21-243

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BLACKBERRY LIMITED FKA RESEARCH IN MOTION LIMITED, THORSTEN HEINS, BRIAN BIDULKA, AND STEVE ZIPPERSTEIN,

Petitioners,

v.

MARVIN PEARLSTEIN, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,

Respondent.

On Petition For Permission to Appeal from the
United States District Court for the Southern District of New York
(Case No. 1:13-cv-07060) (Chief Judge Colleen McMahon)

BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* SUPPORTING PETITIONERS

John M. Masslon II
Cory L. Andrews
WASHINGTON LEGAL FOUNDATION
2009 Massachusetts Ave., NW
Washington, DC 20036
(202) 588-0302
jmasslon@wlf.org

Counsel for Amicus Curiae
Washington Legal Foundation

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INTEREST OF *AMICUS CURIAE*[*]

Washington Legal Foundation is a nonprofit, public-interest law firm and policy center with supporters nationwide. WLF promotes free enterprise, individual rights, limited government, and the rule of law. It often appears as *amicus* in cases about the proper scope of federal securities laws. *See, e.g.*, *Goldman Sachs Grp., Inc. v. Ark. Teacher Retirement Sys.*, 2021 WL 398166 (U.S. brief filed Feb. 1, 2021); *China Agritech, Inc. v. Resh,* 138 S. Ct. 1800 (2018).

INTRODUCTION

Plaintiffs often rely on the inflation-maintenance theory. But unlike plaintiffs in a traditional inflation-maintenance case, Plaintiffs here contend that back-end statements revealed the falsity of front-end representations on the same subject. The District Court bought this argument. If left to stand, the District Court's ruling would make class certification a virtual certainty. The fraud-on-the-market presumption would be irrebuttable—flouting the Supreme Court's decision in

[*] No party's counsel authored any part of this brief. No one, apart from WLF and its counsel, contributed money intended to fund the brief's preparation or submission.

Halliburton Co. v. Erica P. John Fund, Inc. (*Halliburton II*), 573 U.S. 258 (2014).

This Court handles more securities cases than any other federal appellate court. *See* Cornerstone Research, *Securities Class Action Filings: 2019 Year in Review* 38 (Jan. 2020), https://bit.ly/3t8gWHz. This Court's securities opinions thus carry great weight. Given this Court's place in the securities landscape, it should grant the petition and decide this important issue now.

STATEMENT

Fifteen years ago, almost every attorney carried a BlackBerry. Much to firm associates' chagrin, the phones allowed 24/7 access to firm email. But then came the iPhone and Android devices. BlackBerry's market share soon shrank because its phones lacked the bells and whistles that younger consumers desired. In response, BlackBerry dropped its BBOS operating system and developed a new operating system—BB10.

This case arises from statements made around the release of the first BB10 devices. After the phones were released, Petitioners made several factually accurate statements. Petitioners later released truthful

information about BB10 device sales that occurred after their front-end statements. None of Petitioners' back-end statements revealed the falsity of front-end disclosures. Rather, all of Petitioners' statements were accurate.

Seeing dollar signs, Plaintiffs sued after BlackBerry's stock lost value. They argued that back-end statements "corrected" truthful front-end statements on the same subject. The District Court certified a class after holding that statements about the same subject can satisfy the "corrective" requirement of the inflation-maintenance theory. This Court should grant Petitioners permission to appeal the class-certification order.

ARGUMENT

I. THE DISTRICT COURT'S ORDER IMPERMISSIBLY MAKES THE FRAUD-ON-THE-MARKET PRESUMPTION IRREBUTTABLE.

Securities and Exchange Commission Rule 10b-5(b) prohibits "mak[ing] any untrue statement of a material fact" or omitting "a material fact necessary in order to make the statements made . . . not misleading." 17 C.F.R. § 240.10b-5(b). A private party may prevail on a Rule 10b-5 claim if it shows that it suffered an economic loss because it relied on a knowing, material misstatement or omission when purchasing

or selling a security. *See Dura Pharmaceuticals, Inc. v. Brou-do*, 544 U.S. 336, 341-42 (2005).

