No. 17-664

In the Supreme Court of the United States

PETRÓLEO BRASILEIRO S.A. – PETROBRAS, *ET AL.*,
Petitioners,

v.

UNIVERSITIES SUPERANNUATION SCHEME LTD., *ET AL.*,
Respondents.

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

BRIEF OF AMICUS CURIAE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF PETITIONERS

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Table of Contents

Page

TABLE OF CONTENTS.......................................i

TABLE OF AUTHORITIES..................................iv

INTEREST OF *AMICUS CURIAE*..........................1

SUMMARY OF ARGUMENT.................................1

ARGUMENT..4

I. THE SECOND CIRCUIT HAS SUBSTANTIALLY LOWERED THE BAR FOR PROVING MARKET EFFICIENCY PRIOR TO CLASS CERTIFICATION...4

A. *Halliburton II* Required a Plaintiff to Prove Market Efficiency Before Class Certification...4

B. The Second Circuit Has Excused Plaintiffs from Providing Any Empirical Evidence of Market Efficiency in Many Typical Cases............5

C. Even in Cases in which the Second Circuit Says Empirical Evidence of Market Efficiency Is Required, the Court Accepts a Flawed Test as Sufficient..8

D. The Second Circuit's Holdings Will Increase the Burdens that Securities Class Actions Impose on US Capital Markets 10

II. CERTIFICATION OF CLASSES WHEN ASCERTAINING THEIR MEMBERSHIP IS NOT ADMINISTRATIVELY FEASIBLE VIOLATES RULE 23 AND DUE PROCESS AND WOULD HARM INTERNATIONAL SECURITIES MARKETS 11

A. To Be Ascertainable, A Rule 23 Class Should Be Defined in an Administratively Feasible Way 12

B. The Significance of Administrative Feasibility Is Particularly Clear Here ... 14

1. The Securities at Issue Are Part of an Enormous and Consequential Global Market 15

2. It Is Difficult to Determine Whether Transactions in the OTC Market for Debt Securities Are Covered by U.S. Securities Laws 16

C. This Case Clearly Shows the Consequences of Deferring the Determination of Class Membership Until After Class Certification 23

D. The Decision of the Court Below also Undermines the Policy Goals of *Morrison* 25

CONCLUSION 26

Table of Authorities

Page(s)

Cases

Absolute Activist Value Master Fund Ltd. v. *Ficeto*,
677 F.3d 60 (2d Cir. 2012) 17, 18, 22

Am. Pipe & Constr. Co. v. *Utah*,
414 U.S. 538 (1974) 25

Basic Inc. v. *Levinson*,
485 U.S. 224 (1988) 5, 6

Blue Chip Stamps v. *Manor Drug Stores*,
421 U.S. 723 (1975) 24

Briseño v. *ConAgra Foods, Inc.,*
844 F.3d 1121 (9th Cir. 2017), *cert. denied*, --
S. Ct. ----, 2017 WL 1365592 (Oct. 10, 2017) 14

Cammer v. *Bloom*,
711 F. Supp. 1264 (D.N.J. 1989) 6

Carrera v. *Bayer Corp.*,
727 F.3d 300 (3d Cir. 2013) 13

City of Pontiac Policemen's & Firemen's Ret. Sys. v. *UBS AG*,
752 F.3d 173 (2d Cir. 2014) 15, 18

City Select Auto Sales Inc. v. *BMW Bank of N. Am. Inc.*,
867 F.3d 434 (3d Cir. 2017) 12, 13

Halliburton Co. v. *Erica P. John Fund, Inc.*,
134 S. Ct. 2398 (2014) 4, 5, 7, 8

In re DVI Sec. Litig.,
639 F.3d 623 (3d Cir. 2011) 7

In re Petrobras Sec. Litig.,
150 F. Supp. 3d 337 (S.D.N.Y. 2015) 22

In re Petrobras Sec. Litig.,
312 F.R.D. 354 (S.D.N.Y. 2016), *aff'd in part, vacated in part*, 862 F.3d 250 (2d Cir. 2017) 21

In re Petrobras Sec.,
862 F.3d 250 (2d Cir. 2017)........................*passim*

In re Vivendi Universal, S.A. Sec. Litig.,
765 F. Supp. 2d 512 (S.D.N.Y. 2011) 15

In re Xcelera.com Sec. Litig.,
430 F.3d 503 (1st Cir. 2005) 7

Krogman v. *Sterritt*,
202 F.R.D. 467 (N.D. Tex. 2001) 6

Loginovskaya v. *Batratchenko*,
764 F.3d 266 (2d Cir. 2014)...............................18

Marcus v. *BMW of N. Am., LLC*,
687 F.3d 583 (3d Cir. 2012)...............................13

Morrison v. *National Australia Bank Ltd.*,
561 U.S. 247 (2010) ....*passim*

SEC v. *Levine*,
462 Fed. Appx. 717 (9th Cir. 2011)...................17

SEC v. *Tex. Gulf Sulphur Co.*,
401 F.2d 833 (2d Cir. 1968)...............................10

