IN THE SUPREME COURT OF GEORGIA
S09Q1585

IN RE: WORLDCOM, INC. SECURITIES LITIGATION

WILLIAM K. HOLMES, HOLMES CAPITAL, LLC, BREW DOG, LLC, BIMINI STAR, LLC, and EBH INVESTMENTS CO., LLC,

Plaintiffs-Appellants,

-v-

JACK GRUBMAN and CITIGROUP GLOBAL MARKETS, INC. F/K/A/ SALOMON SMITH BARNEY & CO., INC.,

Defendants-Appellees.

Certified Questions from the United States
Court of Appeals for the Second Circuit

AMICUS CURIAE BRIEF OF THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION

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PRELIMINARY STATEMENT

William K. Holmes (and entities he controls) alleges, with perfect hindsight, that, instead of selling 2.1 million shares of Worldcom stock on June 25, 1999 at a price of $92 a share – which, he argues, defendants' positive research report dissuaded him from doing – he held on to them for more than a year and eventually sold them in October 2000 (in response to margin calls) at much lower prices. Although he does not even attempt to allege that any of the price decline between June 1999 and October 2000 was caused by the research report, he claims that the defendants should pay him nearly $200 million on his non-selling claims because, he argues, he would have sold all his shares earlier absent the report. The two issues at the core of the case before this Court, then, are (1) whether – in sharp contrast to well-settled federal law – Georgia should recognize so-called "holder" claims in securities cases (*i.e.*, claims by persons who concede that they did not purchase or sell securities as a result of an alleged misstatement, but rather assert that they decided not to sell securities as a result of the misstatement), and (2) whether the allegations in the complaint satisfy the requirement that the defendants' conduct have been the "proximate cause" of the losses for which Plaintiffs seek recovery.[1]

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[1] We express no view on the third question certified to this Court by the Second Circuit, *i.e.*, whether a fiduciary duty was owed to Plaintiffs under Georgia common law. This issue has been extensively and exhaustively briefed by the

The Securities Industry and Financial Markets Association ("SIFMA") submits this brief to focus on the public policy considerations identified by the courts in analogous cases, because policy concerns are paramount where, as here, legal precedents are not dispositive. As discussed below, when the allegation is that misstatements were made in connection with transactions in publicly-traded securities, identical policy considerations have often informed the interpretation of both common law and federal securities statutes. Given the global reach of the securities markets and the common interest, under both federal law and state common law, in protecting investors while also limiting windfall recoveries and abusive litigation, there are compelling reasons to harmonize Georgia law with federal standards governing the attribution of liability in securities fraud cases.

SIFMA submits that Plaintiffs' expansive proposed theories of liability, if permitted, would upset the appropriate balance between providing a remedy for aggrieved investors, on the one hand, and eliminating the risk of windfall recoveries and the burdens of frivolous suits, on the other. Consistent with the principles applied to similar claims arising under the federal securities laws, as enunciated by the United States Supreme Court in seminal cases, such as *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), and *Dura Pharmaceuticals v. Broudo*, 544 U.S. 336 (2005), as well as in other district court

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parties.

decisions discussed below, SIFMA urges this Court 1) not to recognize a common law cause of action, at least on the facts alleged in this case, based on allegations of fraudulent inducement to hold, rather than sell or buy, publicly-traded securities, and 2) to find that Plaintiffs have not adequately pleaded that Defendants' conduct was the proximate cause of Plaintiffs' losses – a *sine qua non* of both common law and securities fraud claims alike.

STATEMENT OF INTEREST

The Securities Industry and Financial Markets Association represents the aggregate interests of more than 600 securities firms, banks and asset managers locally and globally through offices in New York, Washington, D.C., and London. Its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong. SIFMA's mission is to champion policies and practices that benefit investors and issuers, expand and perfect global capital markets, and foster the development of new products and services. Fundamental to achieving this mission is earning, inspiring and upholding the public's trust in the industry and the markets. (More information about SIFMA is available at http://www.sifma.org.)

SIFMA has an interest in the current proceeding because this Court is called to rule upon issues implicating the balance between two equally important, yet largely conflicting values: the need to afford adequate remedies to aggrieved investors, and the need to minimize the risk of windfall recoveries and the *in terrorem* effect of frivolous litigation.

