

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

August Term, 2009

(Argued: September 30, 2009 Decided: December 3, 2009)

Docket No. 08-0420-cv

- - - - -x

ELECTRONIC TRADING GROUP, LLC, on
behalf of itself and all others
similarly situated,

Plaintiff-Appellant,

- v. -

BANC OF AMERICA SECURITIES LLC, BEAR
STEARNS COMPANIES, INC., CITIGROUP INC.,
CREDIT SUISSE (USA) INC., DEUTSCHE BANK
SECURITIES, INC., GOLDMAN, SACHS & CO.,
MERRILL LYNCH, PIERCE, FENNER & SMITH
INCORPORATED, MORGAN STANLEY & CO.
INCORPORATED, UBS FINANCIAL SERVICES,
INC., CIBC WORLD MARKETS CORP.,
CITIGROUP GLOBAL MARKETS, INC., CREDIT
SUISSE SECURITIES (USA) LLC, GOLDMAN
SACHS EXECUTION & CLEARING, L.P.,
MORGAN STANLEY DW INC., THE GOLDMAN
SACHS GROUP, INC., and VAN DER MOOLEN
SPECIALISTS USA, LLC,

Defendants-Appellees,

JOHN DOES, DAIWA AMERICA CORPORATION,
DAIWA SECURITIES AMERICA INC., BANK OF
NEW YORK, J.P. MORGAN CHASE & CO., J.P.
MORGAN SECURITIES INC., and LEHMAN
BROTHERS INC.,

1 RICHARD H. KLAPPER and RICHARD
2 C. PEPPERMAN, II, Sullivan &
3 Cromwell LLP, New York, New
4 York, for Appellees Goldman,
5 Sachs & Co., Goldman Sachs
6 Execution & Clearing, L.P., and
7 The Goldman Sachs Group, Inc.
8

9 STEPHEN L. RATNER and HARRY
10 FRISCHER, Proskauer Rose LLP,
11 New York, New York, for Appellee
12 Bear Stearns Companies, Inc.
13

14 JAY B. KASNER and SHEPARD
15 GOLDFEIN, Skadden, Arps, Slate,
16 Meagher & Flom LLP, New York,
17 New York, for Appellee Merrill
18 Lynch, Pierce, Fenner & Smith
19 Incorporated.
20

21 JAY P. LEFKOWITZ, MARIA
22 GINZBURG, ANDREW B. CLUBOK,
23 SUSAN E. ENGEL, and ELEANOR R.
24 BARRETT, Kirkland & Ellis LLP,
25 New York, New York and
26 Washington, D.C., for Appellee
27 UBS Financial Services, Inc.
28

29 ROBERT B. McCAW, FRASER L.
30 HUNTER, JR., and ALI M.
31 STOEPPELWERTH, Wilmer Cutler
32 Pickering Hale and Dorr LLP, New
33 York, New York and Washington,
34 D.C., for Appellees Citigroup
35 Inc., Citigroup Global Markets,
36 Inc., Credit Suisse (USA) Inc.,
37 and Credit Suisse Securities
38 (USA) LLC.
39

40 ANDREW J. FRACKMAN and BRENDAN
41 J. DOWD, O'Melveny & Myers LLP,
42 New York, New York, for Appellee
43 Banc of America Securities LLC.
44

1 GREGORY A. MARKEL and MARTIN L.
2 SEIDEL, Cadwalader, Wickersham &
3 Taft LLP, New York, New York,
4 for Appellee Deutsche Bank
5 Securities, Inc.
6

7 DANIEL B. RAPPORT, KATHERINE L.
8 PRINGLE, and LISA S. GETSON,
9 Friedman Kaplan Seiler & Adelman
10 LLP, New York, New York, for
11 Appellee Van Der Moolen
12 Specialists USA, LLC.
13

14 JONATHAN D. POLKES, ROBERT F.
15 CARANGELO, and DEBRA J.
16 PEARLSTEIN, Weil, Gotshal &
17 Manges LLP, New York, New York,
18 for Appellee CIBC World Markets
19 Corp.
20

