279, at *8 (E.D. Pa. Feb. 3, 2016) (citing *Comcast*, 133 S. Ct. at 1433-34) (plaintiffs' damages model improperly "intermingles lawful and unlawful behavior"); *In re POM Wonderful LLC*, 2014 WL 1225184, at *5 (C.D. Cal. Mar. 25, 2014) (plaintiffs' damages expert improperly "assumed that 100% of th[e] price difference was attributable to Pom's alleged misrepresentations").

and business principles from the effect of news about government enforcement activity.

Second, Plaintiffs' damages model ignores that Plaintiffs do not, and cannot, contend that Goldman ever said there was no risk that Goldman would have conflicts of interest with respect to particular transactions, thus giving rise to regulatory issues. Indeed, at least some risk of regulatory problems was disclosed by Defendants and assumed by the class. *See Richman* v. *Goldman Sachs Grp., Inc.*, 868 F. Supp. 2d 261, 272-73 & n.3 (S.D.N.Y. 2012) (JA365-366) (noting that Goldman disclosed the existence of government investigations into its CDO business). Plaintiffs' allegation is, thus, not that the risk was unknown, but rather that Goldman's policies aggravated the risk beyond the level priced into the Goldman stock price. The damages model, however, does not calculate the market reaction to disclosure of an increased risk of an adverse event, but is based on the entire price decline that accompanied the actual occurrence of that event. *See In re BP p.l.c. Sec. Litig.*, 2013 WL 6388408, at *16 & n.15 (S.D. Tex. Dec. 6, 2013) (stock-price drop that would have accompanied disclosure of increased risk of an oil spill is not the same as the stock-price drop that accompanied the actual oil spill).[18]

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[18] *See also* Ann M. Lipton, Halliburton *and the Dog That Didn't Bark*, 10 Duke J. Const. L. & Pub. Pol'y 1, 15-16 (2015).

Third, Plaintiffs made no attempt to put forward a model that predicts the price at which Goldman's stock price would have traded absent the alleged misstatements. The difference between the actual stock prices on the alleged disclosure dates and what the prices would have been in that but-for world is the correct measure of damages.

Since class members are not entitled to Plaintiffs' overstated measure of damages, *Comcast* precludes the certification of the proposed class. *See In re BP p.l.c. Sec. Litig.*, 2014 WL 2112823, at *10-12 (S.D. Tex. May 20, 2014), *aff'd*, *Ludlow*, 800 F.3d at 690-92. Any other result would, as noted above, unfairly turn companies into frequent insurers of losses due to inactionable adverse events, since such events often coincide with alleged securities law violations.

C. The District Court Improperly Accepted Plaintiffs' Promise to Fix Their Damages Model as Sufficient for Class Certification

The District Court erroneously accepted Plaintiffs' expert's unsupported assurance that he "will be able" to disaggregate the stock-price declines supposedly caused by Defendants' statements regarding conflicts of interest from non-recoverable losses. (SPA6225.) Plaintiffs' expert certainly could not do so using his existing event study methodology because an event study alone cannot disentangle the potential causes of the price declines, nor is any established workaround available on these facts.[19] Indeed, Plaintiffs' expert admitted that he plans to "calculate the economic loss per share" based on the full amount of the drop in Goldman's stock price on the dates that SEC and DOJ enforcement action and investigations were announced, adjusted for market-wide and industry-wide effects (JA482), thus failing to address the flaws in the model.

In any case, the mere "conclusory assertion that damages will be calculated on a classwide basis" does not suffice. *BP*, 2014 WL 2112823, at *12. Plaintiffs cannot satisfy their burden of proving the elements of Rule 23 "by asking

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[19] One way to disaggregate confounding events is to shorten the event window. Allen Ferrell & Atanu Saha, *The Loss Causation Requirement for Rule 10b-5 Causes of Action: The Implications of* Dura Pharmaceuticals, Inc. *v.* Broudo, 63 Bus. Law. 163, 168-70 (2007). That is not available here where the *same* event causes the alleged corrective disclosure and the confounding disclosure. Another method is to separately measure the anticipated effect of the confounding event and to subtract that effect from the abnormal return. David I. Tabak & Frederick C. Dunbar, *Materiality and Magnitude: Event Studies in the Courtroom*, *in Litigation Services Handbook* 19.2 (Roman L. Weil et al. eds., 3d ed. 2001). Here, Dr. Choi's report showed that the anticipated effect of the confounding events are consistent with the abnormal return. (SPA8-9, JA5137, 5153-5154.) Another method is to use "content analysis." Frederick C. Dunbar & Arun Sen, *Counterfactual Keys to Causation and Damages in Shareholder Class-Action Lawsuits*, 2009 Wisc. L. Rev. 199, 242 & n.80 (2009). Here, Mr. Porten and Dr. Gompers used that method to show that the confounding events were responsible for the abnormal return. (JA4986-5014, 5192-5213, 5760-5770.) Plaintiffs' expert never said that he could use these methods, *or any* method, to disaggregate the confounding regulatory events from the "corrective" aspects of those events.

the Court simply to trust them." *Id.*[20] Plaintiffs have the burden to put forward a model that disaggregates actionable damages; Defendants do not have the burden to show that disaggregation is impossible.[21]

The District Court was wrong to excuse this flaw in Plaintiffs' damages model on the ground that it may "affect all class members in the same manner." (SPA14.) Under *Comcast*, it is not enough that an arbitrary damages model "can be applied classwide." 133 S. Ct. 1433. That, as the Supreme Court said, "would reduce Rule 23(b)(3)'s predominance requirement to a nullity." *Id.* The Supreme Court has emphasized the predominance requirement precisely because it does not "want a class action suit to drag on for years with the parties and the district judge trying to figure out whether it should have been certified." *Butler* v. *Sears, Roebuck & Co.*, 727 F.3d 796, 800 (7th Cir. 2013). The District

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20 *See also In re Blood Reagents Antitrust Litig.*, 783 F.3d 183, 187 (3d Cir. 2015) ("Actual, not presumed, conformance with the Rule 23 requirements remains necessary, and a party's assurance to the court that it intends or plans to meet the requirements is insufficient.") (citations omitted); *In re Kosmos Energy Ltd. Sec. Litig.*, 299 F.R.D. 133, 152 (N.D. Tex. 2014).

21 *See In re Rail Freight Fuel Surcharge Antitrust Litig.*, 725 F.3d 244, 254 (D.C. Cir. 2013) ("[P]laintiffs are right that the defendants' critique does not disprove the damages model's claim of classwide overcharges as a matter of logical necessity; absence of evidence is not evidence of absence. But they misapprehend their burden. It is not enough to submit a questionable model whose unsubstantiated claims cannot be refuted through *a priori* analysis."); *Processed Egg Products*, 2016 WL 410279, at *4 ("At the class certification stage, it is the plaintiff's burden to show that all the requisite elements of Rule 23 have been met.").

Court's ruling, if followed, would gut this key limitation built into Rule 23, unfairly exposing companies to the nearly irresistible settlement pressures imposed by class certification.

CONCLUSION

For all of the foregoing reasons, this Court should vacate the District Court's class certification order.

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CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because it contains 6,830 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

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