SIFMA represents securities firms that, in good and bad economic times, provide an indispensable service to public investors, allowing them to trade on transparent and efficient markets. The ability of these securities firms to fulfill their valuable societal role depends in no small part on the certainty of their legal duties and the predictability of their exposure to liability. That certainty and predictability are enhanced when state and federal laws regulating the purchase and sale of publicly-traded securities are uniform. Allowing, contrary to federal securities laws and public policy, opportunistic investors to assert claims based on their indefinite holding of securities – as opposed to the defining points of a purchase or sale – would unnecessarily expand the duties and risk exposures of financial service providers, resulting in an influx of "holder"-claim litigation and, ultimately, in increased costs to public investors, whom state and federal legislatures seek to protect.

ARGUMENT

I. THE POLICY CONSIDERATIONS THAT HAVE LED COURTS TO CONSTRICT FRAUD CLAIMS UNDER THE FEDERAL SECURITIES LAWS SHOULD APPLY WITH THE SAME FORCE TO COMMON LAW CLAIMS ARISING OUT OF SIMILAR TRANSACTIONS IN PUBLICLY-TRADED SECURITIES

The Second Circuit, in certifying the issues for resolution by this Court, concluded that there is "no definitive guidance in Georgia law." In the absence of controlling Georgia precedent and guiding policy interests, the public policy considerations underlying analogous federal securities fraud cases obtain increased significance for purposes of this Court's analysis.[2]

A review of the case law in two related areas reveals that courts applying either state common law or the federal securities laws to claims of fraudulent inducement to buy, sell, or hold securities as a result of an allegedly misleading statement have sought to carefully balance the interest in providing meaningful remedies to aggrieved investors while simultaneously reducing the risk of windfall recoveries and abusive litigation. Neither interest is given exclusive weight. Rather, it is the balance of those competing interests that determines how the courts have addressed both the purchaser/seller and proximate cause requirements.

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2 The parties to this case have briefed at length the implications of existing Georgia precedent on the issues we address here. We see little value in burdening the Court with duplicative analyses.

A. The public policy considerations underlying the purchaser/seller requirement in federal securities cases apply with equal force to common law holder actions involving publicly-traded securities.

For more than thirty years, the law in federal securities fraud cases has been that plaintiffs alleging misrepresentations related to the value of securities must plead and prove that they purchased or sold securities in reliance on those statements; mere holders of securities who failed to purchase or sell lack standing under the federal statutory regime. This rule is not so much grounded in the language of Section 10(b) and Rule 10b-5 as it the product of the United States Supreme Court's careful weighing of compelling policy considerations that would apply to all claims sounding in securities fraud.[3]

In *Blue Chip Stamps*, a seminal case decided more than 30 years ago, the United States Supreme Court considered the exact question now before this Court: whether persons who claim to have been fraudulently induced by a misstatement to not purchase or not sell stock could seek relief. *See* 421 U.S. 723. In *Blue Chip Stamps*, those claims were brought under Section 10(b) of the Securities Exchange Act, the principal antifraud provision of the federal securities laws; in this case, the same claims are cloaked in the guise of common law fraud. Yet in affirming the longstanding purchaser-seller requirement long followed by the lower courts in

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[3] In *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, 547 U.S. 71 (2006), the Supreme Court acknowledged that the *Blue Chip Stamps* holding rested "principally on policy considerations." *Id.* at 80.

securities cases, the Supreme Court struck a wise balance among the competing interests affecting investors, defendant securities firms, the securities markets, society, and the courts – a balance this Court should employ here too in seeking to cut the Gordian knot of holder status under Georgia law.

To strike the balance, the Supreme Court carefully weighed all the competing considerations, which, the Court acknowledged, were not entirely on one side of the equation: a categorical exclusion of claims of fraudulent inducement to merely hold, *not* purchase or sell, securities would "prevent some deserving Plaintiffs from recovering damages which have, in fact, been caused by violations of Rule 10b-5."[4] Such a rule, the Court admitted, would foreclose claims by potential purchasers who could claim to have been discouraged from buying because of dismal predictions about the performance of a security, or potential sellers who could allege they decided not to sell because of unduly rosy representations.[5] Imposing a purchaser-seller restriction, the Court explained, would be undesirable and unwise "if it had no countervailing considerations"[6] which the Court thoroughly examined, concluding that it was those considerations that decisively tipped the scale in favor of restricting standing to purchasers and

4 *Blue Chip Stamps,* 421 U.S. at 738.

