No. 18-8013

IN THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

TD AMERITRADE HOLDING CORPORATION, TD AMERITRADE, INC., and FREDRIC TOMCZYK,

Defendants-Petitioners,

v.

RODERICK FORD,
on behalf of himself and all similarly situated,

Plaintiff-Respondent.

On Appeal from an Order of the United States District Court for the District of Nebraska Granting Plaintiffs' Motion for Class Certification No. 8:14-cv-00396 (Hon. Joseph F. Bataillon)

BRIEF FOR THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF DEFENDANTS-PETITIONERS

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1, *Amicus Curiae* Securities Industry and Financial Markets Association certifies that it has no parent corporation, and no publicly held corporation owns ten percent or more of its stock.

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IDENTITY AND INTEREST OF *AMICUS CURIAE*[1]

The Securities Industry and Financial Markets Association ("SIFMA") is the leading trade association for broker-dealers, investment banks, and asset managers operating in the capital markets. On behalf of our industry's nearly one million employees, we advocate on legislation, regulation, and business policy affecting retail and institutional investors, equity and fixed income markets, and related products and services. SIFMA serves as an industry-coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. SIFMA also provides a forum for industry policy and professional development. SIFMA is the U.S. regional member of the Global Financial Markets Association. SIFMA regularly files *amicus curiae* briefs in cases such as this one that raise issues of vital concern to securities industry participants.

This case involves important issues concerning class certification in private securities actions, which are directly relevant to SIFMA's mission of promoting fair and efficient markets and a strong financial services industry. SIFMA filed an *amicus curiae* brief in the leading Circuit case governing the standards for class certification in the "best execution" context, *Newton v. Merrill Lynch, Pierce,*

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[1] Pursuant to Federal Rule of Appellate Procedure 29, undersigned counsel certify that: no party's counsel authored this brief in whole or in part; and no party or party's counsel, or any other person, other than *amici* or their counsel, contributed money that was intended to fund the preparation or submission of this brief.

Fenner & Smith, Inc. (*Newton II*), 259 F.3d 154 (3d Cir. 2001). SIFMA and its members have a substantial interest in the proper application of settled class certification law to the highly-individualized determinations required to analyze a best execution case under the federal securities laws.

SUMMARY OF ARGUMENT

The District Court departed from nearly twenty years of precedent in certifying a sprawling "best execution" class that contains hundreds of thousands of putative class members who engaged in hundreds of millions of securities trades over the course of several years. No court has ever certified a best execution case because the determination of whether any single investor suffered economic injury due to a broker-dealer's trade order routing practices necessarily turns upon highly individualized proof. Simply put, even if a plaintiff could show that one trade executed by a broker resulted in economic injury, that does not mean that the same plaintiff necessarily suffered economic injury on any other trade, let alone that *another plaintiff* suffered economic injury arising from the execution of an entirely different set of trades. Hundreds of thousands of mini-trials would be required to establish, on a trade-by-trade basis, whether each investor suffered economic injury on each individual trade.

It is well-recognized—including by Plaintiffs' own expert—that the determination of whether an order reasonably received the best price execution

requires consideration of all facts and circumstances, including market conditions, market liquidity, market disruptions, investor objectives, etc. Because of this, the Third Circuit in *Newton II*—the leading best execution case—denied class certification based on similar theories. Indeed, the District Court below previously denied class certification in a similar best execution case.

Recognizing the unbroken line of precedents, Plaintiffs here have attempted to sweep individualized issues of proof under the rug using an undisclosed and incomplete algorithm. Plaintiffs claim that their algorithm will identify harm on "an order-by-order basis" and that their expert will apply the algorithm at trial to every single class member. But an algorithm cannot *substitute* for common proof on the key question of economic loss, and as Petitioners amply demonstrate in their papers, even the incomplete algorithm about which Plaintiffs hypothesize plainly requires proof that is *not* common to the class. In granting class certification under these circumstances, the District Court disregarded the rigorous standards of Rule 23 and deviated from prior decisions which hold that allegations virtually identical to those Plaintiffs make here are not susceptible to class treatment.