Stoneridge Inv. Partners, LLC v. *Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008) 10

Teamsters Local 455 Freight Div. Pension Fund v. *Bombardier Inc.*, 546 F.3d 196 (2d Cir. 2008)................................. 7

United States v. *Georgiou*, 777 F.3d 125 (3d Cir. 2015)............................... 17

Waggoner v. *Barclays PLC*, No. 16-1912, 2017 WL 5077355 (2d Cir. Nov. 6, 2017) 6, 7

Statutues and Other Authorities

17 C.F.R. § 23.202... 22

17 C.F.R. § 240.17a-3.. 21

17 C.F.R. § 240.17a-4.. 21

Fed. R. Civ. P. 23 ....2-3, 14

FINRA Rule 6730(c) 21

UCC § 8-502 cmt. 2.. 20

SIFM, *2017 Fact Book* (2017)........................... 15, 19

Cornerstone Research, *Securities Class Action Filings: 2017 Midyear Assessment* (July 2017) 10

Darius P. Miller & John J. Puthenpurackal, *Security Fungibility and the Cost of Capital: Evidence from Global Bonds*, 40 J. Fin. & Quantitative Analysis 849 (2005) 16, 19

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Juan Carlos Gozzi et al., *How Firms Use Corporate Bond Markets under Financial Globalization*, 58 J. Banking & Fin. 532 (2015) 15

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Morten Bech et al., *Hanging Up The Phone – Electronic Trading in Fixed Income Markets and Its Implications*, BIS Quarterly Review, Mar. 2016 .... 20, 21

Paul Ferrillo, Frederick Dunbar & David Tabak, *The "Less Than" Efficient Capital Markets Hypothesis: Requiring More Proof From Plaintiffs in Fraud-on-the-Market Cases*, 78 St. John's L. Rev. 81 (2004) 8, 9

Richard A. Brealey et al., *Principles of Corporate Finance* 598 (10th ed. 2011) 15

Richard D. Bernstein et al., *Closing Time: You Don't Have to Go Home, But You Can't Stay Here*, 67 Bus. Law. 957 (2012) 22

SIFMA Asset Management Group, *Best Execution Guidelines for Fixed-Income Securities* 8 (updated Sept. 2008) 22

INTEREST OF AMICUS CURIAE[1]

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. SIFMA has U.S.-based members who do business abroad, have branches abroad, and/or have non-U.S.-based customers. It also has non-U.S.-based members who have non-U.S.-based customers. SIFMA's 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. It regularly files amicus curiae briefs in cases raising issues of vital concern to securities industry participants. This case involves important issues concerning standards for class certification in private securities actions and the extraterritoriality of the U.S. securities laws, which are directly relevant to SIFMA's mission.

SUMMARY OF ARGUMENT

The Second Circuit's ruling significantly reduces the threshold for plaintiffs seeking certification of a class in securities actions, in two ways.

First, before a securities plaintiff is granted the powerful fraud-on-the-market presumption of reliance necessary to obtain class certification, this

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[1] All parties have received appropriate notice and consented to the filing of this brief. No party's counsel authored this brief in whole or in part, and no person, other than amicus curiae or its counsel, contributed money that was intended to fund the preparation or submission of this brief.

Court has required that the plaintiff first prove, among other things, that the security in question traded in an "efficient market." In the decision below, the Second Circuit reduced the requirement for proving market efficiency below that contemplated by this Court's precedent, both by significantly limiting the circumstances in which plaintiffs must provide empirical evidence of market efficiency and by relaxing the standard for what constitutes sufficient empirical evidence when still required.

Under the Second Circuit's approach, as a practical matter many securities plaintiffs will be able to invoke the fraud-on-the-market presumption (and shift the burden of rebuttal to defendants) by showing nothing more than that the issuer defendant is a large and exchange-traded company. If the decision below stands, in the typical large-company case plaintiffs will not be required to provide *any* empirical evidence showing that the market responds efficiently to new information. And even in the atypical case, in which the Second Circuit's ruling *might* require plaintiffs to provide empirical evidence of market efficiency, the ruling allows a plaintiff to show market efficiency using a weak statistical test that ignores the direction of price movements. Thus, even price increases in the face of bad news and price drops in the wake of good news—which are strongly indicative of market *inefficiency*—can be treated as evidence of market *efficiency* under the Second Circuit's test.

Second, this case also presents a critical question about the ascertainability requirement for certification of class actions under Rule 23 of the

Federal Rules of Civil Procedure ("Rule 23"). There is a fundamental disagreement among the circuits about whether the proponent of class certification must demonstrate an "administratively feasible" method to ascertain who is a member of a class without "extensive and individualized fact-finding," or if it is sufficient that a class definition is based on "objective criteria" without regard to the feasibility of applying those criteria.

The difference between these two standards has important real-world effects. Plaintiffs will be left unsure about whether or not they are class members who are bound by a judgment of the court. Defendants, for their part, will not know which investors are covered by the res judicata effect of any judgment and will be forced to grapple with strategic decisions (including whether to litigate or settle) without knowing the potential scope or magnitude of their damages exposure.