Statements that "have price impact not because they introduce inflation into a share price, but because they 'maintain' it" can trigger Rule 10b-5 liability. *Ark. Teacher Ret. Sys. v. Goldman Sachs Grp., Inc.*, 955 F.3d 254, 264 (2d Cir. 2020) (citation omitted), *cert. granted on other grounds sub nom. Goldman Sachs Grp. v. Ark. Teacher Ret. Sys.*, 2020 WL 7296815 (U.S. Dec. 11, 2020) (*per curiam*). To prevail on that theory, the plaintiff must show that the defendant's back-end statement revealed the falsity of a front-end statement. *See In re Vivendi, S.A. Sec. Litig.*, 838 F.3d 223, 255 (2d Cir. 2016). Without this requirement, any dip in stock price after any statement by a company may qualify as securities fraud. This violates both the letter and the spirit of *Halliburton II*. Yet that is what the District Court did here.

A. The Fraud-On-The-Market Presumption Is Rebuttable.

Plaintiffs' claims rely on the fraud-on-the-market presumption. This is "a rebuttable presumption of reliance on material misrepresentations aired to the general public." *Amgen Inc. v. Conn. Ret. Plans & Tr. Funds*, 568 U.S. 455, 461 (2013) (citing *Basic Inc. v. Levinson*,

485 U.S. 224, 241-49 (1988)); *see Erica P. John Fund, Inc. v. Halliburton Co.* (*Halliburton I*), 563 U.S. 804, 811 (2011). But many courts began treating the presumption as irrebuttable at the class-certification stage. So in *Halliburton II*, the Supreme Court granted certiorari to set the record straight.

The Court explained that "[t]he *Basic* presumption does not relieve plaintiffs of the burden of proving—before class certification—that [Rule 23's predominance] requirement is met." *Halliburton II*, 573 U.S. at 276. The burden always remains with the plaintiff—not the defendant. *See id.* The "plaintiff satisfies that burden by proving the prerequisites for invoking the presumption—namely, publicity, materiality, market efficiency, and market timing." *Id.* And, except for materiality, the requirements "must be satisfied before class certification." *Id.*

It "makes no sense" to allow defendants to rebut the *Basic* presumption only at the merits stage. *Halliburton II*, 573 U.S. at 280. As the Supreme Court has explained, "bizarre results" would follow. In short, the defendant could present strong evidence that a court would have to ignore. *See id.* So the Supreme Court held that "[d]efendants may seek to defeat the *Basic* presumption" before class certification. *Id.* at

283. The District Court's decision, however, effectively eliminates the right to rebut the presumption at the class-certification stage. This Court should intervene.

B. Allowing Any Statement On The Same Subject Matter To Be A Correction Makes Rebuttal Futile.

The District Court's order makes rebutting the *Basic* presumption futile. In granting Plaintiffs' class-certification motion, it held that statements merely touching on the same topic were "sufficiently related" to constitute corrective statements. Opinion at 38. This makes it impossible for the defendant to rebut the *Basic* presumption when competent counsel represents the plaintiff.

Combining the inflation-maintenance theory and the *Basic* presumption is a formidable litigation strategy. The path to victory is straightforward. The plaintiff looks for a drop in a stock's price. It then examines public statements by the company and its officers in the days before that price drop. After compiling those statements, the plaintiff looks at front-end statements that the company or officers made. Then all that is left is to pair back-end statements with front-end statements. Eliminating the defendant's right to rebut the *Basic* presumption is a step too far.

1. The District Court misunderstood the reliance requirement.

The District Court erroneously conflated the loss causation requirement with the reliance requirement. *See* Opinion at 30-31. In opposing Plaintiffs' class-certification motion, Petitioners argued that the back-end statements did not correct any front-end statements. But the District Court rejected this argument because "loss causation . . . need not be adjudicated before a class is certified." *Id.* (quoting *Amgen*, 568 U.S. at 475). This is a correct—but irrelevant—statement. *See Halliburton I*, 563 U.S. at 811-13.

As described above, there are six elements to a Rule 10b-5 claim. *See Stoneridge Inv. Partners, LLC v. Scientific-Atlanta*, 552 U.S. 148, 157 (2008) (citation omitted). The last of these elements is loss causation. To satisfy this requirement, a plaintiff must "demonstrate that the defendant's deceptive conduct caused their claimed economic loss." *Halliburton I*, 563 U.S. at 807. In other words, "loss causation is the causal connection between the material misrepresentation and the economic loss suffered by investors." *Id.* at 808 (cleaned up).