21 DENNIS JACOBS, Chief Judge:
22

23 In this putative class action, plaintiff-appellant
24 Electronic Trading Group, LLC ("ETG"), a short seller, sues
25 certain financial institutions that serve as "prime brokers"
26 in short sale transactions.¹ It is alleged that the prime
27 brokers arbitrarily designated certain securities as hard-

¹ The defendants-appellees are Banc of America Securities LLC; Bear Stearns Companies, Inc.; Citigroup Inc.; Credit Suisse (USA) Inc.; Deutsche Bank Securities, Inc.; Goldman, Sachs & Co.; Merrill Lynch, Pierce, Fenner & Smith Incorporated; Morgan Stanley & Co., Incorporated; UBS Financial Services, Inc.; CIBC World Markets Corp.; Citigroup Global Markets, Inc.; Credit Suisse Securities (USA) LLC; Goldman Sachs Execution & Clearing, L.P.; The Goldman Sachs Group, Inc.; Van Der Moolen Specialists USA, LLC; and Morgan Stanley DW Inc.

1 to-borrow and then fixed the price for borrowing them, in
2 violation of Section 1 of the Sherman Act, 15 U.S.C. § 1
3 (the "antitrust claim").² Three state law claims are also
4 pleaded: breach of fiduciary duty, aiding and abetting
5 breach of fiduciary duty, and unjust enrichment
6 (collectively, the "state law claims").³

7 ETG appeals from a judgment of the United States
8 District Court for the Southern District of New York
9 (Marrero, J.), dismissing the antitrust claim with prejudice
10 on the ground of implied preclusion of the antitrust law by
11 the securities law, and dismissing the state law claims

² "A complaint pleading a violation of section 1 must allege a contract, combination or conspiracy that unreasonably restrains trade." Elecs. Commc'ns Corp. v. Toshiba Am. Consumer Prods., Inc., 129 F.3d 240, 243 (2d Cir. 1997).

³ ETG brought the breach of fiduciary duty claim against Morgan Stanley DW Inc.; Bear Stearns Companies, Inc.; Goldman Sachs Execution & Clearing, L.P.; Goldman, Sachs & Co.; UBS Financial Services, Inc.; Merrill Lynch, Pierce, Fenner & Smith Incorporated; Citigroup Global Markets, Inc.; Credit Suisse Securities (USA) LLC; Deutsche Bank Securities, Inc.; Banc of America Securities LLC; Van Der Moolen Specialists USA, LLC; and CIBC World Markets Corp.

ETG brought the aiding and abetting breach of fiduciary duty claim against the parent corporations of some of the prime brokers named in the breach of fiduciary duty claim-- Morgan Stanley & Co., Incorporated; The Goldman Sachs Group, Inc.; Citigroup Inc.; and Credit Suisse (USA) Inc.

1 without prejudice to refiling in state court. We affirm.

2 The preclusion analysis turns on four considerations
3 identified in Credit Suisse Securities (USA) LLC v. Billing,
4 551 U.S. 264, 285 (2007): whether the “area of conduct [is]
5 squarely within the heartland of securities regulations”;
6 whether the Securities and Exchange Commission (“SEC”) has
7 “clear and adequate [] authority to regulate”; whether there
8 is “active and ongoing agency regulation”; and whether “a
9 serious conflict” arises between antitrust law and
10 securities regulations.

11 Much depends on the level of particularity or
12 generality at which each Billing consideration is evaluated.
13 Obviously, if the inquiry is whether the SEC actively
14 regulates the pricing of borrowed shares, the plaintiff wins
15 the point. By the same token, if the inquiry is whether
16 short selling is within the heartland of securities
17 regulations, the defendants win the point.