5 *Id.* at 737-38.

6 *Id.* at 739.

sellers, *not* holders, of securities.

The Supreme Court correctly recognized that, if standing was granted to investors who merely claimed to have been defrauded into holding on to their securities (essentially, doing nothing), an avalanche of easily manufactured, groundless, difficult to prove, and extremely disruptive claims would flood court dockets, while the spectrum of ever-increasing liability exposure would paralyze the securities services industry. After all, fraud claims by persons who merely abstained from taking any ascertainable action could be brought, in theory, by any investor, cannot be resolved without a trial, and are exceptionally difficult to defend because the sole proof of the supposed fraud is plaintiffs' own subjective digestion of information available in the market and accessible to innumerable potential fraud victims.

The pool of putative fraud claimants is already large, said the Court: billions of shares are traded each day on stock exchange markets, and every single one of those complex transactions could give rise to claims of fraudulent misrepresentations or omissions; every investor buying or selling securities could theoretically seek compensation for losses they might incur as a result of buying or selling securities. The Court expressed concern, however, at the prospect of expanding that already large group into the exponentially broader class of literally everyone, whether or not they purchased or sold, who could claim imaginary losses arising out of "non-transactions." The Court noted that even with the purchaser-seller restriction, securities litigation under the antifraud provisions of the federal securities laws poses a distinct risk of "large judgments, payable in the last analysis by innocent investors, for the benefit of speculators and their lawyers."[7] Without the purchaser-seller restriction, the Court noted, claims for failing to buy or sell a security "will turn largely on which oral version of a series of occurrences a jury will decide to credit" and, therefore, the case will be virtually impossible to dispose of before trial "no matter how improbable the allegations of the Plaintiff."[8] Plaintiff's entire testimony "could be dependent upon uncorroborated oral evidence of many of the crucial elements of his claim."[9] The jury would not even have the benefit of weighing the defendant's version against the plaintiff's version since the elements to which the plaintiff would testify "would be totally unknown and unknowable to the defendant."[10] Absent a purchaser-seller restriction "bystanders to the securities marketing process could await developments on the sidelines without risk, claiming that inaccuracies in disclosure caused nonselling in a falling market and that unduly pessimistic predictions by the issuer followed by a rising

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7 *Id.* at 739, quoting Judge Friendly's remark in *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 867 (2d Cir. 1968).

8 *Id.* at 741.

9 *Id.* at 746.

10 *Id.*

market caused them to allow retrospectively golden opportunities to pass."[11] Given the great ease with which Plaintiffs could manufacture claims about what they would have done, "the risk of strike suits is particularity high"[12] and the purchaser-seller requirement was necessary to strike the appropriate balance by permitting actions to be brought "only by those persons whose active participation in the marketing transaction promises enforcement of the statute without undue risk of abuse of the litigation process and without distorting the securities markets."[13]

Although *Blue Chip Stamps* directly applied only to requirements for standing to bring a private claim under the antifraud provisions of the federal securities laws, the Court also addressed common law precedent as well. Citing Justice Cardozo's concern in *Ultramares Corp. v. Touche*, 255 N.Y. 170, 174 N.E. 441 (1931), about the hazards of business conducted with the threat of "liability in an indeterminate amount for an indeterminate time to an indeterminate class," the Supreme Court did accept that in many cases the common law permitted forbearance claims,[14] but pointed out that the common law cases allowing such claims were "light years away from the world of transactions to which Rule 10b-5 is applicable." Unlike the common law cases permitting forbearance claims, the

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11 *Id.* at 747.

12 *Id.* at 742.

13 *Id.* (internal quotation marks and citation omitted).

14 *Id.* at 748.

securities cases often involved communications that were broadly disseminated, not tailored specifically to the plaintiff, and drafted by someone who had never even met or talked to the plaintiff – precisely, as we understand the allegations, the situation involving the Plaintiffs and the author of the research report that they allege was misleading. While the Supreme Court had no authority to define state common law, the clear implication of the Court's analysis was that the same policies it analyzed under the federal securities laws should apply with equal force to common law claims for securities violations.

