UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

IN RE HEARTWARE INTERNATIONAL, INC. SECURITIES LITIGATION	No. 1:16-cv-00520-RA

MEMORANDUM OF LAW IN SUPPORT OF LEAD PLAINTIFF'S
MOTION FOR FINAL APPROVAL OF SETTLEMENT AND PLAN OF ALLOCATION

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Dated: March 8, 2019

TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

PRELIMINARY STATEMENT 1

ARGUMENT 5

I. THE PROPOSED SETTLEMENT WARRANTS FINAL APPROVAL 5

A. Lead Plaintiff and Lead Counsel Have Adequately Represented the Class 7

B. The Settlement Was Reached After Arm's-Length Negotiations with the Assistance of an Experienced Mediator and Following Substantial Discovery 8

C. The Relief that the Settlement Provides for the Class is Adequate, Taking into Account the Costs and Risks of Further Litigation and All Other Relevant Factors 11

1. The Risks of Establishing Liability and Damages Support Approval of the Settlement 12

(a) Risks To Proving Liability 12

(b) Risks To Proving Damages and Loss Causation 15

2. The Settlement Represents a Substantial Percentage of Likely Recoverable Damages 17

3. The Costs and Delays of Continued Litigation Support Approval of the Settlement 18

4. All Other Factors Set Forth in Rule 23(e)(2)(C) Support Approval of the Settlement 19

D. The Settlement Treats Class Members Equitably Relative to Each Other 20

E. The Reaction of the Class to the Settlement 21

II. THE PLAN OF ALLOCATION IS FAIR AND REASONABLE AND SHOULD BE APPROVED 22

III. NOTICE TO THE CLASS SATISFIED THE REQUIREMENTS OF RULE 23 AND DUE PROCESS 23

CONCLUSION 25

TABLE OF AUTHORITIES

Cases **Page(s)**

In re Advanced Battery Techs.,
298 F.R.D. 171 (S.D.N.Y. 2014); 25

In re Barrick Gold Sec. Litig.,
314 F.R.D. 91 (S.D.N.Y. 2016) 7

In re Bear Stearns Companies, Inc. Sec., Derivative, & ERISA Litig.,
909 F. Supp. 2d 259 (S.D.N.Y. 2012).....21, 22

In re Citigroup Inc. Sec. Litig.,
2014 WL 2112136 (S.D.N.Y. May 20, 2014) 5

City of Detroit v. Grinnell Corp.,
495 F.2d 448 (2d Cir. 1974).....6, 8, 11

D'Amato v. Deutsche Bank,
236 F.3d 78 (2d Cir. 2001).....8

Dura Pharm., Inc. v. Broudo,
544 U.S. 336 (2005).....15

ECA, Local 134 IBEW Joint Pension Trust of Chicago v. JP Morgan Chase Co.,
553 F.3d 187 (2d Cir. 2009).....14

Eisen v. Carlisle & Jacquelin,
417 U.S. 156 (1974).....24

In re Facebook, Inc. IPO Sec. & Derivative Litig.,
2015 WL 6971424 (S.D.N.Y. Nov. 9, 2015),
aff'd, 674 F. App'x 37 (2d Cir. 2016).....8, 9, 17

In re FLAG Telecom Holdings, Ltd. Sec. Litig.,
2010 WL 4537550 (S.D.N.Y. Nov. 8, 2010).....11, 21, 22

In re FLAG Telecom Holdings, Ltd. Sec. Litig.,
574 F.3d 29 (2d Cir. 2009).....15, 16

Fort Worth Emp'rs' Ret. Fund v. Biovail Corp.,
615 F. Supp. 2d 218 (S.D.N.Y. 2009).....15

In re Giant Interactive Grp., Inc. Sec. Litig.,
279 F.R.D. 151 (S.D.N.Y. 2011) 9, 22

In re Gilat Satellite Networks, Ltd.,
2007 WL 1191048 (E.D.N.Y. Apr. 19, 2007) 18