18 For the reasons set forth in this opinion, the fourth
19 consideration--detection of a serious conflict--is evaluated
20 at the level of the alleged anticompetitive conduct. Each
21 of the three remaining considerations is evaluated at the
22 level most useful to the court in achieving the overarching

1 goal of avoiding conflict between the securities and
2 antitrust regimes.

4 BACKGROUND

5 A. Short Selling

6 A short sale transaction proceeds in the following
7 sequence. The short seller identifies securities she
8 believes will drop in market price, borrows these securities
9 from a broker (prime brokers have the greatest market
10 share), sells the borrowed securities on the open market,
11 purchases replacement securities on the open market, and
12 returns them to the broker--thereby closing the short
13 seller's position. The short seller's profit (if any) is
14 the difference between the market price at which she sold
15 the borrowed securities and the market price at which she
16 purchased the replacement securities, less borrowing fees,
17 brokerage fees, interest, and any other charges levied by
18 the broker.

20 B. The Role of the Prime Brokers

21
22 In the context of short selling, a prime broker locates
23 the short seller's requested securities, lends those

1 securities to the short seller for a fee, and delivers those
2 securities to the short seller's purchaser.

3 A short seller seeking to borrow securities contacts
4 the broker's securities loan desk. Pursuant to SEC
5 regulations, the securities loan desk must locate the
6 requested securities before it can accept the short seller's
7 order. See 17 C.F.R. § 242.203(b)(1)(i)-(iii). The
8 securities loan desk may locate the securities in its own
9 proprietary accounts, or in the hands of other brokers or
10 institutional investors with significant long positions.
11 Alternatively, the securities loan desk may locate the
12 securities through a third party who assists the broker in
13 exchange for a locate fee.

14 The broker charges the short seller a borrowing fee
15 affected by supply and demand: the harder the security is to
16 find and borrow, the higher the fee. The broker may develop
17 an easy-to-borrow list of securities that are in abundant
18 supply and a hard-to-borrow list of securities that are
19 scarce. See Short Sales, Exchange Act Release No. 34-50103,
20 83 SEC Docket 1278 (July 28, 2004).

21 A short seller who has sold the borrowed securities on
22 the open market must deliver those securities to the

1 purchaser within three days of the transaction date. If the
2 short seller's broker does not deliver in time, a failure-
3 to-deliver ("FTD") occurs.

4 5 **C. The Borrowing Fees Conspiracy**

6
7 It is alleged that from April 12, 2000 to the present,
8 the prime brokers charged "artificially inflated" borrowing
9 fees by agreeing on which securities to designate
10 arbitrarily as hard-to-borrow, and setting minimum borrowing
11 fees for these securities. (There are other allegations,
12 set out in the margin, which we do not reach.⁴)

13
⁴ ETG's Amended Class Action Complaint (the "complaint") also alleges that the prime brokers (i) failed to enforce the delivery of securities, thereby enabling the prime brokers to charge borrowing fees for securities that were never actually borrowed and giving rise to intentional FTDs; and (ii) charged improper locate fees when the securities were never found and/or borrowed. On appeal, ETG argues that the complaint's "references to failures to deliver" and "improper and unjustified locate fees" were "pleaded [only] as an adjunct to [ETG's] price-fixing claim." Appellant's Reply Br. 17 & 17 n.12. The prime brokers argue that ETG improperly seeks to amend the complaint on appeal by recharacterizing these allegations from integral components of the conspiracy to ancillary means of expanding the conspiracy's scope. Appellees' Opp'n Br. 24-25. We do not reach this issue, because dismissal remains appropriate even if we adopt ETG's appellate posture.

1 **D. Procedural History**

2 On March 15, 2007, the prime brokers moved to dismiss
3 the antitrust claim pursuant to Federal Rules of Civil
4 Procedure 12(b)(6) and 9(b). On June 18, 2007, the United
5 States Supreme Court decided Billing. On December 20, 2007,
6 the district court applied Billing, granted the prime
7 brokers' motion to dismiss the antitrust claim under Rule
8 12(b)(6), and declined to exercise supplemental jurisdiction
9 over the state law claims.⁵ ETG timely appealed the
10 district court's decision, arguing principally that the
11 district court misapplied Billing.

