LINK:

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

CIVIL MINUTES – GENERAL

Case No.	**CV 11-02559 BRO (PLAx)**	Date	August 4, 2014
Title	**LARRY BROWN, ET AL. v. CHINA INTEGRATED ENERGY INC., ET AL.**		

Present: The Honorable	**BEVERLY REID O'CONNELL, United States District Judge**	
Renee A. Fisher	Not Present	N/A
Deputy Clerk	Court Reporter	Tape No.
Attorneys Present for Plaintiffs:	Attorneys Present for Defendants:	
Not Present	Not Present	

Proceedings: (IN CHAMBERS)

ORDER DENYING PLAINTIFFS' MOTION FOR CLASS CERTIFICATION [183]; AND GRANTING DEFENDANTS' MOTION TO EXCLUDE EXPERT DECLARATIONS [226]

Pending before the Court are two motions: (1) Plaintiffs' motion for class certification, (Dkt. No. 183); and (2) Defendants' motion to exclude the declarations and expert testimony of Michael A. Marek and Kenneth W. McGraw, (Dkt. No. 226). The Court held a hearing on these matters on June 23, 2014, where it heard testimony from Marek, McGraw, and Defendants' expert, Dr. Andrew Roper. After considering the parties' papers, the deposition and hearing testimonies, and the expert declarations, the Court finds that Marek and McGraw's declarations should be excluded. The Court reaches this conclusion having determined that McGraw is not qualified to testify and Marek's methodology is unreliable. As a result, Plaintiffs are unable to prove reliance on behalf of the putative class as a whole, and therefore they are cannot show that common issues do not predominate over individual ones. Class certification is therefore improper at this time. Accordingly, Defendants' motion is GRANTED and Plaintiffs' motion is DENIED without prejudice.

I. BACKGROUND

A. Factual History

This is a putative securities fraud class action brought under the Securities Act of 1933 and the Securities Exchange Act of 1934 as amended by the Private Securities Litigation Reform Act of 1995 ("PSLRA"). Plaintiffs assert claims against China

Integrated Energy Corporation ("China Integrated Energy"), some of its officers and directors, and its independent auditor, accounting firm Sherb & Co. (*See* Consolidated Class Action Complaint ("Compl.") ¶¶ 28–41.) Collectively, these individuals and entities are referred to as "Defendants."

Plaintiffs seek to represent a class of individuals who purchased or otherwise acquired common stock in China Integrated Energy between March 31, 2010, and April 21, 2011. (Pls.' Mot. 1 (Dkt. No. 183); Compl. ¶ 52.) China Integrated Energy is a Delaware corporation operating in the People's Republic of China. (Compl. ¶ 2.) It purports to sell finished oil products, heavy oil products, and biodiesel fuel. (Compl. ¶ 2.) It also operates retail gas stations. (Compl. ¶ 2.)

According to Plaintiffs, the class period began on March 31, 2010, when China Integrated Energy issued its 2009 financial results. (Compl. ¶ 52.) They allege that the report was materially false and misleading because it overstated China Integrated Energy's 2009 revenue and net income. (Compl. ¶ 55.) Plaintiffs also assert that Defendants prepared two sets of financial statements: one presumably accurate set that Defendants filed with Chinese regulators, and another false and misleading set that they filed with the Securities and Exchange Commission ("SEC"). (*See* Compl. ¶¶ 55–59.)

The discrepancy between the financial statements filed in China and those filed with the SEC came to light on March 16, 2011. (*See* Compl. ¶¶ 58, 130.) On that day, Sinclair Upton Research published a report alleging that China Integrated Energy's SEC filings overstated revenues as compared with revenues reported in the Chinese filings. (Compl. ¶¶ 58, 130.) The report also asserted that China Integrated Energy had been funneling money to corporations owned by the son of Defendant Xincheng Gao. (Compl. ¶ 130.) In response to this report, China Integrated Energy's share price fell from $5.95 to a closing price of $5.00, nearly a 16% drop. (Compl. ¶ 130.)

