No. 17-1209

In the

Supreme Court of the United States

BARCLAYS PLC, *et al.*,

Petitioners,

v.

JOSEPH WAGGONER, *et al.*,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF *AMICI CURIAE* OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AND THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF PETITIONERS

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INTEREST OF *AMICI CURIAE*[1]

The Chamber of Commerce of the United States of America (the "Chamber") is the world's largest federation of businesses and associations. The Chamber represents 300,000 direct members and indirectly represents an underlying membership of more than three million U.S. businesses and professional organizations of every size and in every economic sector and geographic region of the country. An important function of the Chamber is to represent the interests of its members in matters before the courts, Congress, and the Executive Branch. To that end, the Chamber regularly files *amicus curiae* briefs in cases that raise issues of concern to the Nation's business community, including in securities cases.

The Securities Industry and Financial Markets Association ("SIFMA") is comprised of hundreds of member securities firms, banks, and asset managers. 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.

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1. Pursuant to this Court's Rule 37.6, counsel for *amici curiae* certifies that this brief was not authored in whole or in part by counsel for any party and that no person or entity other than *amici curiae*, their members, or their counsel has made a monetary contribution intended to fund the preparation or submission of this brief. All parties have received timely notice of *amici curiae*'s intent to file and consented to the filing of this brief.

Amici curiae have a strong interest in this case, which involves important issues concerning standards for class certification in private securities actions. Many of *amici*'s members are companies subject to U.S. securities laws who are adversely affected by the Second Circuit's decision (i) relieving plaintiffs of their burden to provide direct evidence of market efficiency before receiving the *Basic* presumption of reliance, and (ii) heightening the burden of company-defendants to then rebut the presumption. In addition, *amici* have long been concerned about the costs that securities class-action lawsuits impose on the American economy.

INTRODUCTION AND SUMMARY OF ARGUMENT

This Court has made clear that "Rule 23 does not set forth a mere pleading standard," and class certification is proper only if "the trial court is satisfied, after a rigorous analysis, that the prerequisites of Rule 23(a) have been satisfied." *Wal-Mart Stores, Inc. v. Dukes*, 564 U.S. 338, 350-51 (2011) (citation omitted). The Second Circuit's decision below failed to follow these instructions, and, in doing so, created a split of authority among the circuit courts and exacerbated confusion in the lower courts about the proof necessary to invoke the fraud-on-the-market presumption of reliance in securities class actions. This Court should grant the petition for certiorari for three reasons.

First, the decision below has created a circuit split regarding the burden that defendants bear in rebutting the presumption of reliance under *Basic Inc. v. Levinson*, 485 U.S. 224 (1988). The Second Circuit mistakenly placed on defendants not only a burden of production

to come forward with evidence rebutting the *Basic* presumption, but also the burden of persuasion to defeat the presumption by a preponderance of the evidence. In doing so, the Second Circuit improperly relieved plaintiffs of their burden of persuasion under this Court's decision in *Halliburton Co. v. Erica P. John Fund, Inc.*, 134 S. Ct. 2398 (2014) ("*Halliburton II*"), once defendants had produced evidence to rebut the presumption. Because the *Basic* presumption relieves plaintiffs of the burden they otherwise carry to show reliance on allegedly misleading information, the Second Circuit announced the wrong standard by placing on defendants the burden of persuasion, instead of a burden of production. This decision created a split with the Eighth Circuit and misapplied Federal Rule of Evidence 301.

Second, the decision below exacerbated confusion among the courts about the proof necessary to invoke the *Basic* presumption of reliance. The Second Circuit held that "indirect evidence" of market efficiency is sufficient for plaintiffs to establish the *Basic* presumption, and thus found it unnecessary to consider "direct evidence" of a cause-and-effect relationship between unexpected news and the market price of the security, even though such a relationship is the essence of the "efficient market" required under *Basic*. By allowing plaintiffs to rely solely on "indirect evidence" of market efficiency, the decision below undermined the foundation of the fraud-on-the-market theory underlying the *Basic* presumption.

Third, the Second Circuit's decision threatens to embolden securities plaintiffs to pursue marginal claims on behalf of questionable classes. If left uncorrected, the decision below would effectively eliminate the

predominance element of Rule 23 in securities class actions and make class certification a near certainty in such cases involving a large, listed issuer. The business community already faces enormous challenges from dubious class-action litigation, in the securities context and elsewhere. The decision below will embolden plaintiffs to bring even more questionable claims that are disconnected from real culpability and allow them to extort settlements using the threat of massive class-wide damages. *Amici curiae* therefore respectfully urge this Court to grant the petition for certiorari.