12
13 **DISCUSSION**

14 "We review the district court's grant of a Rule
15 12(b)(6) motion de novo, drawing all reasonable inferences
16 in plaintiff[']s favor, and accepting as true all the
17 factual allegations in the complaint." In re Elevator
18 Antitrust Litig., 502 F.3d 47, 50 (2d Cir. 2007) (per
19 curiam) (internal quotation marks, citations, and brackets

⁵ The district court did not reach the alternative Rule 9(b) ground for dismissal of the antitrust claim. We do not reach this ground because we affirm the district court's Rule 12(b)(6) dismissal.

1 omitted).

2 Credit Suisse Securities (USA) LLC v. Billing, 551 U.S.
3 264 (2007), was an antitrust action against underwriting
4 firms that marketed and distributed shares in initial public
5 offerings ("IPO"). The plaintiffs alleged "that the
6 underwriters unlawfully agreed with one another that they
7 would not sell shares of a popular new issue to a buyer
8 unless that buyer committed (1) to buy additional shares of
9 that security later at escalating prices (a practice called
10 'laddering'), (2) to pay unusually high commissions on
11 subsequent security purchases from the underwriters, or (3)
12 to purchase from the underwriters other less desirable
13 securities (a practice called 'tying')." Id. at 267.

14 The Supreme Court ruled that federal securities law
15 implicitly precluded application of the antitrust law to the
16 underwriters' alleged anticompetitive conduct. The Court
17 articulated four considerations that bear upon whether "the
18 securities laws are 'clearly incompatible' with the
19 application of the antitrust laws" in a particular context:
20 (A) location within the heartland of securities regulations;
21 (B) SEC authority to regulate; (C) ongoing SEC regulation;
22 and (D) conflict between the two regimes. Id. at 285. In

1 selecting the level of particularity at which to address
2 each consideration, we draw guidance from the specifics of
3 the Supreme Court's analysis in Billing, without suggesting,
4 however, that the level of particularity applied to each
5 consideration in this case is prescriptive in every context.

6
7 **A. Heartland**

8 To ascertain whether "the possible conflict" between
9 securities law and antitrust law affects "practices that lie
10 squarely within an area of financial market activity that
11 the securities law seeks to regulate," the Supreme Court
12 looked to the broad underlying market activity. Billing,
13 551 U.S. at 276. In deciding that the antitrust allegations
14 "concern practices that lie at the very heart of the
15 securities marketing enterprise," the Court considered "the
16 activities in question," which were found to consist of "the
17 underwriters' efforts jointly to promote and to sell newly
18 issued securities." Id. Accordingly, the Court focused on
19 whether "[t]he IPO process" (the underlying market activity
20 in Billing) was within the heartland (and ruled that it
21 was); it did not focus on the laddering and tying
22 arrangements (the alleged anticompetitive conduct in

1 Billing). Id. This analysis suggests that the first
2 consideration is properly evaluated at the level of the
3 underlying market activity.

4 Accordingly, in this case, we consider whether short
5 selling is within the heartland of the securities business.
6 The district court found that "the liquidity and pricing
7 benefits created by the short sales place these transactions
8 'within the heartland' of federal securities regulation and
9 are 'central to the proper functioning of well-regulated
10 capital markets.'" In re Short Sale Antitrust Litig., 527
11 F. Supp. 2d 253, 259 (S.D.N.Y. 2007) (quoting Billing, 551
12 U.S. at 276). ETG itself recognizes that "short selling is
13 market activity regulated by the securities law."

14 Appellant's Reply Br. 3.

15 Short selling--the underlying market activity in this
16 case--is "an area of conduct squarely within the heartland
17 of securities regulations." Billing, 551 U.S. at 285. The
18 first consideration thus weighs in favor of implied
19 preclusion.