The next day, analysts at Roth Capital Partners downgraded China Integrated Energy's shares from a "BUY" status to a "NEUTRAL" status. (Compl. ¶ 132.) They also reported that they had independently obtained the Chinese filings referenced in Sinclair Upton Research's report, and confirmed the prior report's accuracy. (Compl. ¶¶ 58, 132.) China Integrated Energy's share price fell again, from $5.00 to $3.52, a 24.6% drop. (Compl. ¶ 133.)

A week later, on March 23, 2011, China Integrated Energy issued a letter to shareholders, apparently in an attempt to rebut the reports' allegations. (Compl. ¶ 134.) It vigorously denied it had made any misstatements in its financial statements and SEC filings, and denied all other accusations in the Sinclair Upton Research report. (Compl. ¶¶ 134–38.) Notwithstanding this rebuttal attempt, China Integrated Energy's share prices continued to fall. (*See* Compl. ¶ 140.)

On March 28, 2011, additional damaging information surfaced when another analyst firm, Alfred Little, issued a detailed report reviewing China Integrated Energy's Chinese filings and audited financial statements and calling the company a "complete hoax." (Compl. ¶ 141.) This report caused a 29% drop in share price, from $3.76 to $2.66 on March 28, 2011. (Compl. ¶ 143.)

In response to the accusations and resultant drop in share price, China Integrated Energy hired law firms and auditors to conduct an internal investigation. (*See* Compl. ¶ 151.) Ultimately, these firms and auditors resigned, citing management's refusal to cooperate in the investigation. (*See* Compl. ¶¶ 152–55.) On April 26, 2011, the company's outside auditor, KPMG, resigned and cautioned investors that the SEC filings it assisted in preparing should no longer be relied upon. (Compl. ¶¶ 156–57.)

On April 20, 2011, NASDAQ halted trading in China Integrated Energy's shares. (Compl. ¶ 145.) On November 21, 2011, NASDAQ decided to remove the company's shares from listing. (Compl. ¶ 150.)

B. Procedural History

Between March 25, 2011, and May 25, 2011, various plaintiffs filed five separate lawsuits, which were ultimately consolidated into one. (*See* Dkt. Nos. 43–44.) On December 20, 2011, these plaintiffs filed a consolidated class action complaint. (Dkt. No. 59.) In their consolidated complaint, Plaintiffs allege four causes of action: (1) violations of Section 10(b) of the Securities Exchange Act of 1934 and related Rule 10b-5, (Compl. ¶¶ 176–84); (2) violations of Section 20(a) of the Securities Exchange Act of 1934 (against company officers only), (Compl. ¶¶ 185–198); (3) violations of Section 11 of the Securities Act of 1933, (Compl. ¶¶ 199–209); and (4) violations of Section 15 of the Securities Act of 1933 (against company officers only), (Compl. ¶¶ 210–213).

On August 15, 2013, Plaintiffs filed the instant motion to certify their putative class, naming Puerto Rico Teachers Retirement System and Bristol Investment Fund Ltd. as the lead plaintiffs. (Dkt. No. 183.) In support of their motion, Plaintiffs proffer the expert declaration of Michael Marek, (Dkt. No. 185-3), and Kenneth McGraw, (Dkt. No. 205). On April 14, 2014, Defendants filed the instant motion to exclude the declarations of Marek and McGraw. (Dkt. No. 226.)

II. LEGAL STANDARD

A. Motion to Strike Expert Report

Rule 702 of the Federal Rules of Evidence governs admissibility of expert testimony in federal courts. It provides,

> A witness who is qualified as an expert by knowledge, skill, experience, training, or education may testify in the form of an opinion or otherwise if:
>
> (a) the expert's scientific, technical, or other specialized knowledge will help the trier of fact to understand the evidence or determine a fact in issue;
> (b) the testimony is based on sufficient facts or data;
> (c) the testimony is the product of reliable principles and methods; and
> (d) the expert has reliably applied the principles and methods to the facts of the case.