The importance of enforcing an administrative feasibility requirement under Rule 23 is well-illustrated by this case, which involves international debt securities that trade in the "over-the-counter" (OTC) market. On the facts of this case, it would be virtually impossible to know which class members' transactions are subject to U.S. securities laws without a substantial individualized inquiry.

ARGUMENT

I. THE SECOND CIRCUIT HAS SUBSTANTIALLY LOWERED THE BAR FOR PROVING MARKET EFFICIENCY PRIOR TO CLASS CERTIFICATION

This Court has recognized that "market efficiency" is one of the essential "prerequisites" that a plaintiff must prove before invoking the fraud-on-the-market presumption of reliance at the class certification stage. In *Halliburton II*, this Court held that the presumption rests upon the "modest premise" that "public information generally affects stock prices." *Halliburton Co.* v. *Erica P. John Fund, Inc.*, 134 S. Ct. 2398, 2410 (2014) ("*Halliburton II*").

The Second Circuit's decision is worthy of review by this Court because of the fundamental respects in which it departed from *Halliburton II*. The Second Circuit first erred by adopting a test that, in many cases, abates the requirement of *Halliburton II* that a plaintiff demonstrate market efficiency. The Second Circuit also erred by holding that empirical evidence of market efficiency, to the extent required, can be supplied by a statistical test that does not account for the directionality of price movements.

A. *Halliburton II* Required a Plaintiff to Prove Market Efficiency Before Class Certification

It is settled law that "a plaintiff must make the following showings to demonstrate that the presumption of reliance applies in a given case: (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 (citing *Basic Inc.* v. *Levinson*, 485 U.S. 224, 248 n.27 (1988)) (emphasis added). "The burden of proving those prerequisites . . . rests with plaintiffs and (with the exception of materiality) must be satisfied before class certification." *Id.* at 2412.

In *Halliburton II*, as plaintiffs generally do in securities class actions, the plaintiff satisfied its burden with "an event study of various episodes that might have been expected to affect the price of Halliburton's stock." *Id.* at 2415 (citing *Halliburton II* App. 217-30). Specifically, that event study identified all the dates during the class period on which Halliburton's stock experienced a statistically-significant company-specific return, identified any new information about Halliburton released on those days, and analyzed whether the company-specific returns were directionally consistent with the content of the information.

B. The Second Circuit Has Excused Plaintiffs from Providing Any Empirical Evidence of Market Efficiency in Many Typical Cases

In this case, the Second Circuit held that plaintiffs satisfied their burden by pointing to typical public company characteristics and by providing some empirical evidence of about price movements falling well below the level of an event study. *In re Petrobras Sec.*, 862 F.3d 250 (2d Cir. 2017).

The Second Circuit's holding in this case was endorsed and extended in *Waggoner* v. *Barclays PLC*, No. 16-1912, 2017 WL 5077355 (2d Cir. Nov. 6, 2017). In *Barclays*, the Second Circuit held that empirical evidence of market efficiency is generally not necessary at all unless one or more of the typical public company characteristics is absent. *Id.* at *12-14. Because all the characteristics were present in *Barclays*, the Second Circuit did not require plaintiff to supply *any* empirical evidence of market efficiency. *Id.* at *13-14. While, in a footnote, the court stated that it was not creating a *per se* rule that "securities of large publicly traded companies always trade in an efficient market," it declined to specify the "specific circumstances" (other than the absence of one or more of the typical characteristics) that would require a plaintiff to present empirical evidence of market efficiency. *Id.* at *14 n.29.

The characteristics of public companies identified by the Second Circuit as normally sufficient to invoke the *Basic* presumption without resort to empirical evidence of market efficiency include: whether an issuer is eligible to file a simplified registration statement; whether the stock has a large market capitalization; whether the stock is covered by analysts; whether the stock is traded by market makers; and whether the stock has a high trading volume.[2] Because these characteristics will invariably be present for nearly all large, exchange-traded companies, the result of

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[2] These factors were developed in *Cammer* v. *Bloom*, 711 F. Supp. 1264 (D.N.J. 1989), and *Krogman* v. *Sterritt*, 202 F.R.D. 467 (N.D. Tex. 2001).

the Second Circuit's rule in *Petrobras* and *Barclays* is that, in most cases, plaintiffs will not have to provide *any* event study evidence of the sort before this Court in *Halliburton II* to meet their burden of showing market efficiency.

Prior to this case, most lower courts had rightly recognized empirical evidence of a relationship between new information and securities prices as the "most important" factor in proving market efficiency. *E.g.*, *In re DVI Sec. Litig.*, 639 F.3d 623, 634 (3d Cir. 2011); *Teamsters Local 455 Freight Div. Pension Fund* v. *Bombardier Inc.*, 546 F.3d 196, 207 (2d Cir. 2008); *In re Xcelera.com Sec. Litig.*, 430 F.3d 503, 512 (1st Cir. 2005). The public company characteristics deemed sufficient by the Second Circuit do not and cannot establish market efficiency, however. At most, they suggest a mechanism by which new information could in theory influence securities prices. Only empirical evidence tests whether that in fact occurs.