20

21 **B. Authority to Regulate**

22 To ascertain "the existence of regulatory authority

1 under the securities law to supervise the activities in
2 question" in Billing, 551 U.S. at 275, the Supreme Court
3 looked to the role of the underwriters in the IPO process as
4 well as to the alleged laddering and tying arrangements, see
5 id. at 276-77. The Court determined that "the law grants
6 the SEC authority to supervise all of the activities here in
7 question. Indeed, the SEC possesses considerable power to
8 forbid, permit, encourage, discourage, tolerate, limit, and
9 otherwise regulate virtually every aspect of the practices
10 in which underwriters engage." Id. at 276. The Court thus
11 gauged regulation of activity that is more particular than
12 the IPO process (the underlying market activity) and more
13 general than the laddering and tying arrangements (the
14 alleged anticompetitive conduct).

15 In addition, the Court cited regulations that grant the
16 SEC power to regulate "communications between underwriting
17 participants and their customers, including those that occur
18 during road shows," which suggests that the Court also
19 gauged regulation of the specific alleged anticompetitive
20 conduct. Id. at 277.

21 Accordingly, we consider the existence of SEC authority
22 to regulate (i) the role of the prime brokers in short

1 selling, and (ii) the borrowing fees charged by prime
2 brokers. We find such authority in Section 10(a), Section
3 6, and 15 U.S.C. §§ 78o(c)(2)(D) and 78j(b).

4 Section 10(a) of the Securities Exchange Act of 1934
5 provides that it is unlawful “[t]o effect a short sale . . .
6 of any security registered on a national securities
7 exchange, in contravention of such rules and regulations as
8 the Commission may prescribe as necessary or appropriate in
9 the public interest or for the protection of investors.” 15
10 U.S.C. § 78j(a)(1). Citing legislative history, ETG argues
11 that Section 10(a) was intended only to regulate the
12 manipulation of share price through short selling. See
13 Appellant’s Br. 20-21. However, nothing in the wording of
14 Section 10(a) so limits its reach; and the SEC has
15 interpreted Section 10(a) as a grant of “plenary authority
16 to regulate short sales of securities registered on a
17 national securities exchange” Short Sales, Exchange
18 Act Release No. 34-48709, 68 Fed. Reg. 62,972 (proposed Nov.
19 6, 2003). The SEC thus has the authority to regulate the
20 role of the prime brokers in short selling, as well as the
21 borrowing fees charged by the prime brokers, pursuant to
22 Section 10(a).

1 Section 6 of the Securities Exchange Act of 1934
2 provides that the SEC may "permit a national securities
3 exchange, by rule, to impose a schedule or fix rates of
4 commissions, allowances, discounts, or other fees to be
5 charged by its members for effecting transactions" if such
6 fees are "reasonable" and "do not impose any burden on
7 competition not necessary or appropriate" to further the
8 purposes of the securities law. 15 U.S.C. § 78f(e)(1)(B).
9 ETG characterizes Section 6 as a grant of limited authority
10 to permit exchanges to deviate from "the general prohibition
11 on fixed commission rates." Appellant's Br. 22. Even
12 accepting this characterization, the SEC thus has indirect
13 authority to regulate the rates (including the borrowing
14 fees) charged by the prime brokers in short selling.

15 In Billing, the Supreme Court relied in part on 15
16 U.S.C. §§ 78o(c)(2)(D) and 78j(b) as evidence of the SEC's
17 broad power to define and prevent fraudulent, deceptive, and
18 manipulative conduct by brokers and dealers. 551 U.S. at
19 277. These provisions apply with equal force to the role of
20 the prime brokers in short selling and the borrowing fees
21 they charge.

22 This second Billing consideration--focused as it is on

1 whether the SEC has authority to regulate the role of the
2 prime brokers in short selling and the borrowing fees
3 charged by the prime brokers--thus weighs in favor of
4 implied preclusion, even though none of the provisions
5 discussed above explicitly references the regulation of
6 borrowing fees.