To summarize, the purchaser-seller requirement for claims under the antifraud provisions of the federal securities laws was devised mainly on the basis of momentous policy considerations, *i.e.*, the importance of providing remedies to aggrieved investors, on the one hand, and the importance of avoiding windfall recoveries and abusive claims, on the other. Although the Supreme Court could not define the appropriate limitations on similar claims under common law, it intimated that its analysis could be applied by analogy to those cases too, if "light years" no longer separate cases in which forbearance claims are recognized at common law from fraud claims in connection with modern-day securities transactions. In the State of Georgia, this distance now stands eliminated. Hence, the public policy considerations extensively analyzed by the Supreme Court in

Blue Chip Stamps should be given equal weight in common law fraud actions involving securities transactions.

B. The public policy behind both proximate cause and loss causation dictates that the alleged misstatement, on which the fraud claim is based, be the reason for the drop in stock price Plaintiffs seek to recover.

Courts have long recognized the strong relationship between common law fraud actions and actions under Section 10(b) of the Securities Exchange Act.

In common law fraud actions, courts have long held that even a Plaintiff who relies on a false statement to purchase a security that subsequently declines in value cannot recover that subsequent decline in value unless it was caused by the misstatement. For example, Prosser & Keeton observe that under common law:

> if false statements are made in connection with the sale of corporate stock, losses due to a subsequent decline of the market, or insolvency of the corporation, brought about by business conditions or other factors in no way related to the representations, will not afford any basis for recovery.[15]

Similarly, the Restatement (Second) of Torts points out that one who misrepresents the financial condition of a company in order to sell stock will be liable to the purchaser who relies on the misrepresentation for the losses incurred when the facts regarding the company's finances are disclosed and, as a result, the

[15] W. Prosser & W. Keeton, PROSSER AND KEETON ON TORTS ¶ 110, at 767 (5th ed. 1984).

stock subsequently declines in value. But even a wrongdoer does not incur liability for a decline in the price resulting from factors other than the false statement. Thus,

> There is no liability when the value of the stock goes down after the sale, not in any way because of the misrepresented financial condition, but as a result of some subsequent event that has no connection with or relation to its financial condition. There is, for example, no liability when the shares go down because of the sudden death of the corporation's leading officers. Although the misrepresentation has in fact caused the loss, since it has induced the purchase without which the loss would not have occurred, it is not the legal cause of the loss for which the maker is responsible.[16]

The following hypothetical from the Restatement (Second) of Torts is instructive on the limits of liability arising from proximate cause requirements:

> A, seeking to sell to B the municipal bonds of C County, fraudulently tells B that the county has received full payment for the bond issue. B purchases the bonds in reliance upon this statement. Subsequently, the county is paid in full, but the bonds are held void by the supreme court of the state on the ground that the court had no jurisdiction to issue certain orders with respect to them. As a result B suffers pecuniary loss. A is not liable to B for the loss.[17]

The same concept – that "but for" causation is not enough to impose liability and that plaintiff must allege and prove that the false statements are responsible for

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16 RESTATEMENT (SECOND) OF TORTS § 548a cmt. B (1977).

17 *Id.* at § 548A cmt. B, illus. 1 (1977).

the decline in the price that it seeks to recover – has been imported from the common law into the federal securities laws. Most importantly, in *Dura Pharmaceuticals v. Broudo*, 544 U.S. 336 (2005), the United States Supreme Court, in addressing loss causation requirements under Section 10(b), observed that Section 10(b) actions strongly resembled common law actions for fraud and deceit. In rejecting a claim that a plaintiff could show loss causation merely by purchasing stock at a price inflated by defendant's alleged misrepresentation, the Court observed that the subsequent sale at a lower price "may reflect, not the earlier misrepresentation, but changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events, which taken separately or together account for some or all of that lower price."[18] The Supreme Court reversed the appellate court decision allowing the claim to proceed under Section 10(b) because, in language straight from the common law, it was "inconsistent with the law's requirement that a plaintiff prove that the defendant's misrepresentation (or other fraudulent conduct) proximately caused the plaintiff's economic loss."[19] Quoting its decision in *Blue Chip Stamps*,

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18 *Dura Pharmaceuticals,* 544 U.S. at 343.