This Court should therefore grant the petition to appeal and reverse the District Court's certification decision. Otherwise the District Court's erroneous decision may never face appellate scrutiny—and that decision will remain in conflict with

Newton II, creating incentives for forum shopping and upsetting the certainty of the regulatory regime on which SIFMA members rely in conducting their businesses.

ARGUMENT

I. The District Court's Class Certification Order Conflicts with *Newton II* and Rule 23's Requirements.

The Supreme Court has long made clear that "[t]he class action is an exception to the usual rule that litigation is conducted by and on behalf of the individual named parties only." *Wal-Mart Stores, Inc. v. Dukes*, 564 U.S. 338, 348 (2011) (internal quotation marks omitted). Thus, certification is not to be granted without a "rigorous analysis." *In re Initial Pub. Offerings Sec. Litig.*, 471 F.3d 24, 33 (2d Cir. 2006). The predominance requirement is "far more demanding" than Rule 23(a)'s commonality requirement. *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 624 (1997). When assessing a proposed class action, a court may not completely disregard those issues that affect only individual members, as the District Court impermissibly did here when it certified the class action based on an unfinished algorithm that Plaintiffs' expert will continue to buildout through trial. Whether the Plaintiffs suffered economic loss as a result of Defendants' purported breach of the duty of best execution requires proof regarding the highly individualized circumstances of each customer's specific trades, and therefore injury cannot be shown on a class-wide basis. The District Court erred in granting class certification under these circumstances.

A. The District Court Confused the *Existence* of Injury with the *Measure* of Damages.

The District Court observed that "[t]he presence of individualized damages issues does not defeat the predominance of questions common to the class." *Klein v. TD Ameritrade Holding Corp.*, 2018 U.S. Dist. LEXIS 157473, at *23–24 (D. Neb. Sept. 14, 2018) (citing cases). Within the cases it cited, however, the District Court relied on only those sections that discussed damages as separate from liability. Because liability involved only common questions, those courts held, the individualized inquiry into the *amount* of damages each plaintiff suffered did not predominate. *See, e.g., Menocal v. GEO Grp., Inc.*, 882 F.3d 905, 926-27 (10th Cir. 2018). Even the section of the treatise the District Court cited is titled "Recurring issues in the predominance analysis—*Individual damages vs. common liability.*" *See* 2 WILLIAM B. RUBENSTEIN, NEWBERG ON CLASS ACTIONS § 4:54 (5th ed. June 2018 update) (emphasis added).

In this case, the *existence* of injury (*i.e.*, economic loss)—an essential element of Plaintiffs' claim—is the obstacle for class certification, not the *measure* of damages. *See Newton II*, 259 F.3d at 188 ("Proof of injury (whether or not an injury occurred at all) must be distinguished from calculation of damages (which determines the actual value of the injury)."). It is fatal to the District Court's decision that proof of economic loss of a particular trade is by necessity an individualized inquiry. For example, the Second Circuit's decision in *McLaughlin v. American*

Tobacco Co., 522 F.3d 215, 228 (2d Cir. 2008), *abrogated on other grounds by Bridge v. Phx. Bond & Indem. Co.*, 553 U.S. 639 (2008), on which the District Court relied, held that class certification was unavailable as "plaintiffs cannot meet their burden of showing that injury is amenable to common proof." Further, the District Court did not cite to any authority in its erroneous application of predominance principles to the specific facts of this case. *See Klein*, 2018 U.S. Dist. LEXIS 157473, at *34-35. Instead, it departed from years of authority holding that the economic loss inquiry in best execution cases is not susceptible to common proof.