ARGUMENT

I. This Court Should Clarify the Burden for Rebutting the *Basic* Presumption of Reliance.

A. Plaintiffs Bear the Burden of Proving Every Element of the Rule 23 Analysis, Including Predominance.

As this Court has cautioned, the class action remains "an exception to the usual rule that litigation is conducted by and on behalf of the individual named parties only." *Comcast Corp. v. Behrend*, 569 U.S. 27, 33 (2013) (citation omitted). Certification of a class is appropriate only when "questions of law or fact common to class members predominate over any questions affecting only individual members" and when class litigation "is superior to other available methods for fairly and efficiently adjudicating the controversy." Fed. R. Civ. P. 23(b)(3).

Importantly, "Rule 23 does not set forth a mere pleading standard," and a party seeking class certification

"must affirmatively demonstrate [its] compliance with the Rule—that is, [it] must be prepared to prove that there are *in fact* sufficiently numerous parties, common questions of law or fact, etc." *Dukes*, 564 U.S. at 350 (emphasis in original). Plaintiffs carry the burden of proof with respect to every Rule 23 requirement, and courts must conduct the "rigorous analysis" that Rule 23 requires. *Comcast*, 569 U.S. at 33.

This burden of proof is no different for the "predominance" requirement under Rule 23(b)(3). The predominance inquiry is not satisfied unless "a proposed class is 'sufficiently cohesive to warrant adjudication by representation.'" *Amgen Inc. v. Conn. Ret. Plans & Trust Funds*, 568 U.S. 455, 469 (2013) (quoting *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 623 (1997)). Class-wide issues predominate only when "the elements of the claim are susceptible to classwide proof." *Id.* at 491. The requirement's purpose is to ensure that the class will be certified only when it "would achieve economies of time, effort, and expense, and promote … uniformity of decision as to persons similarly situated, without sacrificing procedural fairness or bringing about other undesirable results." *Amchem*, 521 U.S. at 615 (citation omitted).

Thus, plaintiffs must prove at the class certification stage that "questions of law or fact common to class members predominate" in their underlying cause of action—in this case, under Section 10(b) of the Exchange Act and Rule 10b-5. *See Erica P. John Fund, Inc. v. Halliburton Co.*, 563 U.S. 804, 809 (2011) ("*Halliburton I*"). Section 10(b) and Rule 10b-5 "prohibit making any material misstatement or omission in connection with the purchase or sale of any security." *Halliburton II*,

134 S. Ct. at 2407. To recover damages for violations of these provisions, plaintiffs must prove "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation." *Id.* (citation omitted).

The reliance element is a critical component of this cause of action because it "ensures that there is a proper connection between a defendant's misrepresentation and a plaintiff's injury." *Amgen*, 568 U.S. at 461 (citation omitted). "The traditional (and most direct) way a plaintiff can demonstrate reliance is by showing that he was aware of a company's statement and engaged in a relevant transaction—*e.g.*, purchasing common stock—based on that specific misrepresentation." *Halliburton I*, 563 U.S. at 810. Thus, the Court noted in *Halliburton II* that the "traditional … way" of proving reliance—*i.e.*, "[r]equiring proof of individualized reliance" from every securities fraud plaintiff "effectively would ... prevent [plaintiffs] from proceeding with a class action" in Rule 10b-5 suits. 134 S. Ct. at 2407-08 (citation omitted).

In *Basic*, this Court held that "securities fraud plaintiffs can in certain circumstances satisfy the reliance element of a Rule 10b-5 action by invoking a rebuttable presumption of reliance, rather than proving direct reliance on a misrepresentation." *Halliburton II*, 134 S. Ct. at 2408 (citing *Basic*, 485 U.S. at 246-47). The Court based that presumption on the "fraud-on-the-market" theory, which holds that "the market price of shares traded on well-developed markets reflects all publicly available information, and, hence, any material misrepresentations." *Basic*, 485 U.S. at 246.

The *Basic* presumption is premised on "price impact"—*i.e.*, "whether the alleged misrepresentations affected the market price in the first place." *Halliburton I*, 563 U.S. at 814. "In the absence of price impact, *Basic*'s fraud-on-the-market theory and presumption of reliance collapse." *Halliburton II*, 134 S. Ct. at 2414. "The fundamental premise underlying the presumption is that an investor presumptively relies on a misrepresentation so long as it was reflected in the market price at the time of his transaction." *Id*. (quotation marks and citation omitted). "If it was not, then there is no grounding for any contention that the investor indirectly relied on that misrepresentation through his reliance on the integrity of the market price." *Id*. (quotation marks and citation omitted).