Fed. R. Evid. 702 (West 2011). The key inquiry in evaluating expert testimony centers on reliability. *See Daubert v. Merrell Dow Pharm. Inc.*, 509 U.S. 579, 590 (1993). As the Ninth Circuit recently reiterated, "We are concerned not with the correctness of the expert's conclusions but the soundness of his methodology." *Estate of Barabin v. AstenJohnson Inc.*, 740 F.3d 457, 463 (9th Cir. 2014) (internal quotation marks and alterations omitted). Thus, it is incumbent upon a district court to "act as a gatekeeper to exclude junk science that does not meet Federal Rule of Evidence 702's reliability standards." *Ellis v. Costco Wholesale Corp.*, 657 F.3d 970, 982 (9th Cir. 2011) (internal quotation marks omitted). These same standards apply to all expert testimony, not just scientific testimony. *Kumho Tire Company, Ltd. v. Carmichael*, 526 U.S. 137 (1999).

Importantly, the Rule 702 inquiry is flexible, and courts may exercise significant discretion. *Daubert*, 509 U.S. at 594; *City of Pomona v. SQM N. Am. Corp.*, 750 F.3d 1036, 1044 (9th Cir. 2014).

Finally, a proponent of expert testimony has the burden of proving that the proposed expert testimony is admissible under Rule 702, *Daubert* and its progeny. *Lust ex rel. Lust v. Merrell Dow Pharm., Inc.*, 89 F.3d 594, 598 (9th Cir. 1996).

B. Motion for Class Certification

A Rule 23 class action is "an exception to the usual rule that litigation is conducted by and on behalf of the individual named parties only." *Califano v. Yamasaki*, 442 U.S. 682, 700–01 (1979). Certification is the process by which a named party may begin representing a class of individuals who are not named and do not otherwise participate in the litigation. Pursuant to Rule 23, a class may be certified only if four requirements are satisfied: (1) the class is so numerous that joinder would be impracticable—numerosity; (2) there are questions of law or fact that are common to the class as a whole—commonality; (3) the representative parties have claims or defenses typical of those of the class—typicality; and (4) the representative parties will fairly and adequately protect the class's interests—adequacy. Fed. R. Civ. P. 23(a). Additionally, a class may be certified only if one of Rule 23(b)'s requirements is met.

The party seeking class certification bears the burden of establishing the requirements of Rules 23(a) and 23(b). *See Wal-Mart Stores Inc. v. Dukes*, 131 S. Ct. 2541, 2551 (2011) ("A party seeking class certification must affirmatively demonstrate his compliance with [] Rule [23]."). When ruling on a motion for certification, a court generally must accept as true the allegations in the complaint, especially when "the issues are plain enough from the pleadings to determine whether the interests of the absent parties are fairly encompassed within the named plaintiff's claim." *Gen. Tel. Co. of Sw. v. Falcon*, 457 U.S. 147, 160 (1982). Nevertheless, "sometimes it may be necessary for the court to probe behind the pleadings" when considering certification. *Id.* A court's analysis should be rigorous and may "entail some overlap with the merits of the plaintiff's underlying claim." *Dukes*, 131 S. Ct. at 2551.

III. DISCUSSION

In support of their motion for class certification, Plaintiffs proffer the declarations of Michael Marek and Kenneth McGraw. (Dkt. Nos. 185-3, 205.) They rely on Marek and McGraw as expert witnesses to testify that China Integrated Energy's stock was traded in an efficient market. Demonstrating market efficiency is crucial to Plaintiffs' motion. This is because Plaintiffs must prove reliance; that is, they must prove that they relied on Defendants' misrepresentations in purchasing China Integrated Energy's securities. Proof of reliance ensures an adequate connection between Defendants' wrongful conduct (the misrepresentations) and Plaintiffs' resultant injury (buying shares worth less than they were priced). *Erica P. John Fund Inc. v. Halliburton Co.*, 131 S. Ct. 2179, 2184 (2011) (*Halliburton I*). But proving direct reliance on misrepresentations is somewhat difficult. A plaintiff establishes direct reliance by showing that it was aware of the defendant's statement and thereafter engaged in a relevant transaction, such as purchasing stock. *Id.* at 2185. Even more difficult (if not entirely impossible) would be proving direct reliance individually for each member of a putative class. *See Halliburton I*, 131 S. Ct. at 2185; *Basic Inc. v. Levinson*, 485 U.S. 224, 245 (1988). And even were it feasible to prove direct reliance individually for each member of the class, class certification would be improper under Rule 23(b)(3) because individual issues would predominate over common ones. *See Amgen Inc. v. Conn. Retirement Plans and Trust Funds*, 133 S. Ct. 1184, 1199 (2013).