19 *Id.* at 346.

it stated that allowing such a claim to proceed would "transform a private securities action into a partial downside insurance policy."[20]

Similarly, long before *Dura*, the Fifth Circuit, in *Huddleston v. Herman & MacLean*, 640 F.2d 534 (5th Cir. 1981), *aff'd in part, rev'd in part on other grounds*, 459 U.S. 375 (1983), explained that "but for" causation was not enough to recover for price declines under the federal securities law. Instead, as at common law, the plaintiff also had to show that the misrepresented fact was a proximate cause of the loss:

> Causation is related to but distinct from reliance. Reliance is a *causa sine qua non*, a type of "but for" requirement: had the investor known the truth he would not have acted. Causation requires one further step in the analysis: even if the investor would not otherwise have acted, was the misrepresented fact a proximate cause of the loss? The Plaintiff must prove not only that, had he known the truth, he would not have acted, but in addition that the untruth was in some reasonably direct, or proximate, way responsible for his loss. The causation requirement is satisfied in a Rule 10b-5 case only if the misrepresentation touches upon the reasons for the investment's decline in value. If the investment decision is induced by misstatements or omissions that are

[20] *Id.* at 348. *See also, e.g., Bastian III v. Petren Resources Corp.*, 892 F.2d 680 (7th Cir. 1990) (rejecting recovery where plaintiffs sufficiently alleged only the cause of their entering into the transaction, "but not the cause of the transaction's turning out to be a losing one." The court stated, "No social purpose would be served by encouraging everyone who suffers an investment loss because of an unanticipated change in market conditions to pick through offering memoranda with a fine-tooth comb in the hope of uncovering a misrepresentation. Defrauders are a bad lot and should be punished, but Rule 10b-5 does not make them insurers against national economic calamities.").

> material and that were relied on by the claimant, but are not the proximate reason for his pecuniary loss, recovery under the Rule is not permitted.[21]

The court then gave the following example:

> [A]n investor might purchase stock in a shipping venture involving a single vessel in reliance on a misrepresentation that the vessel had a certain capacity when in fact it had less capacity than was represented in the prospectus. However, the prospectus does disclose truthfully that the vessel will not be insured. One week after the investment the vessel sinks as a result of a casualty and the stock becomes worthless. In such circumstances, a fact-finder might conclude that the misrepresentation was material and relied on by the investor but that it did not cause the loss.[22]

The court in *Huddleston* referenced Judge Meskill's widely quoted dissent in *Marbury Management, Inc. v. Kohn*, 629 F.2d 705 (2d Cir. 1980), where Judge Meskill observed:

> From time immemorial proof of proximate cause – the legal link between the misconduct alleged and the injury averred – has been a precondition of recovery under theories of fraud and deceit. It is axiomatic that fraudulent misrepresentations are not actionable where the subsequent injury is due to an intervening or supervening cause. As applied to the sale of stock precipitated by misstatements, these principles of causation are satisfied only where the misrepresentation touches upon the reasons for the investment's decline in value. Thus, where one is induced to purchase securities in reliance upon a claim which, however deceitful, is immaterial to the operative reason for the pecuniary loss,

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21 *Huddleston v. Herman & MacLean,* 640 F.2d at 549 (emphasis added).

22 *Id.* at 549 n.26.

> recovery under a theory of fraud is precluded by the inability to prove requisite causation.[23]

Judge Meskill observed that proximate cause requirements under common law and loss causation requirements under federal securities law were designed to make sure that even an alleged wrongdoer does not "become an insurer of the investment, responsible for an indefinite period of time for any and all manner of unforeseen difficulties which may eventually beset the stock."[24]

In *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161 (2d Cir. 2005), the court addressed whether the district court properly dismissed a claim by investors who claimed they were induced by fraudulent research reports to purchase securities of companies whose prices later declined. In affirming the dismissal, the court observed that plaintiff had to allege and prove not only transaction causation – which it described as an allegation that "but for the claimed misrepresentations or omissions, the plaintiff would not have entered into the detrimental securities transactions" – but also loss causation.[25] The court stated that for there to be loss causation with regard to publicly-traded securities, the misstatement or omission must "conceal[] something from the market that, when disclosed, negatively affected the value of the security." "Otherwise," the court stated, "the loss in

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23 *Marbury*, 629 F.2d at 718 (emphasis added).