For the *Basic* presumption to apply, plaintiffs must show: "(1) that the alleged misrepresentations were publicly known, (2) that they were material, (3) that the stock traded in an efficient market, and (4) that the plaintiff traded the stock between the time the misrepresentations were made and when the truth was revealed." *Halliburton II*, 134 S. Ct. at 2408. To prove market efficiency, "the most important" factor to consider is direct evidence of cause and effect—*i.e.*, a causal relationship between unexpected news and the market price. *Teamsters Local 445 Freight Div. Pension Fund v. Bombardier Inc.*, 546 F.3d 196, 207 (2d Cir. 2008) (citation omitted). "[I]n an efficient market, all publicly available information is rapidly incorporated into, and thus transmitted to investors through, the market price." *Amgen*, 568 U.S. at 466. As a result, "[e]vidence that unexpected corporate events or financial releases cause an immediate response in the price of a

security" is "the essence of an efficient market and the foundation for the fraud on the market theory." *Teamsters Local 445 Freight Div. Pension Fund*, 546 F.3d at 207 (citation omitted). "Without the demonstration of such a causal relationship, it is difficult to presume that the market will integrate the release of material information about a security into its price." *Id.*

B. The Decision Below Erroneously Places the Burden of Class Certification in Securities Fraud Cases on Defendants.

Against this backdrop, the Second Circuit erred by relieving Respondents of their burden of persuasion once Petitioners rebutted the *Basic* presumption of reliance. In *Halliburton II*, this Court made clear that market efficiency—even if shown—does not establish an irrebuttable presumption of price impact, and that, at the class certification stage, the defendant must be afforded an opportunity to rebut the plaintiffs' "indirect way of showing price impact" (*i.e.*, via the fraud-on-the-market presumption) by providing "direct, more salient evidence showing that the alleged misrepresentation did not actually affect the stock's market price." 134 S. Ct. at 2415-16. The burden then shifts back to plaintiffs to prove price impact, which is "an essential precondition for any Rule 10b-5 class action." *Id.* at 2416.

In this case, the Second Circuit erroneously eliminated the burden shifting by holding that defendants bear the ultimate burden of proving the absence of a price impact. App. 44a. Thus, even though Petitioners produced evidence that the alleged misstatements did not cause any statistically significant price increase, the court below held that this was insufficient because Petitioners

continued to bear the burden of persuasion. *Id*. This error is particularly important in light of the Second Circuit's critical role in capital markets and securities law.

The decision below also conflicts with *IBEW Local 98 Pension Fund v. Best Buy Co.*, 818 F.3d 775 (8th Cir. 2016). There, the Eighth Circuit applied Federal Rule of Evidence ("FRE") 301 to the *Basic* presumption of reliance and required the defendant only to "come forward with evidence showing a lack of price impact." *Id*. at 782. This is consistent with *Halliburton II*, which, as described above, makes clear that the burden of proving reliance, like the burden for other elements of securities fraud, normally falls on the plaintiff. *See* 134 S. Ct. at 2407.

Under FRE 301—which informs the effects of the fraud-on-the-market presumption, *see Basic*, 485 U.S. at 245—when a defendant produces evidence that would permit a reasonable jury to infer that the presumption is incorrect, the presumption is rebutted and ceases to operate. The burden then shifts back to the plaintiff to prove the fact without benefit of the presumption. *Cf. St. Mary's Honor Ctr. v. Hicks*, 509 U.S. 502, 507 (1993) ("[A]lthough the *McDonnell Douglas* presumption shifts the burden of *production* to the defendant, '[t]he ultimate burden of persuading the trier of fact that the defendant intentionally discriminated against the plaintiff remains at all times with the plaintiff.'") (emphasis in original); *see also ITC Ltd. v. Punchgini, Inc.*, 482 F.3d 135, 148-49 (2d Cir. 2007) ("[T]he party against whom [a presumption] is directed" has "the burden of going forward with evidence to rebut or meet the presumption," but the burden of persuasion "remains on the party who had it originally."). Thus, the Eighth Circuit held that defendants bear only

a burden of production, while plaintiffs bear the burden of persuasion. *See Best Buy*, 818 F.3d at 782.

By ruling that Petitioners' evidence was insufficient to rebut the *Basic* presumption and to shift the burden to Respondents, the court below adopted an overly lax test that would permit plaintiffs to satisfy the predominance requirement simply by pleading market efficiency and without sustaining their burden to prove price impact. This test effectively creates an irrebuttable presumption contrary to *Halliburton II* and FRE 301.