Accordingly, Plaintiffs attempt to invoke a rebuttable presumption of reliance on behalf of the entire class as a whole, based on the "fraud-on-the-market" theory. "According to that theory, 'the market price of shares traded on well-developed markets reflects all publicly available information, and hence, any material misrepresentations.'" *Halliburton I*, 131 S. Ct. at 2185 (quoting *Basic*, 485 U.S. at 245). As such, the theory presumes that, by trading based on share price, an investor necessarily relies on any misrepresentations inherently incorporated into it. But the "fraud-on-the-market" theory applies only to the extent that the shares were traded in an efficient market. *Id.* Thus, demonstrating market efficiency is in essence a lynchpin to Plaintiffs' motion for class certification: market efficiency is essential to "fraud-on-the-market"; "fraud-on-the-market" is essential to demonstrating reliance on behalf of the class as a whole; demonstrating reliance on behalf of the class as a whole is necessary to show that individual issues do not predominate over common ones, as required by Rule 23(b)(3).

See Halliburton Co. v. Erica P. John Fund, Inc., 134 S. Ct. 2398, 2412 (2014) (*Halliburton II*) (reiterating that a plaintiff must prove "the prerequisites for invoking the [*Basic*] presumption—namely, publicity, materiality, market efficiency, and market timing . . . before class certification"). Accordingly, Plaintiffs must demonstrate market efficiency to prevail upon their motion.

Given the importance of their testimony to Plaintiffs' motion for class certification, the Court will first discuss Defendants' motion to exclude Marek and McGraw as expert witnesses. The Court will then consider Plaintiffs' motion for class certification.

A. Defendants' Motion to Exclude Declarations and Expert Testimony of Michael Marek and Kenneth McGraw

Defendants contend that the Court should exclude the declarations and testimony of Marek and McGraw for three reasons: (1) they are not qualified to offer an opinion on market efficiency; (2) they have not based their opinions on sound scientific principles and deviate from the methodologies and principles set forth in their declarations; and, (3) they base their opinions on factors that are not dispositive of market efficiency. (Defs.' Mot. 2.) The Court will separately discuss the first and second arguments.

1. Marek is Qualified to Offer His Opinion; McGraw is Not

Federal Rule of Evidence 702 prescribes the requirements for testimony by expert witnesses. The rule "contemplates a broad conception of expert qualifications." *Thomas v. Newton Int'l Enters.*, 42 F.3d 1266, 1269 (9th Cir. 1994). It permits an expert to be qualified by "knowledge, skill, experience, training, or education." Fed. R. Evid. 702. "Moreover, the advisory committee notes emphasize that Rule 702 is broadly phrased and intended to embrace more than a narrow definition of qualified expert." *Thomas*, 42 F.3d at 1269.

In his declaration, deposition testimony, and at the hearing on this matter, Marek described his qualifications. He received a bachelor's of science degree in economics from Wharton School of Finance at University of Pennsylvania. (Marek Decl. Ex. A.) He has achieved the professional designation of Chartered Financial Analyst ("CFA"), a widely recognized standard for measuring the competence of financial analysts, and is a

member in good standing of the CFA Institute. (*Id.*) Moreover, he has worked in the financial industry for nearly thirty years and has rendered expert opinions in a number of securities class actions, at least four of which specifically addressed the subject of market efficiency. (*Id.* ¶ 5, Ex. A; Pls.' Opp'n 10–11; *see* Buckley Decl. Ex. A ("Marek Depo.") 25:3–26:5.) Given his long career in finance and his experience in determining market efficiency specifically, Plaintiffs have demonstrated Marek has the necessary expertise to opine in this case.

Nevertheless, Defendants attempt to malign Marek's qualifications. They point out that he has no graduate degree. (Defs.' Mot. 3.) They also contend that he has never taught, or written any books, articles, or papers on any financial topic, and specifically on market efficiency. (*Id.*) Yet Defendants fail to explain why graduate-level education or scholastic authorship is necessary to provide an expert opinion on market efficiency.