24 *Id.*

25 *Lentell,* 396 F.3d at 172.

question was not foreseeable."[26] Although plaintiffs alleged that the research reports in *Lentell* were misleading, the court found that this did not satisfy loss causation because "plaintiffs do not allege that the subject of those false recommendations . . . or any corrective disclosure regarding the falsity of those recommendations, is the cause of the decline in stock value that plaintiffs claim as their loss."[27] With regard to allegedly misleading research reports, the court stated, "[t]he only misrepresentation that can inhere to the 'buy' and 'accumulate' recommendations is that they were not Merrill's true and sincere opinion", and there was no loss causation because "plaintiffs allege no loss resulting from the market's realization that the opinions were false, or that Merrill concealed any risk that could plausibly (let alone foreseeably) have caused plaintiffs' loss."[28]

In short, the federal securities law concept of loss causation is based on the common law concept of proximate cause. The policy underlying both, especially as applied to disclosure claims involving publicly-traded securities, is that even alleged wrongdoers are not responsible for market losses untethered to their alleged misrepresentations or omissions. "But for" causation, while necessary for a plaintiff to plead a claim for common law fraud or securities fraud, is not sufficient

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26 *Id.* at 173 (emphasis added).

27 *Id.* at 175.

28 *Id.* at 176.

or else an alleged wrongdoer would be an insurer against losses unrelated to any misrepresentation or omission. Since any wrongful inflation of an actively traded security is embedded in the price of that security until the concealed facts are disclosed or the misrepresentations are revealed as such, one who sells before the misrepresentations or concealed facts are revealed to the marketplace has no claim for relief – at common law and under the federal securities laws. Far from being in tension, the similarity of the causes of action, the overlapping elements of proximate cause and loss causation, and the identical policy considerations suggest that the results should be the same, i.e., recovery should be denied when an investor in a publicly-traded security fails to show not only "but for" causation but also that the decline in the price of the security was proximately caused by disclosures concerning the alleged misrepresentations or omissions.

II. ON THE FACTS OF THIS CASE, SOUND PUBLIC POLICY SUPPORTS REJECTION OF HOLDERS' COMMON LAW SECURITIES CLAIM

As discussed above, the careful balancing of investor protection interests with the interest in avoiding abusive litigation and windfall recoveries has led courts to limit claims in federal securities cases to investors who purchased or sold in reliance on alleged misrepresentations or omissions rather than those who claim they were induced not to purchase or sell. These policy considerations apply equally to common law actions involving public securities.

PIABA, in its amicus, asks that this Court depart from the result reached in *Blue Chip Stamps* for a variety of reasons that are unpersuasive.

First, PIABA states that the common law addresses conduct that induces a plaintiff "to refrain from acting." (PIABA Br. at 1.) But PIABA itself concedes that in the context of securities claims based on allegedly misleading statements, there is no common law claim based on being induced not to purchase. (Id. at 4 n.2.) PIABA does not explain why, if the forbearance language is dispositive, non-seller and non-purchaser claims should be treated differently.

Second, PIABA simply rejects the policies that the Supreme Court found dispositive in *Blue Chip Stamps*, not because of considerations unique to common law securities claims, but because it thinks the Supreme Court wrongly decided *Blue Chip Stamps*. (PIABA Br. at 4-7.) With due respect to PIABA, it has simply given conclusive weight to one of those concerns (the opportunity for investors to seek redress) and no weight to the countervailing considerations discussed at length by the Supreme Court. Since PIABA represents lawyers that make their living by suing brokerage firms, that is understandable, but it is not a basis for rejecting the Supreme Court's detailed analysis of these countervailing considerations.

Third, PIABA mentions that the Supreme Court itself in *Blue Chip Stamps* acknowledged that the common law provides forbearance claims. (PIABA Br. at

8-9.) But it ignores that the Court emphasized that such common law forbearance cases were "light years away" from modern securities transactions, and that the policies it identified as being critical to its analysis of the securities claims applies equally to common law claims involving securities transactions. No one can fairly read the Supreme Court's decision in *Blue Chip Stamps*, particularly its observation that common law forbearance cases are "light years away" from modern securities transactions, as supporting the creation of causes of action for persons who claim they were induced not to buy or sell securities.

Fourth, PIABA observes that various statutes and regulations do not provide relief to persons who claim they were induced not to take action in connection with securities transactions (PIABA Br. at 9-10.) But the obvious implication of this is not that the courts should, therefore, create such actions under common law, but that legislatures recognize the sound policy reasons counseling against allowing such claims.