B. Economic Loss Cannot Be Shown with Common Evidence in Best Execution Cases.

It is has long been accepted that proving economic loss in a "best execution" case must proceed on an individualized basis. In *Newton II*, the Third Circuit explained that the individualized injury issue would predominate over the class issues and denied class certification in a best execution case. 259 F.3d at 187. To show that every member of the class suffered loss, a lead plaintiff would have to present "proof of the circumstances surrounding each trade, the available alternative prices, and the state of mind of each investor at the time the trade was requested," a "Herculean task, involving hundreds of millions of transactions." *Id.* Notably, the Third Circuit held that, "even if plaintiffs could present a viable formula for calculating damages (which they have not), defendants could still require individualized proof of economic loss." *Id.* at 188.

After *Newton II*, courts have uniformly refused to certify classes in best execution cases. *See, e.g.*, *Pearce v. UBS PaineWebber, Inc.*, 2004 U.S. Dist. LEXIS 30426, at *33–37 (D.S.C. Aug. 13, 2004). In fact, this District Court previously denied a motion for class certification in a best execution case on the basis that individual determination of injury would predominate over issues susceptible to common proof. *See Telco Grp., Inc. v. Ameritrade, Inc.*, 2007 U.S. Dist. LEXIS 6256 (D. Neb. Jan. 23, 2007) (Bataillon, J.), adopting 2006 U.S. Dist. LEXIS 83475 (D. Neb. Nov. 6, 2006) (report and recommendation), *aff'd on other grounds*, 552 F.3d 893 (8th Cir. 2009). The uniformity of these rulings in best execution cases is explained by the impediments to proving injury on a class-wide basis with common evidence.

Here, the District Court justified its departure from all prior best execution cases on the basis of Plaintiffs' algorithm, which their expert will continue to build until and possibly through trial. That algorithm, however, does not establish the common evidence necessary to satisfy Rule 23(b)(3)'s predominance requirement because it cannot determine loss on a class-wide basis. Rather, in the words of Plaintiffs' own expert, it will "identify harm on...an order-by-order basis," *i.e.*, an individualized inquiry. D.E. 229 at 104:21–25.[2] Plaintiffs' expert intends to run his

[2] Further illustrating the District Court's error in certifying a class and ignoring the individual issues at play is that an unknown number of the putative class, including the lead Plaintiff, benefitted from the non-execution of some orders,

algorithm at trial on every single class member's orders, and will require such varying inputs as to each class member and trade as liquidity (number of shares available at varying prices), market conditions, order price, order type, order time, order size, and market center availability. *See, e.g.*, D.E. 229 at 105:6–108:4. And no computer algorithm can account for an investor's state of mind and trading strategy, certain market conditions, or other subjective determinations. This is essentially a mass-joinder action, not litigation by a representative plaintiff with representative claims that can establish all elements of liability utilizing common proof.

II. Immediate Review of the Class Certification Decision Is Warranted.

The District Court's decision introduces unpredictability into an area of law that was settled almost two decades ago in *Newton II*. Securities law is "an area that demands certainty and predictability," *Pinter v. Dahl*, 486 U.S. 622, 652 (1988). A court's departure from well-settled jurisprudence is particularly troublesome in the best execution context, which affects the financial services industry. *See Newton II*, 259 F.3d at 177-88; *Telco Grp. Inc.*, 2007 U.S. Dist. LEXIS 6256; at *1; *Pearce*, 2004 U.S. Dist. LEXIS 30426, at *33–37.

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whose replacement orders were executed at better prices. *See Klein v. TD Ameritrade Holding Corp.*, 2018 U.S. Dist. LEXIS 157501, at *16 (D. Neb. July 12, 2018) (findings and recommendation).