Goldberger v. Integrated Res., Inc.,
209 F.3d 43 (2d Cir. 2000).....6

In re IMAX Sec. Litig.,
283 F.R.D. 178 (S.D.N.Y. 2012).....22

In re Initial Pub. Offering Sec. Litig.,
671 F. Supp. 2d 467 (S.D.N.Y. 2009).....22

In re Luxottica Grp. S.p.A. Sec. Litig.,
233 F.R.D. 306 (E.D.N.Y. 2006).....11

In re Marsh & McLennan Cos. Sec. Litig.,
2009 WL 5178546 (S.D.N.Y. Dec. 23, 2009).....25

In re NASDAQ Market-Makers Antitrust Litig.,
187 F.R.D. 465 (S.D.N.Y. 1998).....10

In re PaineWebber Ltd. P'ship Litig.,
171 F.R.D. 104 (S.D.N.Y. 1997).....22

In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.,
2019 WL 359981 (E.D.N.Y. Jan. 28, 2019).....7

In re Polaroid ERISA Litig.,
240 F.R.D. 65 (S.D.N.Y. 2006).....7

Shapiro v. JPMorgan Chase & Co.,
2014 WL 1224666 (S.D.N.Y. Mar. 24, 2014).....10

In re Telik, Inc. Sec. Litig.,
576 F. Supp. 2d 570 (S.D.N.Y. 2008).....15

In re Veeco Instruments Inc. Sec. Litig.,
2007 WL 4115809 (S.D.N.Y. Nov. 7, 2007).....10, 15, 21

Wal-Mart Stores, Inc. v. Visa U.S.A. Inc.,
396 F.3d 96 (2d Cir. 2005).....5, 6, 9, 24

Weinberger v. Kendrick,
698 F.2d 61 (2d Cir. 1982).....8

Yang v. Focus Media Holding Ltd.,
2014 WL 4401280 (S.D.N.Y. Sept. 4, 2014).....9

Other Authorities

Fed. R. Civ. P. 23(c)(2)(B) 24, 25

Fed. R. Civ. P. 23(e) 5

Fed. R. Civ. P. 23(e)(2).....5, 6

Fed. R. Civ. P. 23(e)(2)(A) 7

Fed. R. Civ. P. 23(e)(2)(B) 8

Fed. R. Civ. P. 23(e)(2)(C) 11, 19, 20

Pursuant to Rule 23(e) of the Federal Rules of Civil Procedure, Lead Plaintiff St. Paul Teachers' Retirement Fund Association ("Lead Plaintiff" or "St. Paul Teachers"), on behalf of itself and the Class, respectfully submits this memorandum of law in support of its motion for final approval of: (1) the proposed settlement resolving all claims in the Action for the payment of $54.5 million in cash for the benefit of the Class (the "Settlement"), and (2) the proposed plan of allocation of the proceeds of the Settlement (the "Plan of Allocation").[1]

PRELIMINARY STATEMENT

Subject to Court approval, Lead Plaintiff has agreed to settle all claims in the Action in exchange for a cash payment of $54.5 million, which has been deposited into an escrow account. Lead Plaintiff respectfully submits that the proposed Settlement is an excellent result for the Class and satisfies the standards for final approval under Rule 23 of the Federal Rules of Civil Procedure. As detailed in the accompanying Rizio-Hamilton Declaration and summarized herein, the Settlement represents a substantial percentage of likely recoverable damages at trial – between 29% and 66% depending on the outcome of certain disputed issues.[2]

The Settlement was reached after two mediation sessions overseen by an experienced class action mediator, and is particularly favorable in light of the substantial risks of continued litigation.

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[1] Unless otherwise noted, capitalized terms have the meanings ascribed to them in the Stipulation and Agreement of Settlement dated November 13, 2018 (ECF No. 69-1) (the "Stipulation") or in the Declaration of John Rizio-Hamilton in Support of (I) Lead Plaintiff's Motion for Final Approval of Settlement and Plan of Allocation, and (II) Lead Counsel's Motion for an Award of Attorneys' Fees and Litigation Expenses (the "Rizio-Hamilton Declaration" or "Rizio-Hamilton Decl."), filed herewith. In this memorandum, citations to "¶ __" refer to paragraphs in the Rizio-Hamilton Declaration and citations to "Ex. __" refer to exhibits to the Rizio-Hamilton Declaration.