Defendants also point to *IBEW Local 90 Pension Fund v. Deutsche Bank AG*, No. 11 Civ. 4209(KBF), 2013 WL 5815472 (S.D.N.Y. 2013), in support of their motion to exclude Marek. In that case, the Southern District of New York found Marek to be unqualified and his opinion to be unreliable. *Id.* at *15–16. In so finding, the court relied upon facts that are not on the record before this Court. For example, the court mentioned that Marek worked for Princeton Venture Research where he worked "behind the scenes drafting declarations signed by John Torkelson in various securities class action cases." *Id.* at *2, 14. Evidently, Torkelson was later indicted for submitting false declarations. *Id.* at *2, 14. It is true Marek testified at the hearing that at times he worked under Mr. Torkelson, but Defendants never established that Market "draft[ed] declarations signed by" Mr. Torkelson. (*See* Hr'g Tr. 47:13–48:12.) Certainly, the Court may take judicial notice of decisions in other cases. *Smith v. Ortiz*, 234 Fed. App'x 698 (9th Cir. 2007). But the Court may not take judicial notice and thereby rely on factual findings in other cases. *Wyatt v. Terhune*, 315 F.3d 1108, 1114 (9th Cir. 2003) ("taking judicial notice of findings of fact from another case exceeds the limits of [Federal Rule of Evidence] 201"), *overruled on other grounds by Albino v. Baca*, 747 F.3d 1162, 1166 (9th Cir. 2014) (en banc); *see also Lee v. City of Los Angeles*, 250 F.3d 668, 690 (9th Cir. 2001) (explaining that "when a court takes judicial notice of another court's opinion, it may do so 'not for the truth of the facts recited therein, but for the existence of the opinion'"); *M/V Am. Queen v. San Diego Marine Constr. Corp.*, 708 F.2d 1483, 1491 (9th Cir. 1983) ("As a general rule, a court may not take judicial notice of proceedings or records in another

cause so as to supply, without formal introduction of evidence, facts essential to support a contention in a cause then before it."). As such, compelling as *IBEW Local Pension Fund*'s factual findings may be, the Court may not consider them in determining whether Marek is qualified to opine in this matter.

Therefore, Plaintiffs have satisfied their burden in demonstrating that Marek is qualified to provide his expert opinion in this case.

As for McGraw, however, the Court is not persuaded that he is qualified to testify as an expert witness. McGraw received a bachelor's of arts degree in chemistry and a master's degree in philosophy and literature from Johns Hopkins University. (McGraw Decl. App'x A.) Later, he received a master's of business administration in finance from Harvard University. (*Id.*) He has worked in finance for over thirty years and has testified as an expert witness in more than 80 cases. (*Id.* App'x B.) These are impressive credentials. But an MBA and significant experience as an expert witness in the past is insufficient to qualify as an expert witness now. McGraw must have expertise in the matters on which he will opine in this case—specifically, market efficiency.

Yet only once before has McGraw submitted expert testimony based on an event study, which is the method he uses in this case to evaluate market efficiency. (McGraw Decl. App'x B.) And in that instance, Mr. Marek played a significant role in preparing the expert report. (Hr'g Tr. 67:17–23; Buckley Decl. Ex. B ("McGraw Depo."), at 213:19–214:13, 220:6–222:9.) Even here, in this case, McGraw delegated significant responsibility to Ms. Jones. She performed the regression analysis using a computer spreadsheet, which McGraw has never done before—the heart of the analysis. (McGraw Depo. 69:7–71:10.) She also prepared sections of McGraw's report. (McGraw Dep. 61:20–25.)

Moreover, his deposition and hearing testimony leaves the Court unconvinced that he has any expertise in the area. For example, when defense counsel asked McGraw what he had told plaintiff counsel "about [his] experience on the issue of market efficiency," McGraw responded, "[I] [t]old them that I had testified in the case in Chicago and that I had some knowledge of the matter and that I thought that I could be of assistance to them." (McGraw Depo. 29:22–30:4.) "Some knowledge" in market efficiency does not strike the Court as expertise. Defense counsel followed up, "Had you