C. Even in Cases in which the Second Circuit Says Empirical Evidence of Market Efficiency Is Required, the Court Accepts a Flawed Test as Sufficient

The Second Circuit also held that plaintiffs here provided "direct evidence" of market efficiency by passing the so-called "FDT test." 862 F.3d at 276-77.[3] Unlike the market efficiency evidence before this Court in *Halliburton II*, an FDT test is not an event study and does not test whether company-specific returns are consistent with the content of new information.

The FDT test merely compares the proportion of "days with news" on which there were statistically significant stock price movements to the proportion of "days with no news" on which significant movements occurred. Ferrillo et al., *supra* n.3, at 119-22. That's all. The test says nothing about the *directionality* of securities price movements—that is, whether the price declines in response to bad news and increases in response to good news, or vice versa.

No peer reviewed article has ever endorsed the FDT test as a sufficient test of market efficiency. Indeed, the same law review article that introduced the FDT test said that it should be used as a

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[3] The label "FDT" derives from the first letters of the last names of authors of the non-peer-reviewed law review article first discussing this test: Paul **F**errillo, Frederick **D**unbar & David **T**abak, *The "Less Than" Efficient Capital Markets Hypothesis: Requiring More Proof From Plaintiffs in Fraud-on-the-Market Cases*, 78 St. John's L. Rev. 81 (2004).

"threshold step, not a sufficient condition, to show that a stock traded in an efficient market." *Id.* at 122. Rather, the FDT test was described as a robustness check to be applied to a more traditional showing, which might involve only a "small number" of observations. *Id.* at 128. The Second Circuit has thus approved the use of the test in a context that its authors plainly did not intend. And there is good reason why they did not intend it.

Suppose, for example, that after properly controlling for general market effects and industry effects, the company's stock price increases after company-specific bad news. That observation would tend to show that the market is *not* efficient. But the FDT test, as applied by the Second Circuit, would illogically treat the observation as evidence that the market *is* efficient. The Second Circuit's use of the FDT test is like allowing pharmaceutical companies seeking to prove that a drug is beneficial simply to show a drug has *some effect* on patients—whether it cures them or kills them.

Together, the Second Circuit's holdings—that (i) no empirical evidence of market efficiency is necessary in many cases; and (ii) even when required, the non-directional FDT test is sufficient empirical evidence of market efficiency—significantly undermine the important requirement that a plaintiff prove market efficiency before class certification.

D. The Second Circuit's Holdings Will Increase the Burdens that Securities Class Actions Impose on US Capital Markets

The Second Circuit's easing the path to class certification comes at a time when securities class actions are already being filed at a "record pace." At this rate, 9.5% of all companies listed on either NYSE or NASDAQ will be sued this year.[4] That level of litigation imposes real costs on capital markets and investors as a whole.

The class certification stage serves an important gatekeeping function. Once a class is certified, defendants are often forced to settle.[5] As this Court has recognized, that dynamic often "allow[s] plaintiffs with weak claims to extort settlements from innocent companies." *Stoneridge Inv. Partners, LLC* v. *Scientific-Atlanta, Inc.*, 552 U.S. 148, 162-64 (2008). And the costs of these settlements are "payable in the last analysis by innocent investors, for the benefit of speculators and their lawyers." *SEC* v. *Tex. Gulf Sulphur Co.*, 401 F.2d 833, 867 (2d Cir. 1968) (Friendly, J., concurring).

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[4] *See* Cornerstone Research, *Securities Class Action Filings: 2017 Midyear Assessment* 1, 15 (July 2017), https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2017-Midyear-Assessment.

[5] *See* 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 . . . .").

II. CERTIFICATION OF CLASSES WHEN ASCERTAINING THEIR MEMBERSHIP IS NOT ADMINISTRATIVELY FEASIBLE VIOLATES RULE 23 AND DUE PROCESS AND WOULD HARM INTERNATIONAL SECURITIES MARKETS

The circuit courts are currently divided as to whether a class can be certified if it is not administratively feasible to determine who is in the class. The division on this question produces considerable uncertainty for class action litigants, creates significant due process issues, and creates a major incentive for forum shopping by plaintiffs.

Without a class whose membership is ascertainable, due process issues will arise throughout class litigation. It will be impossible to give proper notice to potential class members, because without a workable means of determining who is a class member, any notice will necessarily be either over-inclusive or under-inclusive—and often both. Even if they do receive notice, potential class members will be unable to determine whether their interests are at issue.

Defendants will also be disadvantaged because they will not know the true size of the class and thus the scope of their potential liability. Even after a settlement or a victory on the merits, defendants will not be able to know who will be bound by the judgment and thus barred from asserting future claims.