[2] The Rizio-Hamilton Declaration is an integral part of this submission and, for the sake of brevity in this memorandum, the Court is respectfully referred to it for a detailed description of, *inter alia*: the history of the Action (¶¶ 15-47); the nature of the claims asserted (¶ 21); the negotiations leading to the Settlement (¶¶ 42-45); the risks and uncertainties of continued litigation (¶¶ 48-75); the terms of the Plan of Allocation for the Settlement proceeds (¶¶ 81-86); and a description of the services Lead Counsel provided for the benefit of the Class (¶¶ 15-47).

At bottom, this was not a case with clearly false financial statements or a parallel government enforcement action to buoy Lead Plaintiff's claims. The alleged misstatements in this case were more general in nature, and concerned life-saving, experimental medical technology meant to benefit gravely ill patients, as well as an early-stage medical trial – subjects that are highly complex, inherently uncertain, and likely to elicit sympathy from a jury. This Action presented a number of serious risks to establishing both liability and damages.

First, Lead Plaintiff would have faced a number of challenges in proving at trial that the challenged statements were false or misleading. Lead Plaintiff had alleged three principal categories of misstatements: (i) statements about the extent of HeartWare's progress in remediating deficiencies identified in the FDA Warning Letter; (ii) statements about MVAD's safety profile and commercial viability; and (ii) statements about adverse events in MVAD's first clinical trial. ¶ 21. With respect to the statements about the remediation efforts, Defendants had a number of potentially powerful arguments that (i) their statements were too vague to be the basis for a securities fraud claim, and were unactionable statements of corporate optimism or puffery; (ii) any definite statements about the progress of the remediation were accurate because HeartWare had engaged in extensive efforts and spent more than $10 million on those efforts during the Class Period; and (iii) they were accurate because they had included cautionary language stating that the remediation process was not complete. ¶ 51. With respect to the alleged misstatements about MVAD's safety profile and commercial prospects, Defendants had substantial arguments that data from pre-clinical bench testing showed that their statements were accurate to the best of their knowledge at the time they were made. ¶ 52. Finally, Defendants could argue that their statement that the adverse events in the MVAD clinical trial were "typical" of adverse events in other trials was not false, because the events were in fact typically seen in similar trials. ¶ 53.

Lead Plaintiff also faced serious risks in establishing Defendants' scienter. Defendants would have contended that any misstatements were innocent rather than intentional. ¶¶ 54-58. This argument would have been strengthened by the fact that Defendants' statements concerned risky and experimental medical technology and an early-stage medical trial – highly uncertain subjects. ¶ 55. In addition, Defendants would argue that the alleged fraud was simply not logical because the status of HeartWare's remediation efforts would ultimately become public through FDA's action regarding the Warning Letter, and any concealed issues with MVAD's safety would be soon revealed by the results of required clinical trials. ¶ 56. Further, Defendants would argue that Defendant Godshall had not engaged in insider trading during the Class Period and, therefore, had no financial incentive to inflate the price of HeartWare stock. ¶ 57.

Even if Lead Plaintiff succeeded in establishing liability, there would be very serious challenges in establishing that the disclosure of the alleged misstatements caused investors' losses ("loss causation") and in proving damages. Defendants would argue that the declines in HeartWare's stock price following each of the alleged corrective disclosures were not caused by the alleged fraud because the disclosures did not directly reveal that the alleged misstatements were false. ¶¶ 62-63. Defendants had a strong argument that the first alleged corrective disclosure – the announcement of the proposed Valtech transaction on September 1, 2015 – did not correct any alleged misstatements about the remediation efforts or the MVAD's prospects (indeed, it did not even discuss these issues), and that the price decline following that announcement could be explained by reasons unrelated the alleged fraud – namely, the market's reaction to the dilutive nature of the proposed transaction. ¶¶ 66-70. Similarly, Defendants would contend that their statements concerning adverse events in the MVAD clinical trial on October 12, 2015 and January 11, 2016 did not specifically correct any of the alleged misstatements, but were simply

announcements of new negative information. ¶¶ 71-72. In short, Defendants would argue that the negative outcome of the MVAD clinical trial did not represent the materialization of a risk concealed by Defendants' alleged misstatements, but, instead, was the materialization of the disclosed risk, fully understood by investors, that experimental medical devices may sometimes experience adverse events in clinical trials that prevent them from reaching the market. ¶ 72. In short, there were a number of significant risks that could have resulted in the Class obtaining no recovery or a lesser recovery as a result of continued litigation.