The SEC and FINRA actively audit and review broker-dealer practices for best execution and permit the general practice Plaintiffs challenge here, namely, payment for order flow. Most significantly, FINRA has promulgated (and the SEC has adopted) FINRA Rule 5310, concerning "Best Execution and Interpositioning," which states, *inter alia*, that brokers must consider a wide variety of factors when seeking best execution, including:

> (A) the character of the market for the security (e.g., price, volatility, relative liquidity, and pressure on available communications);
>
> (B) the size and type of transaction;
>
> (C) the number of markets checked;
>
> (D) accessibility of the quotation; and
>
> (E) the terms and conditions of the order which result in the transaction, as communicated to the member and persons associated with the member.

See also Disclosure of Order Execution & Routing Practices, 65 Fed. Reg. 75,414 (Dec. 1, 2000) (issuing an SEC rule regarding best execution); FINRA Regulatory Notice 15-46 (providing guidance on best execution considerations). The regulators have made clear that whether the duty of best execution has been satisfied is not determined by price alone. *See, e.g.*, Disclosure of Order Execution & Routing Practices, 65 Fed. Reg. at 75420 ("[A] broker-dealer is required to seek to obtain the most favorable *terms* reasonably available under the circumstances for a transaction

(which may not in every case necessarily be the best price that might be available)."). By contrast, Plaintiffs' theory is that economic loss exists whenever an order does not achieve the best price that may have been available. This illustrates a reason why the District Court's conflation of the duty of best execution and harm is mistaken. *See Klein*, 2018 U.S. Dist. LEXIS 157473, at *30 ("The methodology of analysis proposed by the plaintiff [*i.e.*, for assessing harm] is the same method the defendant uses to route orders in the first place [*i.e.*, to fulfill its duty]."); *see also Newton II*, 259 F.3d at 180, 188 (distinguishing duty to seek best execution from injury).

Further, the SEC and FINRA actively police the securities market to enforce best execution duties. *See, e.g.*, Press Release, SEC, Credit Suisse Agrees to Pay $10 Million to Settle Charges Related to Handling of Retail Customer Orders (Sept. 28, 2018), https://www.sec.gov/news/press-release/2018-224 (censuring and fining a company for a best execution violation); FINRA, DISCIPLINARY AND OTHER FINRA ACTIONS 2 (May 2018),[3] (censuring and fining a company and ordering restitution for a best execution violation). Thus, if the District Court's decision stands, instead of being able to rely on clear regulatory guidance and industry standards, broker-dealers would be subject to a highly uncertain liability theory

[3]Available at https://www.finra.org/sites/default/files/publication_file/May_2018_Disciplinary_Actions.pdf.

governing best execution that would be impossible to apply within the context of unique, individualized transactions.

The open break made by the District Court with *Newton II* further supports granting the Rule 23(f) petition. The Eighth Circuit has expressed particular reluctance to disturb well-settled law, stating:

> [W]e adhere to the policy that a sister circuit's reasoned decision deserves great weight and precedential value. As an appellate court, we strive to maintain uniformity in the law among the circuits, wherever reasoned analysis will allow, thus avoiding unnecessary burdens on the Supreme Court docket.

Aldens, Inc. v. Miller, 610 F.2d 538, 541 (8th Cir. 1979). Given the importance of certainty in the securities market, this Court should grant the Rule 23(f) petition and reverse the decision below.

* * *

CONCLUSION

Petitioners' petition should be granted and the certification order reversed.

Dated: October 5, 2018

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I hereby certify that this brief complies with the typeface requirements of Federal Rule of Appellate Procedure 32(a)(5) and the type styles requirements of Federal Rule of Appellate Procedure 32(a)(6) because it has been prepared in 14-point Times New Roman, a proportionally spaced typeface.

I further certify that this brief complies with the type-volume limitation of Federal Rules of Appellate Procedure 5(c)(1) and 29(a)(5) because it contains 2,473 words, excluding parts of the brief exempted under Rule 32(f), according to the count of Microsoft Word.

Finally, I certify that this brief complies with the requirements of Eighth Circuit Local Rule 28A(h)(2) because it has been scanned for viruses and is virus-free.

Dated: October 5, 2018

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