These concerns are particularly evident in the instant case, which involves international debt securities. Under this Court's jurisprudence, the U.S. securities laws only apply if the securities at issue were purchased on a domestic exchange or in

a domestic transaction. Plaintiffs here chose to define their class as broadly as possible under the law, including all who purchased in "domestic transactions." But the test for what constitutes a domestic transaction is complicated and fact-intensive, and in cases such as this one the necessary facts are not readily available. Therefore, the decision by the court below to certify a class without regard to whether there is an administratively feasible way to determine who is or is not a class member introduces significant confusion into litigation involving debt securities, which will have deleterious effects on an enormous, and globally important, market.

A. To Be Ascertainable, A Rule 23 Class Should Be Defined in an Administratively Feasible Way

In their Brief in Opposition, Plaintiffs-Respondents incorrectly assert that only one circuit court requires administrative feasibility. *See* Resp't Br. in Opp'n at 26-29. In fact, as Defendants-Petitioners note, several circuits—the Third, Fourth, and Eleventh—currently recognize that a class cannot be certified unless the class definition can be readily applied to determine who belongs to the class. Pet. at 30-32.[6] On the other

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[6] The status of the administrative feasibility is not, as Plaintiffs-Respondents claim, "uncertain" in the Third Circuit, Resp't Br. in Opp'n at 27; indeed, the Third Circuit recently reaffirmed this requirement. *City Select Auto Sales Inc.* v. *BMW Bank of N. Am. Inc.*, 867 F.3d 434, 439 (3d Cir. 2017). Plaintiffs alleged that some subset of individuals listed in a consumer database received junk faxes in violation of the Telephone Consumer Protection Act. The Third Circuit held that

hand, the Sixth, Seventh and Ninth Circuits have rejected the administrative feasibility requirement, holding that ascertainability is satisfied as long as the class is defined based on an "objective" test. Pet. at 31-32.

In the decision below, the Second Circuit joined the circuits rejecting administrative feasibility, holding that "a class is ascertainable if it is defined using objective criteria that establish a membership with definite boundaries." 862 F.3d at 257. Certiorari should be granted here; otherwise, considerable confusion and incentives for forum shopping result from the fact that litigants in certain circuits will benefit from this standard while litigants in other circuits will not.

Moreover, review by this Court of the decision below is warranted because the administrative feasibility requirement protects absent class members by facilitating proper notice, including for the purpose of opting out or objecting to a settlement, and protects defendants' due process rights, including the right to challenge each claimant's class membership and the practical ability to bind all class members in the event of a defense verdict. *Carrera* v. *Bayer Corp.*, 727 F.3d 300, 305-06 (3d Cir. 2013) (citing *Marcus* v. *BMW of N. Am., LLC*, 687 F.3d 583, 593 (3d Cir. 2012)).

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this database, combined with affidavits from recipients, could potentially satisfy the ascertainability requirement, but noted that "a high degree of over-inclusiveness"—that is, entities listed in the database who did not receive junk faxes— "could prevent certification." *Id.* at 442 & n.4.

B. The Significance of Administrative Feasibility Is Particularly Clear Here

Ascertainability can arise in the context of any class action under Rule 23. Recent cases have concerned retail transactions and other consumer actions. *E.g.*, *Briseño* v. *ConAgra Foods, Inc.*, 844 F.3d 1121 (9th Cir. 2017), *cert. denied*, -- S. Ct. ----, 2017 WL 1365592 (Oct. 10, 2017).[7] But these considerations are particularly salient in class actions involving international securities, where even the basic question of where a transaction took place can require an intensive factual inquiry. This case is thus an excellent vehicle to resolve the circuit split because it clearly presents the consequences of the differing standards.

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[7] This case demonstrates the significance of administrative feasibility much more clearly than it was presented in *ConAgra*. In *ConAgra*, the defendant argued that there was no administratively feasible way to identify class members where the class was defined as consumers who had purchased a specific product. 844 F.3d at 1124. The predicate question for class membership in ConAgra was simply whether or not the consumer purchased the product, and was thus based on facts that that the consumer would have known when making the purchase. Similarly, defendant-sellers would have records of the quantity of products sold. Here, by contrast, neither potential plaintiffs nor defendants have knowledge or records sufficient to determine either whether individual investors are part of the class or the size of the class overall.

1. The Securities at Issue Are Part of an Enormous and Consequential Global Market

Like most debt securities, Petrobras's debt securities trade "over the counter" (OTC), rather than on an exchange.[8] Investors who wish to purchase bonds OTC generally place orders with dealers, who in turn will either match an order with an offer from another investor or sell the bonds from their own inventories. Since 2002, there have been over 79,000 issues of international debt securities.[9] There are currently approximately $92 trillion of debt securities outstanding.[10]

More specifically, the Petrobras bonds at issue here are "global bonds," which are bonds with custody and clearing arrangements that make them easily tradeable across geographic markets.[11]

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[8] While debt securities are sometimes *listed* (or *approved* for trading) on exchanges, debt securities generally are not actually *traded* on exchanges. *See, e.g.*, Juan Carlos Gozzi et al., *How Firms Use Corporate Bond Markets under Financial Globalization*, 58 J. Banking & Fin. 532, 535 n.11 (2015). Mere *listing*, without *trading*, is insufficient for the federal securities laws to apply. *See, e.g.*, *City of Pontiac Policemen's & Firemen's Ret. Sys.* v. *UBS AG*, 752 F.3d 173, 179-80 (2d Cir. 2014) (rejecting "listing theory"); *In re Vivendi Universal, S.A. Sec. Litig.*, 765 F. Supp. 2d 512, 527-31 (S.D.N.Y. 2011) (collecting cases).