ever worked on any other cases on the issue of market efficiency, other than the [Chicago] case?" (*Id.* at 30:14–17.) McGraw answered that his firm "had had other engagements involving market efficiency, and [that he] had peripheral contact on those assignments." (*Id.* at 30:18–21.) He continued, "So I had familiarity, but I didn't represent to him that I had any other experience in connection with market efficiency." (*Id*. at 30:21–24.) Again, "peripheral contact" and mere "familiarity" is not the expertise required in an expert witness. Defense counsel inquired, "When you say you were peripherally involved . . . on the issue of market efficiency, what do you mean? What was the nature of your peripheral involvement in those matters?" (*Id.* at 30:25–31:5.) McGraw's response is entirely underwhelming: "CFC is a—a small firm, and when we have assignments . . . it's quite common for us to discuss the assignments, and that's the extent of my involvement." (*Id.* at 31:6–11.) Defense counsel then asked, "What [was] the nature of your contributions to the other assignments on the issue of market efficiency at CFC?" (*Id.* at 31:14–16.) McGraw answered, "I don't recall specifically. I frequently have opinions and offer them." (*Id.* at 31:17–20.) Round table discussions about other people's assignments where McGraw offered his opinions on the issue of market efficiency is not the kind of experience necessary to qualify as an expert in the area of market efficiency. If this is "the extent of [McGraw's] involvement," the Court is unconvinced that he is qualified to opine in this case on the issue of market efficiency. His hearing testimony confirmed his limited involvement in market efficiency. (Hr'g Tr. 68:9–69:3.)

McGraw's experience is thin, and the one time he did prepare a report on market efficiency, he received help from Marek. Here, Ms. Jones, performed the regression analysis on the computer spreadsheet—the crux of the event study analysis. On this basis alone, the Court finds that McGraw is not qualified to testify as an expert, and therefore excludes McGraw's declaration and testimony. As such, Defendants' motion is GRANTED with respect to McGraw.

2. Marek's Methodology is Flawed

In his declaration, Marek opines that China Integrated Energy's shares traded in an efficient market. (*See* Marek Decl. ¶ 2.) In reaching this conclusion, he considered the five factors discussed in *Cammer v. Bloom*, 711 F. Supp. 1264, 1286–87 (D.N.J. 1989). (Marek Decl. ¶ 21.) The most important factor discussed in *Cammer* is the fifth one:

whether there is "a cause and effect relationship between unexpected corporate events or financial releases and an immediate response in the stock price." *See Cammer*, 711 F. Supp. at 1287. To evaluate this factor, Marek performed an event study. (Marek Decl. ¶¶ 53–69.) As he explains, "Event studies involve the examination of stock price behavior following announcements of relevant events." (Marek Decl. ¶ 55.) If the stock price changes immediately following the unexpected announcement, and the change is statistically significant—that is, greater than would be expected absent the announcement—then one might be able to conclude that the announcement caused the change in stock price. (*Id.*)

Defendants contend that Marek's event study is methodologically flawed. To support their contention, Defendants provide the expert declaration of Andrew Roper, Ph.D. (Dkt. No. 226-6.) Roper is vice-president of a financial and economic consulting firm and a lecturer at Stanford University Law School. (Roper Decl. 1.) At Stanford, he teaches a course on fraud-on-the-market theory, market efficiency, and application of economic analyses, including event studies, to assess economic and legal questions arising within securities class actions. (*Id.*) Prior to joining his consulting firm, Roper was a professor of finance at the School of Business at University of Wisconsin—Madison. (*Id.*) There, he taught courses on financial economics, which included securities markets, market efficiency, investment strategy, and the application of reliable economic analyses in empirical finance. (*Id.*) He holds a master's degree in economics from University of California, Davis, and a Ph.D. in finance from Duke University. (*Id.*) Throughout his career, Roper has published articles in leading peer-reviewed journals on economic and financial topics. (*Id.*) His articles have involved economic analysis, including event studies. (*Id.*) From his background and experience, it is evident to the Court that Roper is well qualified to opine on event studies, market efficiency, and the proper methods for conducting an event study.