At the time the agreement to settle was reached, Lead Plaintiff and Lead Counsel had a well-developed understanding of the strengths and weaknesses of the Action. Before the Settlement was agreed to, Lead Counsel had: (i) conducted an extensive investigation into the alleged fraud, which included a thorough review of public information such as SEC filings, analyst reports, conference call transcripts, and news articles, consultation with multiple experts, and interviews with 91 potential witnesses, including dozens of former HeartWare employees; (ii) drafted and filed an initial complaint and a detailed amended complaint based on this investigation; (iii) successfully opposed Defendants' motion to dismiss through briefing and argument; (iv) successfully obtained certification of the Class; (v) engaged in substantial fact discovery, which included serving document requests and interrogatories on Defendants, serving 27 document subpoenas on non-parties, obtaining and reviewing more than 450,000 pages of documents produced by Defendants and third parties, and producing over 7,500 pages of documents to Defendants in response to their requests; (vi) worked extensively with experts in bioengineering, cardiovascular medicine, statistics, regulatory compliance, and financial economics; and (vii) engaged in extended arm's-length settlement negotiations, including two

mediation sessions overseen by an experienced mediator, Jed D. Melnick, Esq. of JAMS. ¶ 5, 10-45.

Absent the Settlement, the Parties faced the prospect of protracted litigation through the remainder of fact discovery; costly expert discovery; additional contested motions; a trial; post-trial motion practice; individual class member loss causation and damages challenges; and likely ensuing appeals. The Settlement avoids these risks and delays while providing a substantial, certain and immediate benefit to the Class in the form of a $54.5 million cash payment. In light of these considerations, Lead Plaintiff and Lead Counsel respectfully submit that the Settlement warrants final approval by the Court.

ARGUMENT

I. THE PROPOSED SETTLEMENT WARRANTS FINAL APPROVAL

Federal Rule of Civil Procedure 23(e) requires judicial approval for any compromise or settlement of class action claims. *See* Fed. R. Civ. P. 23(e). A class action settlement should be approved if the court finds it "fair, reasonable, and adequate." Fed. R. Civ. P. 23(e)(2).

The Second Circuit has recognized that public policy favors the settlement of disputed claims among private litigants, particularly in class actions. *See Wal-Mart Stores, Inc. v. Visa U.S.A. Inc.*, 396 F.3d 96, 116 (2d Cir. 2005) ("*Visa*") ("We are mindful of the 'strong judicial policy in favor of settlements, particularly in the class action context.'") (citation omitted). In ruling on final approval of a class settlement, the court should examine both the negotiating process leading to the settlement, and the settlement's substantive terms. *See Visa*, 396 F.3d at 116; *In re Citigroup Inc. Sec. Litig.*, 2014 WL 2112136, at *2-3 (S.D.N.Y. May 20, 2014).

Rule 23(e)(2), as amended on December 1, 2018, provides that the Court should determine whether a proposed settlement is "fair, reasonable, and adequate" after considering whether:

> (A) the class representatives and class counsel have adequately represented the class;
>
> (B) the proposal was negotiated at arm's length;
>
> (C) the relief provided for the class is adequate, taking into account:
>
> (i) the costs, risks, and delay of trial and appeal;
>
> (ii) the effectiveness of any proposed method of distributing relief to the class, including the method of processing class-member claims;
>
> (iii) the terms of any proposed award of attorney's fees, including timing of payment; and
>
> (iv) any agreement required to be identified under Rule 23(e)(3); and
>
> (D) the proposal treats class members equitably relative to each other.

Fed. R. Civ. P. 23(e)(2). As discussed below, all of these factors strongly support approval of the Settlement here.