The Second Circuit reasoned that FRE 301 does not apply because it includes an exception for when "a federal statute ... provides otherwise," thereby shifting the burden of persuasion to defendants. App. 48a. But its questionable assertion that there is a "sufficient link" to the federal securities laws to trigger the exception ignores that a Section 10(b) private action is a private right of action and not part of the statute itself. The Second Circuit's conclusion creates a conflict with the Eighth Circuit's decision in *Best Buy* warranting this Court's review.

II. This Court Should Clarify That Plaintiffs Must Present Direct Evidence of Market Efficiency at the Class Certification Stage.

The court below also erred in holding that plaintiffs can benefit from the *Basic* presumption of reliance without direct evidence that the relevant securities were traded in an efficient market. The court concluded that "indirect evidence" of market efficiency is sufficient to satisfy the *Basic* presumption on class certification. App. 36a.

Specifically, the Second Circuit held that direct evidence of market efficiency is necessary only in cases involving large companies where "the other four *Cammer* factors (and/or the *Krogman* factors) are less compelling in showing an efficient market." *Id.*

But exclusive reliance on indirect evidence is inconsistent with this Court's teaching in *Halliburton II* that the *Basic* presumption of reliance is meant to substitute for proof of a plaintiff's "direct reliance" on a misrepresentation. *Halliburton II*, 134 S. Ct. at 2407-08. Direct evidence of causality is necessary to determine whether a security is traded in an efficient market. The decision below therefore undermines the requirement that a plaintiff prove that a market promptly incorporated new, material information, which is the "fundamental premise" of the fraud-on-the-market presumption. *Id.* at 2414.

To establish the *Basic* presumption, a plaintiff bears the burden of "prov[ing]" that the price of the security generally incorporates "all public, material information." *Id.* at 2407, 2413. In *Halliburton II*, this Court noted that securities plaintiffs provide direct evidence of market efficiency through "event studies." *Id.* at 2415; *see also, e.g.*, *Best Buy*, 818 F.3d at 779-82; *Schleicher v. Wendt*, 618 F.3d 679, 684 (7th Cir. 2010). "Without the demonstration of such a causal relationship, it is difficult to presume that the market will integrate the release of material information about a security into its price." *Teamsters Local 445 Freight Div. Pension Fund*, 546 F.3d at 207; *see also In re Xcelera.com Secs. Litig.*, 430 F.3d 503, 512 (1st Cir. 2005) (Without "a historical cause-and-effect relationship between company disclosures and an immediate response in stock price … there is little assurance that information

is being absorbed into the market and reflected in its price."). An empirical study is thus essential for evaluating market efficiency. *See* Pet'r Br. 20.

The decision below, however, held that such direct evidence is unnecessary and that plaintiffs can benefit from the fraud-on-the-market presumption based solely on "indirect factors." App. 36a. These "indirect factors," which stem from two district court decisions, *see Cammer v. Bloom*, 711 F. Supp. 1264 (D.N.J. 1989), and *Krogman v. Sterritt*, 202 F.R.D. 467 (N.D. Tex. 2001), have created an illusory substitute for evidence of market efficiency and have caused confusion among the courts. *See* Pet'r Br. 20-21. Those indirect factors are essentially proxies for the size of the company and the liquidity of the market in which the company's securities trade, but they do not measure the efficiency of the market.

The Second Circuit's decision threatens to eviscerate the reliance element in securities class actions. If "indirect evidence" were sufficient to find market efficiency, which then established reliance, then most, if not all, large companies would be potentially liable for any statement regardless whether investors actually relied on it. This would have the effect of turning the securities laws into an insurance policy. *See Dura Pharms., Inc. v. Broudo*, 544 U.S. 336, 347-48 (2005) ("Such a rule would tend to transform a private securities action into a partial downside insurance policy."). Indeed, almost all large companies satisfy these "indirect" factors, which include commonplace features such as heavy trading volume, analyst coverage, and market capitalization. Conversely, investors in smaller issuers or bond offerings would rarely benefit from the presumption.

This Court should grant certiorari to clarify the standard for proving market efficiency under *Basic* and *Halliburton II*, and to reject the Second Circuit's holding that no direct evidence of market efficiency is necessary to establish the *Basic* presumption of reliance.

III. The Decision Below Will Embolden Securities Plaintiffs To Pursue Marginal Claims on Behalf of Questionable Classes.

Left uncorrected, the Second Circuit's errors will not only cause upheaval to class action law generally, but they will cause particular damage in securities class actions, making class certification a near certainty in the vast majority of those actions, while depriving defendants of their rights to a defense. This outcome will embolden plaintiffs to bring insubstantial securities fraud claims that bear little relation to any real culpability and serve only to extract settlements by wielding the threat of overbroad class-wide damages.