Together with Roper, Defendants identify three flaws in Marek's event study : (1) the selection of events (releases of unexpected information) is entirely subjective; (2) Marek failed to utilize a prespecified threshold or known rejection rate; and, (3) Marek failed to address contradictory evidence. (Defs.' Mot. 12–18; Roper Decl. 36–64.) After reviewing the declarations of Roper and Marek, their respective deposition testimony and their testimony at the hearing in this matter, the Court agrees with Defendants and need only discuss the first flaw—subjectivity.

a. Subjectivity in their Studies

Roper explains that a reliable event study must begin by objectively identifying events that will later be examined. (Roper Decl. 27–28.) A researcher must define certain protocol for identifying what qualifies as an event. (*Id.*) "Absent a predefined protocol, the researcher's identification of [events] becomes ad hoc and risks introducing subjective bias into what should be an objective analysis." (*Id.*) Yet Marek never articulates any objective criteria that he used to identify the events used in his study. In his declaration and hearing testimony, Marek explained, "I preliminarily identified a total of 17 days associated with Company-specific disclosures or other Company-specific relevance (for example, financial press releases, business updates and the analyst coverage beginning on March 16, 2011 regarding the fraud alleged in this matter)." (Marek Decl. ¶ 61.) He never indicates what criteria he used to identify event days (though his deposition and hearing testimony confirms they were subjective). And although Marek insisted at the hearing on this matter that his "criteria for events [were] specifically set out as a hypothesis in [his] report, paragraph 61 and 62," (Hr'g Tr. 11:9–10), the Court can find no such criteria. The closest he comes is explaining that he included information for which he had no reason to believe "was of the import necessary to change the price of China Integrated common stock by a statistically significant amount," just to be conservative. (Marek. Decl. ¶ 62.) But whether information is "of the import necessary to change the price of" stock is not objective. This is evident, as McGraw used similarly subjective criteria, yet ended up selecting a very different group of event dates, as noted below.

In the Court's view, Marek's subjective determination of which events to examine in his event study renders unreliable his analysis and conclusion. The Court is mindful that designing an event study inevitably requires some subjectivity. *See In re Diamond Foods Inc. Sec. Litig.*, 295 F.R.D. 240, 249 (N.D. Cal. 2013). But the researcher must take steps to minimize that inevitable subjectivity. *See id.* And the Court does not see where Marek has taken such steps.

For example, Marek decided not to include in his study three particular articles. One of those was a December 1, 2010 article by Ben Axler. The Ben Axler article alleged that China Integrated Energy was misrepresenting itself to investors—information a reasonable investor might like to know. (*See* Marek Depo. 297:18–21.)

Although Marek did not include this article as an event in his study, he did include a December 3, 2010 press release by China Integrated Energy, which included what appears to be a rebuttal to Ben Axler's allegations. (*Id.* 294:4–302:15.) Marek never could satisfactorily explain why he decided to include in his study the December 3, 2010 rebuttal press release but not the December 1, 2010 article. (*See id.*) He testified that he "considered [the December 1, 2010 article] might be [relevant and material to investors]," yet he ultimately did not include it. (*Id.* at 301:14–15.) He conceded that he would not have objected if someone else included the article in an event study. (*Id.* at 301:18–19, 302:13–15.)

More concerning to the Court is Marek's description of how he determines the materiality of a particular news item or press release. In essence, he admits that when assessing materiality he looks to the market's reaction to the information. (*See* Marek Depo. 248:4–15, 264:2–14.) In other words, it appears that Marek does not use objective criteria to determine what kind of information should be included as an event in his study. Instead, he looks to see how the market reacted to it—whether the share price jumped or dropped after the information was released. (*See* Marek Depot 248:4–15, 264:2–14.) In Roper's view, this subjective approach is inconsistent with commonly accepted practice. (Roper Decl. ¶¶ 43–47, 75.) In the Court's view, it compromises the reliability of Marek's methodology and conclusion.

Notably, Marek and McGraw's entirely subjective approach to selecting events to include in their studies resulted in significantly differing lists of events. Marek's list included a total of 17 events. (*See* Marek Decl. 29.) McGraw's list included only 12 events. (McGraw Decl. 11.) And not all 12 of McGraw's events appear on Marek's list. (*Compare* Marek Decl. 29 *with* McGraw Decl. 11.) In total, Marek's list has 7 events not included on McGraw's list, and McGraw has 2 events not included on Marek's list. (*Compare* Marek Decl. 29 *with* McGraw Decl. 11.) This high level of discrepancy further evidences the subjectivity Marek employed in designing his event study.