Historically, the Second Circuit has held that district courts should consider following factors set forth in *City of Detroit v. Grinnell Corp*. in evaluating a class action settlement:

> (1) the complexity, expense and likely duration of the litigation; (2) the reaction of the class to the settlement; (3) the stage of the proceedings and the amount of discovery completed; (4) the risks of establishing liability; (5) the risks of establishing damages; (6) the risks of maintaining the class action through the trial; (7) the ability of the defendants to withstand a greater judgment; (8) the range of reasonableness of the settlement fund in light of the best possible recovery; [and] (9) the range of reasonableness of the settlement fund to a possible recovery in light of all the attendant risks of litigation.

495 F.2d 448, 463 (2d Cir. 1974) (citations omitted), *abrogated on other grounds by Goldberger v. Integrated Res., Inc.*, 209 F.3d 43 (2d Cir. 2000), *see also Visa*, 396 F.3d at 117.

The Advisory Committee Notes to the 2018 amendments to the Federal Rules of Civil Procedure indicate that the four factors set forth in Rule 23(e)(2) are not intended to "displace" any factor previously adopted by the Court of Appeals, but "rather to focus the court and the

lawyers on the core concerns of procedure and substance that should guide the decision whether to approve the proposal." Advisory Committee Notes to 2018 Amendments.

Accordingly, Lead Plaintiff will discuss the fairness, reasonableness, and adequacy of the Settlement principally in relation to the four factors set forth in Rule 23(e)(2), but will also discuss the application of relevant, non-duplicative *Grinnell* factors. *See In re Payment Card Interchange Fee & Merch. Disc. Antitrust Litig.*, 2019 WL 359981, at *13 (E.D.N.Y. Jan. 28, 2019) ("The Court understands the new Rule 23(e) factors to add to, rather than displace, the *Grinnell* factors.").

A. Lead Plaintiff and Lead Counsel Have Adequately Represented the Class

In determining whether to approve a class action settlement, the court should consider whether "the class representatives and class counsel have adequately represented the class." Fed. R. Civ. P. 23(e)(2)(A); *see generally In re Barrick Gold Sec. Litig.*, 314 F.R.D. 91, 99 (S.D.N.Y. 2016) (noting that "the adequacy requirement 'entails inquiry as to whether: 1) plaintiffs' interests are antagonistic to the interest of other members of the class and 2) plaintiffs' attorneys are qualified, experienced and able to conduct the litigation'").

Here, Lead Plaintiff and Lead Counsel have adequately represented the Class in both their vigorous prosecution of the Action for over two and a half years and in the negotiation and achievement of the Settlement. Lead Plaintiff has claims that are typical of and coextensive with those of other Class Members, and has no interests antagonistic to the interests of other members of the Class. On the contrary, Lead Plaintiff – like other Class Members – has an interest in obtaining the largest possible recovery from Defendants. *See In re Polaroid ERISA Litig.*, 240 F.R.D. 65, 77 (S.D.N.Y. 2006) ("Where plaintiffs and class members share the common goal of maximizing recovery, there is no conflict of interest between the class representatives and other class members."). In addition, Court-appointed Lead Counsel is highly qualified and experienced

in securities litigation, as set forth in its firm resume (*see* Ex. 4 to the Rizio-Hamilton Declaration), and was able to successfully conduct the litigation against skilled opposing counsel.

Accordingly, as the Court previously found in certifying the Class and appointing Lead Plaintiff as Class Representative and Lead Counsel as Class Counsel, Lead Plaintiff and Lead Counsel have adequately represented the Class. *See* ECF No. 64 (Court's order certifying Class); ECF No. 54 at 12-13 (discussion of adequacy in Lead Plaintiff's memorandum of law in support of motion for class certification).

B. The Settlement Was Reached After Arm's-Length Negotiations with the Assistance of an Experienced Mediator and Following Substantial Discovery

In weighing approval of a class action settlement, the Court must consider whether the settlement "was negotiated at arm's length." Fed. R. Civ. P. 23(e)(2)(B). Courts have traditionally considered other related circumstances in determining the "procedural" fairness of a settlement, including (i) counsel's understanding of the strengths and weakness of the case based on factors such as "the stage of the proceedings and the amount of discovery completed,"[3] (ii) the absence of any indicia of collusion;[4] and (iii) the involvement of a mediator.[5] All of these circumstances strongly support the approval of the Settlement here.