This Court has repeatedly warned against the threat of abuse and unfair settlement pressures that often attend the class treatment of securities fraud claims. *See, e.g.*, *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 163 (2008) (noting that "extensive discovery and the potential for uncertainty and disruption in a [securities fraud] lawsuit allow plaintiffs with weak claims to extort settlements from innocent companies"); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 739 (1975) (noting that securities class action litigation poses "a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general").

Given the costs of defending against such litigation and the potential for massive liability, settlement is a virtual certainty in cases that survive a motion to dismiss, regardless of merit, according to research by the Stanford Law School Securities Class Action Clearinghouse. *See* Stanford Clearinghouse, *Securities Class Action Filings: 2016 Year in Review* 13 (2017) (less than 1 percent of securities class action filings from 1997 to 2016 have reached a trial verdict).

The targeting of defendants for securities lawsuits likewise often has little to do with the merits. Although the implied private right of action under Section 10(b) and Rule 10b-5 is intended to provide a remedy for investors who suffer genuine injury from securities fraud, securities class actions are routinely filed in the wake of almost any negative announcement by a company that corresponds to a stock price decline. For example, of the companies in the S&P 500 at the beginning of 2016, one in about 12 companies (8.4 percent) was a defendant in a class action filed during the year. Stanford Clearinghouse, *Securities Class Action Filings: 2016 Year in Review*, *supra*, 23. Statistics from the Stanford Clearinghouse also show that securities fraud suits often target particular industry sectors, in many cases ensnaring a large portion of the publicly traded companies in a given industry. *See id.* (noting that the percentage of filings in the health care sector was over 21 percent). Because securities fraud cases can take years to resolve, the filing of a significant number of cases against an industry in one year can mire that industry in litigation for years to come.

Companies already face enormous pressure to settle securities class actions. Securities fraud class actions led

to nearly $6 billion in settlements in 2016, with an average settlement of over $70 million per case. *See* Stanford Clearinghouse, *Securities Class Action Settlements: 2016 Review and Analysis* 1 (2017). Defense costs in these cases have been estimated to range from 25 to 35 percent of the settlement value. *See* John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation*, 106 Colum. L. Rev. 1534, 1546 (2006). The Second Circuit's approach, if permitted to stand, would increase these burdens.

Such burdens are not limited to companies against which suits have been brought. They are spread to all U.S. public companies, which must pay more for insurance, pay more to access capital, and be placed in a worse competitive position than their overseas counterparts. Indeed, these cases threaten the health of the U.S. economy—imposing huge costs on American businesses, investors, and employees while hurting the global competiveness of U.S. securities markets.

In addition to these costs, the Second Circuit's decision could have even greater economic consequences by spurring foreign issuers to turn to securities markets in other jurisdictions. *See* Stephen M. Bainbridge, *Fee-Shifting: Delaware's Self-Inflicted Wound*, 40 Del. J. Corp. L. 851, 865-66 (2016) (discussing studies confirming that "the U.S. capital markets became less competitive vis-à-vis other markets" and "blam[ing] shareholder litigation, in part, for that decline"). The decision below could discourage foreign global issuances involving the United States due to concerns about the risk of facing large U.S. class action lawsuits, even if most of the transactions occurred outside the United States. *See, e.g.*, *id.* at

866 ("The perception that exposure to the U.S. capital markets significantly increases an issuer's litigation risk has a measurable impact on the attractiveness of those markets.").

The costs of excessive securities class actions are not offset by corresponding benefits in the form of effective fraud deterrence. *See* William W. Bratton & Michael L. Wachter, *The Political Economy of Fraud on the Market*, 160 U. Pa. L. Rev. 69, 72-73 (2011). In fact, most often the main result of settlements is a wealth transfer from one group of innocent shareholders to another. *See* Donald C. Langevoort, *Capping Damages for Open-Market Securities Fraud*, 38 Ariz. L. Rev. 639, 648 n.43 (1996) ("[I]n the average settlement, 68.2% comes from the insurer and 31.4% from the issuer, with only 0.4% coming from individual defendants.") (citation omitted).

At bottom, this Court should be mindful of the legal and economic burdens that flow from the decision below. Many in the business community are already deeply vulnerable to massive liability from insubstantial securities class actions. The Court should not increase this exposure by allowing the casual approach to class certification taken by the Second Circuit to stand.

CONCLUSION

For the foregoing reasons, *amici curiae* respectfully request that the Court grant the petition for certiorari.

Respectfully submitted,

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