7 8 **C. Ongoing Regulation**

9 To evaluate "evidence that the responsible regulatory
10 entities exercise [their] authority," Billing, 551 U.S. at
11 275, the Supreme Court looked to the role of the
12 underwriters in the IPO process, see id. at 277. The Court
13 determined that "the SEC has continuously exercised its
14 legal authority to regulate conduct of the general kind now
15 at issue. It has defined in detail, for example, what
16 underwriters may and may not do and say during their road
17 shows." Id. The Court thus looked to activity more
18 particular than the IPO process (the underlying market
19 activity) and more general than the laddering and tying
20 arrangements (the alleged anticompetitive conduct).

21 In this case, we therefore consider whether there is
22 ongoing SEC regulation of the role of the prime brokers.

1 Ample evidence reveals that the SEC exercises its authority
2 to regulate the role of the prime brokers in short selling.
3 “[A]ctive and ongoing agency regulation” is evidenced by
4 Regulation SHO and a recent SEC roundtable. Id. at 285.

5 Regulation SHO, adopted by the SEC in 2004, imposes a
6 “locate” requirement on brokers involved in short selling.
7 See 17 C.F.R. § 242.203(b)(1)(i)-(iii) (“A broker or dealer
8 may not accept a short sale order in an equity security from
9 another person . . . unless the broker or dealer has: (i)
10 [b]orrowed the security, or entered into a bona-fide
11 arrangement to borrow the security; or (ii) [r]easonable
12 grounds to believe that the security can be borrowed so that
13 it can be delivered on the date delivery is due. . . .”).
14 Regulation SHO also imposes a “delivery” requirement on such
15 brokers. See 17 C.F.R. § 242.203(b)(3) (with certain
16 enumerated exceptions, “[i]f a participant of a registered
17 clearing agency has a fail to deliver position at a
18 registered clearing agency in a threshold security for
19 thirteen consecutive settlement days, the participant shall
20 immediately thereafter close out the fail to deliver
21 position by purchasing securities of like kind and
22 quantity”). Regulation SHO thus constitutes an exercise of

1 the SEC's authority to supervise the role of the prime
2 brokers in short selling.

3 On September 29-30, 2009 (at the time of oral argument
4 in this appeal), the SEC hosted a roundtable "regarding
5 securities lending and short sales." Securities Lending and
6 Short Sale Roundtable, Exchange Act Release No. 34-60643,
7 2009 WL 2915632, at *1 (Sept. 10, 2009) (announcing the
8 roundtable). The roundtable intended to focus on "a range
9 of securities lending topics, such as current lending
10 practices and participants, compensation arrangements and
11 conflicts, the benefits and risks of securities lending,
12 risks related to cash collateral reinvestment, improvements
13 to transparency, and consideration of whether the securities
14 lending regulatory regime can be improved for the benefit of
15 investors." Id. The roundtable also intended to focus on
16 "short sale disclosure topics" and addressed "the potential
17 impact of imposing a pre-borrow or enhanced 'locate'
18 requirement on short sellers . . . as a way to curtail
19 abusive 'naked' short selling." Id. This roundtable
20 indicates active SEC monitoring of the role of the prime
21 brokers in short selling.

22 ETG's complaint implicitly confirms active regulation.

1 The complaint affirmatively alleges, presumably to flesh out
2 claims of wrongdoing, that certain prime brokers "have been
3 fined for not borrowing securities or failing to enter into
4 agreements to borrow securities that are sold in short sale
5 transactions and/or having reasonable grounds to believe
6 that the securities could be borrowed so that they could be
7 delivered on the delivery due date," Compl. ¶ 91, and that
8 "federal prosecutors and the [New York Stock Exchange] have
9 launched a joint investigation into [certain prime brokers']
10 alleged price gouging . . . by artificially inflating
11 borrowing fees and by charging fees for which no services
12 were rendered," id. ¶ 92. A fair inference from these
13 allegations is that the SEC and securities self-regulating
14 organizations actively exercise regulatory authority over
15 the role of the prime brokers in short selling.