Fifth, PIABA states that failing to provide a cause of action for holders would encourage misconduct by those in the securities industry. But, in cases involving widely disseminated information (such as research reports) it is absurd to suggest that the possibility of liability to thousands of actual purchasers and sellers, as well as the potential for government criminal and civil actions, is an inadequate deterrent. To be sure, some miscreants may still violate the law, but they are not the type of miscreants who would change their calculus based on whether there is also potential liability to holders.

NASCAT, whose website boasts that its members are made up of "many of the most well known and prestigious firms in the plaintiff's class action community" (http://www.nascat.org/about/), has very recently filed an amicus brief that makes many of the same arguments as PIABA.

First, NASCAT states that it is a "myth" that "every fraud claim based upon fraudulently induced forbearance is, by definition, unmeritorious." (NASCAT Br. at 4.) As discussed above, the United States Supreme Court acknowledged in *Blue Chip Stamps* that a purchaser-seller requirement would foreclose some meritorious suits but nevertheless imposed a strict purchaser-seller requirement because of the overwhelming countervailing considerations.

Second, NASCAT states that it is a "myth" that because federal securities law prohibits holder claims, Georgia should too. (NASCAT Br. at 4.) Of course, Georgia is free to adopt any standard it chooses. We simply point out that in a global securities market, there is a benefit in harmonizing federal and state law as it applies to identical transactions. Like PIABA, NASCAT also points to the fact that the Supreme Court recognized the possibility of state law remedies in *Blue Chip Stamps*. But like PIABA, NASCAT also ignores the Supreme Court's observation that the common law forbearance cases are "light years away" from modern securities transactions and that every one of the policies identified by the Supreme Court in *Blue Chip Stamps* has equal application to securities law claims brought at common law. NASCAT also mistakenly claims that the ruling was based on the language of Section 10(b), ignoring that the Supreme Court in *Dabit* held that the language of Section 10(b) covered holders and that *Blue Chip Stamps* had been based "principally on policy considerations" involving modern securities transactions.[29]

Third, NASCAT states that it is another "myth" that forbearance claims are inherently unprovable. (NASCAT Br. at 9). But, the Supreme Court's concern in *Blue Chip Stamps* was not that such claims were inherently unprovable, but that the proof could be easily manufactured and lead to abusive litigation and windfall recoveries because it consisted of what plaintiff would say was in his head in the context of complaining about widely disseminated communications related to publicly-traded securities.

Fourth, NASCAT identifies as another "myth" Defendants' argument that a clear majority of states to have considered the issue have rejected holder claims. To bolster their otherwise unsupported proposition, NASCAT cites obsolete cases, decided long before the Supreme Court's *Blue Chip Stamps* opinion, and some even before the enactment of the securities laws, when different conditions existed

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29 *Dabit*, 547 U.S. at 80 (2006).

in the securities markets, and, hence, different policy interests were at stake. These cases are inapposite.[30]

In addition, even assuming the accuracy of the statement that the majority of *other* states to have considered the issue recognize holder status, SIFMA (as we stated at the outset) is not addressing the common law precedents that the parties have extensively briefed, but rather is addressing the policy considerations that have been paramount in cases involving similar transactions. If the precedent in Georgia mandated a particular result, we do not believe the Second Circuit would have certified the case to this Court. We have focused on policy considerations because we, as well as the Second Circuit, understand there is no controlling Georgia precedent on the issues presented.

Fifth, NASCAT states that another "myth" is that there can be no "injury" in a holders' case. (NASCAT Br. at 15.) But, again, neither the Supreme Court nor SIFMA denied that a holder could ever be injured. Rather, we have pointed out that the purchaser-seller limitations arose from a balancing of public policy considerations that included not only potential harm to holders but also countervailing factors – such as the ease of manufacturing forbearance claims in

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30 *Fottler v. Moseley*, 60 N.E. 788 (Mass. 1901), the 1901 Massachusetts case cited by NASCAT, is distinguishable for the additional reason that the plaintiff there did, in fact, take concrete steps towards selling his securities, by placing an order to sell, which he later withdrew. This is not the case here.

volatile public securities markets where billions of shares change hands every day and where it is incredibly tempting for a plaintiff, with the benefit of hindsight, to claim she would have bought at a lower price or sold at a higher price had it not been for defendant's allegedly fraudulent statements, which might not have even been intended to reach plaintiff.