The loss causation requirement is distinct from the reliance element. As the Supreme Court explained, "the element of reliance in a

private Rule 10b-5 action [is] 'transaction causation,' not loss causation." *Halliburton I*, 563 U.S. at 812 (citation omitted); *see Basic*, 485 U.S. at 248-49. The difference is striking.

On the one hand, loss causation "requires a plaintiff to show that a misrepresentation that affected the integrity of the market price also caused a subsequent economic loss." *Halliburton I*, 563 U.S. at 812 (emphasis removed). Reliance, however, "focuse[s] on facts surrounding the investor's decision to engage in the transaction." *Id.* So loss causation focuses on whether a misstatement injured the plaintiff while transaction causation focuses on whether someone bought a security because of a misstatement or omission.

Whether a back-end statement corrected a front-end statement may implicate loss causation. But whether the back-end statement corrected a front-end statement also goes to transaction causation. If a back-end statement does not correct a front-end statement, then a plaintiff could not have mistakenly relied on that front-end statement when making the trade. So the District Court's analysis relied on a false dichotomy between loss causation and transaction causation.

The Supreme Court's decision in *Halliburton II* illustrates the point. There, the Court held that if "the plaintiff has carried its burden to prove market efficiency, but that the evidence shows no price impact with respect to the specific misrepresentation challenged in the suit" then class certification is improper. *Halliburton II*, 573 U.S. at 281. Such a plaintiff has failed to prove reliance. *See id.* The same rationale applies here.

Petitioners had every right to rebut the *Basic* presumption. This included the ability to show that the back-end statements did not correct any front-end statements. Such a showing would defeat the *Basic* presumption—just as disproving price impact would in the *Halliburton II* example.

The District Court missed this distinction. Rather than rely on the Supreme Court's decisions, the District Court extrapolated from a fellow district court's decision. Opinion at 31 (citation omitted). This Court should grant the petition to fix this error.

2. This misunderstanding allows plaintiffs' attorneys to manufacture a back-end correction.

Because of this conflation, the District Court's order allows for any competent attorney to plead around the reliance requirement at the class-certification stage. Public statements made by companies and their officers are limited in scope. They generally focus on the company's products, services, and financial health. Companies do not talk about a product once and then never mention it again. Nor do they discuss their accounting methodology a single time. Rather, complying with SEC rules, companies repeatedly discuss these issues.

This means that a back-end statement is almost always "related to" a front-end statement. Opinion at 33. If the plaintiffs' attorneys know that the back-end statement did not reveal the falsity of a front-end statement, they can still obtain class certification by connecting the back-end statement to a front-end statement on the same general subject. Once this happens, as detailed below, the plaintiffs' attorneys can book a first-class trip to Tahiti.

An example proves the point. Assume that today a mask manufacturer makes a front-end statement about how the COVID-19 pandemic has affected its demand for N95 masks. And then later—when

vaccines are ubiquitous—it makes a statement about how construction during the post-pandemic recovery is affecting demand for N95 masks. Around the same time as this back-end statement, the stock's price falls.

Under the District Court's rationale, this is enough to certify a class against the company under the inflation-maintenance theory. Both of the company's statements relate to the demand for N95 masks—just like some of BlackBerry's statements here related to BB10 device sales. The plaintiff could assert that the statements about the demand after the pandemic "corrected" the statements about demand during the pandemic. According to the District Court, this suffices to prove reliance and justifies class certification.

The absurdity of this line of reasoning is self-evident. The company neither made a misstatement nor issued a correction; it provided only truthful information to investors. Such truthful disclosures do not violate Rule 10b-5. Rather, such truthful disclosures are sometimes required by SEC rules.

Yet the District Court would prohibit the defendant from rebutting the *Basic* presumption and certify the class. So long as the statements relate to the same topic—the demand for N95 masks—the presumption

applies. Even if the defendant showed that both the front-end and back-end statements were true, and the back-end statement did not reveal the falsity of the front-end statement, the District Court would ignore that showing at the class-certification stage.

This makes the *Basic* presumption irrefutable. Any attempt by the defendant to rebut the presumption is futile. Creative plaintiffs' counsel will always be able to show that a back-end statement relates to a front-end statement.