[9] SIFMA, *2017 Fact Book* 51 (2017), *available at* https://www.sifma.org/resources/research/sifma-fact-book-2017/ (hereinafter "Fact Book").

[10] Fact Book at 55, 57.

[11] *See* Richard A. Brealey et al., *Principles of Corporate Finance* 598 (10th ed. 2011).

Global bonds have become the "debt instrument of choice for large corporate issuers."[12] According to Thomson Reuters and Bloomberg data, more than $10 trillion of global bonds, in more than 7,000 offerings, have been issued since 2005. Such bonds were issued by corporations from at least 32 countries, from Australia to Venezuela.[13]

2. It Is Difficult to Determine Whether Transactions in the OTC Market for Debt Securities Are Covered by U.S. Securities Laws

Determining whether a putative class member's transactions in OTC debt securities are covered by the U.S. securities laws, as interpreted by this Court in *Morrison* v. *National Australia Bank Ltd.*, 561 U.S. 247 (2010), is not simple. In some cases, such as this one, it may require an inquiry that turns on information that is not in the hands of either an investor or an issuer. In *Morrison*, the Court held that the federal securities laws apply only to (i) transactions on U.S. securities exchanges

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[12] Lubomir Petrasek, *Multimarket Trading and Corporate Bond Liquidity*, 36 J. Banking & Fin. 2110, 2110-12 (2012); *see also* Darius P. Miller & John J. Puthenpurackal, *Security Fungibility and the Cost of Capital: Evidence from Global Bonds*, 40 J. Fin. & Quantitative Analysis 849, 849-55 (2005).

[13] These countries are: Australia, Austria, Belgium, Bermuda, Brazil, Canada, China, Colombia, Finland, France, Germany, Hong Kong, Ivory Coast, Jamaica, Japan, Luxembourg, Mexico, The Netherlands, Panama, Peru, Philippines, Poland, Republic of Ireland, South Korea, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States, Uruguay, and Venezuela.

and (ii) "domestic transactions in other securities." 561 U.S. at 267. Where, as is the case with the Petrobras debt securities at issue here, the securities do not trade on a U.S. exchange, the federal securities laws only apply to transactions that are "domestic." Because plaintiffs defined their class to reach the full breadth of "domestic transactions," the litigation will require evaluation of the circumstances of each class member's transaction.

To determine which transactions are domestic, courts look to various facts relating to both the purchase and the sale of the security. This is so because, unlike a consumer transaction, the counterparties to a securities transaction may be anywhere in the world, and may transact through intermediaries who also may be anywhere in the world. Given these complexities, courts have operationalized the "location of the *transaction*," as required under *Morrison*, 561 U.S. at 268, as the location where "irrevocable liability" was incurred. *E.g., United States* v. *Georgiou*, 777 F.3d 125, 135-36 (3d Cir. 2015); *SEC* v. *Levine*, 462 Fed. Appx. 717, 719 (9th Cir. 2011); *Absolute Activist Value Master Fund Ltd.* v. *Ficeto*, 677 F.3d 60, 62 (2d Cir. 2012).

This determination requires courts to consider a wide array of information, including, among other things, facts related to the "formation of the contracts, the placement of purchase orders, the passing of title, or the exchange of money," in order to determine where irrevocable liability was incurred. *Georgiou*, 777 F.3d at 136 (quoting *Absolute Activist*, 677 F.3d at 69, 70).

No one fact is necessarily sufficient to make a transaction domestic. For example, a transaction is not domestic, without more, just because the issuer is a U.S. resident, the investor is a U.S. resident, the investor placed a purchase order in the U.S., the dealer is in the U.S., the security is issued and registered in the U.S., or the investor wired funds to the U.S. *See Loginovskaya* v. *Batratchenko*, 764 F.3d 266, 274-75 (2d Cir. 2014); *City of Pontiac*, 752 F.3d at 181-82 & n.33; *Absolute Activist*, 677 F.3d at 68-70.

The characteristics of the Petrobras debt securities at issue here make it particularly difficult to determine whether they were acquired in a domestic transaction. Because of the ease with which they can be traded across geographic markets, the same security may change hands in both domestic and foreign transactions. A bond initially distributed through a foreign transaction may subsequently be sold in a domestic aftermarket transaction, just as a bond initially distributed through a domestic transaction may be traded in a foreign aftermarket transaction. For these reasons, it is generally not possible to isolate any subset of a tradeable security that would have been traded only in domestic transactions or that would never have been traded in domestic transactions.