This very case illustrates the problem of holder claims and the heightened risk of windfall recoveries and abusive litigation. Holmes was wealthy and sophisticated enough to amass 2.1 million shares of Worldcom and hold it when the stock was still trading at more than $90 a share.[31] He now wants to recover on a theory that he would have sold it all for more than $200 million if, more than ten years ago, he had not read a favorable research report prepared for general circulation to clients by a firm that followed telecommunication companies. On its face, it is implausible that an investor sophisticated enough to have amassed a $200 million fortune would make a 15-month long non-investment decision on the basis of a single such report that 1) did not even address his personal circumstances and 2) would have been superseded many times during the 15 months that Holmes claims he relied on it. In light of the absence of controlling precedent permitting such claims to proceed under Georgia common law, SIFMA submits that the same

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31 Joint Appendix-1877-78, ¶¶147, 154.

balancing of policy considerations that led the Supreme Court to reject such claims in *Blue Chip Stamps* should lead to a rejection of such claims here.

III. PLAINTIFFS HAVE FAILED TO PLEAD FACTS SHOWING DEFENDANTS' CONDUCT PROXIMATELY CAUSED THE LOSSES THEY SEEK TO RECOVER

Holmes's claim that but for the research reports, he would have sold his 2.1 million shares of Worldcom stock also fails the proximate cause requirements at common law.

As we discussed above, proximate cause under common law and loss causation under federal law reject claims based only on "but for" causation. The federal securities cases applying loss causation requirements under Section 10(b) acknowledge their debt to proximate causation requirements under common law, and they frequently equate the two. Under the cases discussed above, proximate cause (and loss causation) is satisfied in the context of securities transactions only when, unlike in this case, Plaintiff pleads that the misrepresentation or omission produced the decline in price that the Plaintiff seeks to recover.

Alleging proximate cause is not a matter of using magic language, but of alleging facts supporting a theory that, after plaintiff entered into the transaction at issue (or here the non-transaction at issue), the defendants' conduct caused the price decline for which the plaintiff seeks compensation. Where, as here, a plaintiff sells a publicly-traded security before there has been any disclosure related to an allegedly fraudulent research report, only "but for" causation is alleged. Indeed, one of the very purposes of proximate cause requirements in securities transactions – to eliminate the possibility that accused wrongdoers would be responsible for market losses and other losses that they did not cause – dictates this result. Again, this reflects the courts' careful balancing of the interest in providing truly aggrieved investors a reasonable remedy while at the same time avoiding windfall recoveries where the defendants' alleged misconduct did not cause the price decline.

PIABA's theory that it is enough to allege that misrepresentations and omissions "caused the [plaintiffs] to hold their existing Worldcom securities" (PIABA Br. at 14) is clearly wrong as that is the standard formulation for what the courts sometimes refer to as "but for" causation or "transaction causation" or "reliance," but not proximate causation. It does not satisfy the requirement that plaintiffs demonstrate the price decline was attributed to defendants' misconduct. Moreover, it is no answer for PIABA to state this is not a fraud-on-the-market case. First, concepts of proximate cause are not limited to fraud-on-the-market cases, but rather apply broadly to claims at common law. Second, although plaintiffs allege individual reliance, what they allegedly relied on was a research report on a very widely followed public company whose stock was actively traded and whose price, therefore, reflected whatever public information existed in the marketplace about it. In those circumstances, plaintiffs' failure to allege that the decline in the price of the stock was caused by the allegedly misleading disclosures being revealed as such does not satisfy proximate cause under the cases discussed above.

Finally, PIABA's attempt to use language like "foreseeable" simply does not fit the facts alleged here. To be sure, it is foreseeable that stock prices go up and down, but to say that it is foreseeable that the price of a stock might go down is not to show that it went down because the misstatements defendants made were revealed to the market – which is what the courts require to show proximate cause and loss causation. Here, Holmes failed to allege any reason for the decline in Worldcom stock between 1999 and 2000. This is not surprising – since Holmes sold before any corrective disclosure allegedly related to the research report, he was selling at a price that had not been adversely affected by the report on which he claims to have relied. On these facts, Holmes has not pled proximate cause under the common law.

CONCLUSION

For the foregoing reasons, SIFMA respectfully urges that this Court harmonize Georgia law with federal law applicable to similar securities transactions and hold 1) Georgia common law does not recognize a claim by non-sellers of securities on the facts pled here, and 2) Plaintiffs' allegations fail to satisfy the requirements of proximate cause under Georgia law.

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