16 Regulation SHO and the recent roundtable do not focus
17 on the regulation of borrowing fees (the particular conduct
18 alleged to be anticompetitive); but it is enough for this
19 purpose that the SEC's ongoing regulation is focused on the
20 role of the prime brokers in short selling. The third
21 consideration thus weighs in favor of implied preclusion.

22

1 **D. Conflict**

2 To ascertain the “risk that the securities and
3 antitrust laws, if both applicable, would produce
4 conflicting guidance, requirements, duties, privileges, or
5 standards of conduct,” Billing, 551 U.S. at 275-76, the
6 Supreme Court considered whether allowing antitrust
7 liability for the conduct alleged to have the
8 anticompetitive effect would inhibit permissible (and even
9 beneficial) market behavior. See id. at 282 (“And the
10 threat of antitrust mistakes, i.e., results that stray
11 outside the narrow bounds that plaintiffs seek to set, means
12 that underwriters must act in ways that will avoid not
13 simply conduct that the securities law forbids (and will
14 likely continue to forbid), but also a wide range of joint
15 conduct that the securities law permits or encourages (but
16 which they fear could lead to an antitrust lawsuit and the
17 risk of treble damages).”). In evaluating conflict,
18 therefore, the proper focus is on the alleged
19 anticompetitive conduct:

20 [W]e do not read the complaints as attacking the
21 bare existence of IPO underwriting syndicates or
22 any of the joint activity that the SEC considers a
23 necessary component of the IPO-related syndicate
24 activity. . . . Nor do we understand the complaints
25 as questioning underwriter agreements to fix the

1 levels of their commissions, whether or not the
2 resulting price is "excessive." We . . . read the
3 complaints as attacking the *manner* in which the
4 underwriters jointly seek to collect "excessive"
5 commissions. The complaints attack underwriter
6 efforts to collect commissions through certain
7 practices (i.e., laddering, tying, collecting
8 excessive commissions in the form of later sales of
9 the issued shares)

10 Id. at 278 (citations omitted).

11 In this case, therefore, we consider the impact that
12 antitrust liability may have on arrangements for borrowing
13 fees. ETG argues (i) that "there should be little
14 difficulty in distinguishing collusive fee-fixing agreements
15 from routine communications concerning stock availability
16 and market pricing permissible under Regulation SHO"; and
17 (ii) that "there is no actual or potential conflict that
18 necessitates immunity" because neither the securities law
19 nor the antitrust law permit the collusive fixing of
20 borrowing fees. Appellant's Br. 32-33. The district court
21 found otherwise. See In re Short Sale Antitrust Litig., 527
22 F. Supp. 2d at 260.

23 We conclude that antitrust liability would create
24 actual and potential conflicts with the securities regime.
25 An actual conflict arises because antitrust liability would
26 inhibit the prime brokers (and other brokers) from engaging

1 in other conduct that the SEC currently permits and that
2 benefits the efficient functioning of the short selling
3 market. There is a potential conflict because the SEC in
4 the future may decide to regulate the borrowing fees charged
5 by brokers.

6 **1. Actual Conflict**

7 Antitrust liability would inhibit conduct that the SEC
8 permits and that assists the efficient functioning of the
9 short selling market. The thrust of ETG's case is that the
10 prime brokers communicated with one another to designate
11 hard-to-borrow securities and to fix inflated borrowing fees
12 for those securities. However, it is permissible for
13 brokers to communicate about the availability and price of
14 securities. As the district court observed, "such exchanges
15 are implicitly permitted by the SEC's Regulation SHO." In
16 re Short Sale Antitrust Litig., 527 F. Supp. 2d at 260
17 (citing 17 C.F.R. § 242.203(b)(1) (requiring that a broker
18 borrow the securities or have reasonable grounds to believe
19 that the securities can be borrowed before accepting an
20 order from a short seller)). It is a lot to expect a broker
21 "to distinguish what is forbidden from what is allowed," so
22 that the broker collects just so much information as

1 required to satisfy the locate requirement and for the
2 efficient functioning of the short selling market--but not
3 an iota more--or suffer treble damages. Billing, 551 U.S.
4 at 280.