The geographic facts relevant to a particular OTC transaction may not be limited to a single country. Cross-border debt transactions are

commonplace.[14] The dealers that place and trade these bonds, and the investors that buy them, are located both in the U.S. and abroad.[15] And both the dealers and investors may be headquartered in one place, while conducting their relevant operations from other places. Similarly, the securities accounts in which the bonds are held by the buyer and seller, and the bank accounts from which the purchase price is paid and received, may be located either in the U.S. or abroad. There are consequently many possible permutations of relevant contacts that could be either domestic or foreign.

Investors typically do not know whether their trades are domestic. Each participant in an OTC trade only knows the identity of the other participants with whom it is directly communicating. When talking to a dealer, an investor typically does not know whether the dealer is trading for its own account or whether there is a counterparty investor on the "other side" of the trade. And dealers often trade with agents, such as investment advisors, without knowing the identities of their principals. Indeed, an investment advisor typically has trading authority over multiple accounts, and the advisor may decide to which account to allocate the trade only after the fact.

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[14] In 2016 alone, non-U.S. persons traded $2.3 trillion of debt issued in the U.S.; and U.S. persons traded $11.2 trillion of debt issued abroad. Fact Book at 66, 64.

[15] Petrasek, *supra* n.12, at 2111-12; Miller & Puthenpurackal, *supra* n.12, at 852-53.

Furthermore, defining and isolating a single "transaction" may require "matching" closely related buys and sells. Multiple investors may buy units of a bond from a dealer contemporaneously with other investors selling units of the same bond to that dealer. A qualitative decision must be made as to whether—for purposes of the *Morrison* analysis—these are all separate transactions, and complex evidentiary issues can therefore arise concerning which purchases should be matched with which sales. In short, given the industry practice of booking securities trades on a net basis, matching can sometimes be more of an art than a science.[16]

Nor is the traditional OTC market the only way to trade. The volume of corporate bonds traded over electronic trading platforms has more than doubled over the past five years.[17] There are a number of different platforms that operate according to distinct trading protocols. Some permit an investor to enter into direct buy and sell transactions with one particular dealer. Others connect investors with multiple dealers. *Id.* at 81. Still other platforms, called "all-to-all," allow investors to trade with dealers or directly with

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[16] *See* UCC § 8-502 cmt. 2 ("Because securities trades are typically settled on a net basis by book-entry movements, it would ordinarily be impossible for anyone to trace the path of any particular security, no matter how the interest of parties who hold through intermediaries is described.").

[17] Morten Bech et al., *Hanging Up The Phone – Electronic Trading in Fixed Income Markets and Its Implications*, BIS Quarterly Review, Mar. 2016, at 84, *available at* http://www.bis.org/publ/qtrpdf/r_qt1603h.pdf.

other investors. *Id.* at 84. There are also different levels of transparency. Some platforms, known as "dark platforms" or "dark pools," allow parties to trade directly with each other while withholding their identities so that neither party knows the counterparty with whom it is trading. *Id.* at 83.

In short, given the realities of this market, there is often no easy, or uniform, answer to the question of *where* the trade occurred.

Nor are there records that could readily answer the question. Dealers are not required by SEC or FINRA to maintain, and they do not maintain, records stating whether a transaction is "domestic" under *Morrison*.[18] Nor are dealers required to tell their customers whether a trade was "domestic."[19]

Dealers' records of many facts relevant to *Morrison* will not be readily accessible and may not exist at all. A typical trade confirmation, for example, will include neither an ultimate determination of domesticity under *Morrison* nor all the key facts.[20] Reconstructing the

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[18] *See* 17 C.F.R. §§ 240.17a-3, 240.17a-4 (SEC recordkeeping rules); FINRA Rule 6730(c) (data required to be reported to TRACE).

[19] The District Court's assertion, without any record evidence, that the domesticity issue would be resolved by "discrete, objective record[s] routinely produced by the modern financial system," *In re Petrobras Sec. Litig.*, 312 F.R.D. 354, 364 (S.D.N.Y. 2016), *aff'd in part, vacated in part*, 862 F.3d 250 (2d Cir. 2017), was thus not accurate.

[20] *See, e.g.*, *In re Petrobras Sec. Litig.*, No. 14-9662 ("Dist. Ct. Dkt."), ECF No. 269-10 (example of a trade confirmation); Dist. Ct. Dkt. ECF No. 539 at 5 n.1

circumstances of particular trades—beyond those recited in the confirmation—is burdensome. Trades are typically negotiated informally, over the telephone or via instant electronic message.[21] For example, the sequence of "offer and acceptance" (and the locations of the offeror and offeree) may matter under *Morrison*.[22] Determining this information, if possible at all, would frequently require a voluminous collection and review of electronic communications and/or (if recorded)[23] phone calls. Indeed, at an earlier stage in this litigation the District Court conducted an extensive analysis of twenty documents submitted by named plaintiffs to determine whether they acquired securities in domestic transactions, and found that two of the four named plaintiffs failed to establish a domestic transaction. *In re Petrobras Sec. Litig.*, 150 F. Supp. 3d 337, 339-41 (S.D.N.Y. 2015).