The Court is mindful that Marek testified at the hearing that his subjectivity did not affect the conclusion of his study. In an attempt to justify his exclusion of certain articles from his event study, Marek testified that his conclusion would remain the same even if he had included those articles. (Hr'g Tr. 28:5–29:4.) But the Court is not concerned with the correctness of Mr. Marek's conclusions; it is concerned with the soundness of his

methodology. *Estate of Barabin*, 740 F.3d at 463. Because Marek's methodology is inherently subjective, it is inconsistent with commonly accepted practice, and therefore unsound. (Roper Decl. ¶¶ 43–47, 75.)

Accordingly, because Marek did not follow commonly accepted methods in performing his event study, the Court finds that his declaration and testimony are unreliable and should be excluded. On this basis, Defendants' motion is GRANTED with respect to Marek as well.

B. Plaintiffs' Motion for Class Certification

In their motion, Plaintiffs seek to certify a class comprising

> all persons and entities, other than Defendants and their affiliates, who purchased or otherwise acquired the common stock of China Integrated [Energy] between March 31, 2010 through April 21, 2011 . . . , including persons or entities that purchased common stock pursuant and/or traceable to [China Integrated Energy's] Registration Statement, effective May 19, 2010, and the Prospectuses issued in connection with [its] Secondary Offerings on or about December 28, 2010 through January 7, 2011 . . . , and who were damaged thereby.

(Pls.' Mot. 1.) Defendants contend certification is improper for a number of reasons. (Defs.' Opp'n 3–4.) Given the Court's discussion above, the reason most relevant to the Court's analysis is the contention that certification should be denied because individual issues predominate over the common ones of the proposed class. (Defs.' Opp'n 12.) The Court agrees.

A class may be certified only if the plaintiffs can satisfy the requirements of Rule 23(a) and 23(b). Fed. R. Civ. P. 23. Here, even assuming Plaintiffs can satisfy Rule 23(a), they cannot satisfy Rule 23(b).

Rule 23(b) can be satisfied in one of three ways. In cases like this one, where Plaintiffs assert individualized monetary claims, certification is properly considered under Rule 23(b)(3). *Wal-Mart Stores Inc. v. Dukes*, 131 S. Ct. 2541, 2558 (2011). To

certify a class under Rule 23(b)(3), a court must find that "the questions of law or fact common to class members predominate over any questions affecting only individual members." Fed. R. Civ. P. 23(b)(3).

As the Court explained at the beginning of its discussion above, proving direct reliance (an essential element of a § 10(b) cause of action) individually for each member in a securities class action makes it impossible to satisfy the predominance requirement of Rule 23(b)(3). *See Halliburton*, 131 S. Ct. at 2184–85; *Amgen*, 133 S. Ct. at 1199. Accordingly, Plaintiffs must show that they can invoke the "fraud-on-the-market" theory to thereby establish reliance on behalf of the class as a whole. *Halliburton I*, 131 S. Ct. at 2184–85. And "[t]he burden of proving those prerequisites [to invoking the "fraud-on-the-market" theory] still rests with plaintiffs and (with the exception of materiality) must be satisfied before class certification." *Halliburton II*, 134 S. Ct. at 2412.

In their motion, Plaintiffs attempt to invoke the theory, and therefore establish reliance for the putative class, by citing Marek's declaration. (Pls.' Mot. 19–23.) They also submit McGraw's supplemental declaration. (Dkt. No. 205.) But as discussed above, Marek's declaration is unreliable, McGraw is unqualified, and the Court granted Defendants' motion to exclude them. As such, Plaintiffs have failed to show that they are able to invoke the "fraud-on-the-market" theory of reliance. Consequently, they also fail to demonstrate that individual issues (like reliance) do not predominate over common ones. On this basis, Plaintiffs' motion for class certification is DENIED without prejudice.

IV. CONCLUSION

For the reasons discussed above, Defendants' motion is GRANTED and Plaintiffs' motion is DENIED without prejudice.

IT IS SO ORDERED.

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