5 Conflict is a risk unless there is a "practical way to
6 confine antitrust suits so that they challenge only activity
7 of the kind the [plaintiffs] seek to target" without
8 inhibiting other conduct that is permitted or encouraged
9 under the securities law. Id. at 282. The drawing of such
10 intricate lines demands "securities-related expertise." Id.
11 Moreover, it is likely that the very communications in which
12 short sellers do what the securities law allows would by
13 "reasonable but contradictory inferences" serve as evidence
14 of conduct forbidden by the antitrust law. Id. Reliance on
15 a jury therefore gives rise to a serious "risk of
16 inconsistent court results." Id.

17 Antitrust liability, with the prospect of treble
18 damages, would be an incentive for the prime brokers to curb
19 their permissible exchange of information and thereby harm
20 the efficient functioning of the short selling market. This
21 inhibiting effect weighs in favor of implied preclusion.

22 **2. Potential Conflict**

1 In addition to the actual conflict described above, a
2 potential conflict exists based on the possibility that the
3 SEC will act upon its authority to regulate the borrowing
4 fees set by prime brokers. As the Supreme Court
5 acknowledged in Billing, a potential conflict of this kind
6 may exist even if there is no conflict that is actual and
7 immediate. See Billing, 551 U.S. at 273 (describing the
8 “upshot” of Gordon v. N.Y. Stock Exch., Inc., 422 U.S. 659,
9 690-91 (1975), as “in light of potential future conflict,
10 the Court found that the securities law precluded antitrust
11 liability even in respect to a practice that both antitrust
12 law and securities law might forbid”). In the context of an
13 implied repeal case, this Court observed that “the proper
14 focus is not on the Commission’s current regulatory position
15 but rather on the Commission’s authority to permit conduct
16 that the antitrust laws would prohibit.” In re Stock
17 Exchs. Options Trading Antitrust Litig., 317 F.3d 134, 149
18 (2d Cir. 2003).

19 It is therefore not decisive that neither securities
20 law nor antitrust law allows--or encourages--the collusive
21 fixing of borrowing fees. The present securities regime
22 expressly allows prime brokers to rely on easy-to-borrow

1 lists as reasonable grounds "to believe that the security
2 sold short is available for borrowing without directly
3 contacting the source of the borrowed securities." Short
4 Sales, Exchange Act Release No. 34-50103, 83 SEC Docket 1278
5 (July 28, 2004). The SEC has taken note that hard-to-borrow
6 lists "are not widely used by broker-dealers" and that,
7 therefore, "the fact that a security is not on a hard to
8 borrow list cannot satisfy the 'reasonable grounds' test"
9 described above. Id. But if and when such hard-to-borrow
10 lists come into broader use, it is easy to see how they
11 could increase the efficiency of the short selling market,
12 in which event the SEC could move quickly to regulate the
13 borrowing fees charged by brokers for securities appearing
14 on such lists. This potential conflict weighs in favor of
15 implied preclusion.

17 CONCLUSION

18 All four Billing considerations weigh in favor of
19 implied preclusion.⁶ We therefore affirm the district

⁶ Because all four of the Billing considerations point in the direction of implied preclusion, we need not address the weight to be accorded these considerations when they point in different directions.

1 court's Rule 12(b)(6) dismissal of ETG's antitrust claim
2 with prejudice. Moreover, we affirm the dismissal of ETG's
3 state law claims without prejudice because we find no abuse
4 of discretion in the district court's decision to decline to
5 exercise supplemental jurisdiction over these claims. See
6 Kolari v. N.Y.-Presbyterian Hosp., 455 F.3d 118, 122 (2d
7 Cir. 2006).

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