This holding conflicts with *Halliburton II*'s assurance that the defendant may rebut the *Basic* presumption at the class-certification stage. The District Court thus erred by certifying the class. As shown by the District Court extrapolating from another district court's opinion, this error will continue to proliferate without this Court's intervention.

II. SETTLEMENT PRESSURE WILL PREVENT THIS COURT FROM REVIEWING THIS IMPORTANT ISSUE AFTER A FINAL JUDGMENT.

Generally, this Court has jurisdiction over only final orders. *See Hegna v. 650 Fifth Ave. Co.*, 673 F. App'x 54, 56 (2d Cir. 2016) (*per curiam*) (citation omitted). But under 28 U.S.C. § 1292(e) and Federal Rule of Civil Procedure 23(f), this Court can hear appeals from class-

certification orders. Allowing appeals from class-certification orders in cases like this one is critical to the proper development of securities law.

Class certification is "the whole shooting match." David L. Wallace, *A Litigator's Guide to the 'Siren Song' of 'Consumer Law' Class Actions*, LJN's Prod. Liab. L. & Strategy 10 (Feb. 2009). "With vanishingly rare exception, class certification sets the litigation on a path toward resolution by way of settlement, not full-fledged testing of the plaintiffs' case by trial." Richard A. Nagareda, *Class Certification in the Age of Aggregate Proof*, 84 N.Y.U. L. Rev. 97, 99 (2009).

As the Supreme Court has recognized, "extensive discovery and the potential for uncertainty and disruption in a lawsuit allow plaintiffs with weak claims to extort settlements from innocent companies." *Stoneridge*, 552 U.S. at 163 (citing *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 740-41 (1975)). This pressure is even heavier in securities class actions.

Class "certification substantially increases the settlement value of a securities suit." *Schleicher v. Wendt*, 618 F.3d 679, 682-83 (7th Cir. 2010). The result is that "settlements in large class actions can be divorced from the parties' underlying legal positions." *Hevesi v. Citigroup*

Inc., 366 F.3d 70, 80 (2d Cir. 2004) (citation omitted). That is why "very few securities class actions are litigated to conclusion." *West v. Prudential Sec., Inc.*, 282 F.3d 935, 937 (7th Cir. 2002). Settlement pressure is simply too high.

So it's no surprise that both this Court and other courts of appeals often grant Rule 23(f) petitions in securities cases. *See Hevesi*, 366 F.3d at 80 (the "decision to apply the *Basic* presumption at the certification stage is likely to escape effective review after entry of final judgment" (quotation omitted)); *West*, 282 F.3d at 937 ("review of this novel and important legal issue [about the *Basic* presumption] may be possible only through the Rule 23(f) device").

Not resolving this case would have a domino effect of encouraging weak claims based on non-corrective statements. This would harm the wider economy, particularly less-capitalized businesses. They can least afford to gamble when faced with a securities class action. So they would likely settle the claims for far more than what they are worth.

The plaintiffs' bar will quickly latch on to the District Court's decision and begin reverse engineering securities class actions based on statements about the same subject in hopes of hitting pay dirt. The best

way to avoid this potential harm is to grant the petition and decide whether the District Court properly certified this class. This Court should take that step and protect our economy.

CONCLUSION

This Court should grant the petition.

Respectfully submitted,

/s/ John M. Masslon II
John M. Masslon II
Cory L. Andrews
WASHINGTON LEGAL FOUNDATION
2009 Massachusetts Ave. NW
Washington, DC 20036
(202) 588-0302
jmasslon@wlf.org

Counsel for Amicus Curiae
Washington Legal Foundation

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CERTIFICATE OF COMPLIANCE

I hereby certify that this brief contains 2,598 words, excluding the parts exempted by Federal Rule of Appellate Procedure 32(f)—less than one-half the length permitted for a Rule 23(f) petition. *See* Fed. R. App. P. 5(c)(1); *cf.* Second Circuit Rule 29.1(c) (permitting *amicus* briefs to be one-half the length of the party's brief).

I also certify that this brief complies with the typeface and type-style requirements of Federal Rules of Appellate Procedure 32(a)(5) and (6) because it uses 14-point Century Schoolbook font.

/s/ John M. Masslon II
JOHN M. MASSLON II
Counsel for Amicus Curiae
Washington Legal Foundation

February 10, 2021