(holding that an opt-out plaintiff's trade confirmations did "not provide any material locative details").

[21] *See* SIFMA Asset Management Group, *Best Execution Guidelines for Fixed-Income Securities* 8, 10 (updated Sept. 2008), *available at* https://www.sifma.org/wp-content/uploads/2017/05/sifma-amg-white-paper-best-execution-guidelines-for-fixed-income-securities.pdf.

[22] *See* Richard D. Bernstein et al., *Closing Time: You Don't Have to Go Home, But You Can't Stay Here*, 67 Bus. Law. 957, 964 (2012) (noting the ambiguity of how *Absolute Activist* would apply to an offer made in the U.S. and accepted abroad, or an offer made abroad and accepted in the U.S.).

[23] As authorized by Dodd-Frank, the CFTC requires swap dealers to record oral communications with customers. *See* 17 C.F.R. § 23.202. The SEC has not imposed similar regulations in the OTC market.

C. This Case Clearly Shows the Consequences of Deferring the Determination of Class Membership Until After Class Certification

Despite these complexities, the Second Circuit below held that the lack of administrative feasibility does not prevent certification of a class of debt securities acquired in domestic transactions. The court incorporated the *Morrison* inquiry into the predominance analysis as one of the issues to be balanced to determine whether common questions predominate over individual questions. 862 F.3d at 270-75. But the inability to determine who is and who is not part of the class cannot be cured, or even mitigated, by the presence of other, unrelated common questions. This case thus squarely presents the importance of this question, which is applicable to all class actions but particularly significant where OTC debt securities are at issue.

If an indeterminate standard, such as the "domestic transaction" test, can be incorporated into a class definition, the basic question of who is and who is not part of the class will not be resolved until after class certification. This raises serious due process concerns for both plaintiffs and defendants.

It will be impossible to give proper notice to potential class members, as any notice will necessarily be either over-inclusive or under-inclusive—and often both. For example, here notice could be given to all known investors who acquired Petrobras securities. But many of those investors would not satisfy *Morrison*'s domestic

transaction test, and so would not in fact be class members.

Even if they do receive notice, individuals will be unable to determine whether their interests are at issue without a factual investigation and ad hoc judgment as to whether they satisfy the class definition. Here, investors will have to collect various records, which may or may not resolve the Morrison question, from non-party entities.

Defendants will also be disadvantaged by their inability to estimate the scope of the class. The problem is particularly acute here: issuers and underwriters cannot estimate the proportion of non-domestic transactions to which the securities laws do not apply. They will thus face increased pressure to settle, because, as the Court has recognized, "even a complaint which by objective standards may have very little chance of success at trial has a settlement value to the plaintiff out of any proportion to its prospect of success at trial." *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 740 (1975).

Even if they are victorious on the merits, defendants will be unable to know which plaintiffs will be bound by the decision and thus barred from asserting future claims in other jurisdictions.

Nor can defendants be assured that the class membership decisions reached in these collateral proceedings after a defense verdict will be the same as those that would have been reached by the district court in the event of a verdict for the class. Thus, the class of persons who will bound by the res judicata effect of that judgment remains undefined. The ability of absent class members to claim the

benefit of a verdict in favor of the class while avoiding the consequences of a defense verdict would essentially revive the historically unfair practice of "one-way intervention" that Rule 23 was intended to eliminate. *Am. Pipe & Constr. Co.* v. *Utah*, 414 U.S. 538, 547 (1974).

These risks are particularly high in the instant case because the securities at issue trade globally. Defendants' ability to enforce a class verdict in their favor will depend on future decisions by unknown courts applying the laws of various international forums in which absent class members later choose to sue.

Parties that reach a settlement to resolve a class action will be similarly disadvantaged. Defendants will be unable to determine which potential plaintiffs will be bound by the terms of the settlement. Plaintiffs who receive notice will still not have clarity as to whether they really are class members whose interests are at issue. They will thus have to decide whether to opt out or object before knowing if the settlement even applies to them.

D. The Decision of the Court Below also Undermines the Policy Goals of *Morrison*

Delaying the resolution of the *Morrison* issue also undermines the policy goals underlying *Morrison* itself. By the time that a court conducts these mini-trials, the mischief of interfering with foreign securities regulation—including the regulation of "what discovery is available in litigation" and "what individual actions may be joined in a single suit," *Morrison*, 561 U.S. at 269—

will already be accomplished. In practice, this approach resurrects the evil of the United States as "the Shangri-La of class-action litigation for lawyers representing those allegedly cheated in foreign securities markets." *Id.* at 270.

CONCLUSION

For the foregoing reasons, as well as those presented in the petition for writ of certiorari, the petition should be granted.

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Respectfully Submitted,

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