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[3] *See Grinnell*, 495 F.2d at 463 (third factor); *see also In re Facebook, Inc. IPO Sec. & Derivative Litig.*, 2015 WL 6971424, at *4 (S.D.N.Y. Nov. 9, 2015) ("the question is whether the parties had adequate information about their claims, such that their counsel can intelligently evaluate the merits of plaintiff's claims, the strengths of the defenses asserted by defendants, and the value of plaintiffs' causes of action for purposes of settlement"), *aff'd*, 674 F. App'x 37 (2d Cir. 2016).

[4] *Weinberger v. Kendrick*, 698 F.2d 61, 74 (2d Cir. 1982) ("the absence of any indication of collusion, the protracted settlement negotiations, the ability and experience of plaintiffs' counsel, [and] the extensive discovery preceding settlement . . . are important indicia of the propriety of settlement negotiations").

[5] *D'Amato v. Deutsche Bank*, 236 F.3d 78, 85 (2d Cir. 2001) (a mediator's involvement in settlement negotiations "helps to ensure that the proceedings were free of collusion and undue pressure").

The Settlement was reached only after several months of arm's-length negotiations between experienced counsel, which included two separate full-day mediation sessions with Jed D. Melnick of JAMS, an experienced mediator of securities class actions and other complex litigation. ¶¶ 42-44. *See Yang v. Focus Media Holding Ltd.*, 2014 WL 4401280, at *5 (S.D.N.Y. Sept. 4, 2014) ("The participation of this highly qualified mediator [Mr. Melnick] strongly supports a finding that negotiations were conducted at arm's length and without collusion."); *In re Giant Interactive Grp., Inc. Sec. Litig.*, 279 F.R.D. 151, 160 (S.D.N.Y. 2011) (the fact that "settlement was the product of prolonged, arms-length negotiation, including as facilitated by a respected mediator" established that it was "procedurally fair").

Indeed, the Settlement merits a presumption of fairness because it was achieved after extensive arm's-length negotiations between well-informed and experienced counsel after a substantial amount of discovery. *See Visa*, 396 F.3d at 116 (a class action settlement is entitled to a "presumption of fairness, adequacy, and reasonableness" when "reached in arms' length negotiations between experienced, capable counsel after meaningful discovery"); *Facebook*, 2015 WL 6971424, at *3 (same).

In addition, as noted above, the Parties and their counsel were knowledgeable about the strengths and weaknesses of the case prior to reaching the agreement to settle. Lead Counsel conducted a detailed substantive investigation prior to filing the Complaint by, among other things, reviewing SEC filings, analyst research reports, investor conference calls, press releases, media reports, and other public material; consulting with several experts; and speaking with 91 potential witnesses. ¶¶ 18-20. Lead Counsel also performed extensive legal research in preparing the Complaint and the briefing in opposition to Defendants' motion to dismiss. ¶¶ 21, 23. After the motion to dismiss was denied, Lead Counsel obtained and reviewed a substantial amount of fact

discovery, including 450,000 pages of documents produced by Defendants and non-parties. ¶¶ 28-35. Lead Counsel also consulted extensively with experts in bioengineering, cardiovascular medicine, statistics, regulatory compliance, and financial economics throughout the litigation to enhance their understanding of the complex subject matter involved in the Action. ¶¶ 40-41. Finally, the Parties engaged in extensive settlement negotiations, including exchanging detailed mediation statements, which further informed the Parties of the strength of each side's arguments. ¶¶ 42-45.

The conclusion of Lead Plaintiff and Lead Counsel that the Settlement is fair and reasonable and in the best interests of the Class further supports its approval. Lead Plaintiff is a sophisticated institutional investor that took an active role in supervising this litigation, as envisioned by the PSLRA, and has strongly endorsed the Settlement. *See* Declaration of Jill E. Schurtz (Ex. 2) ("Schrutz Decl.") at ¶¶ 2-5. A settlement reached "under the supervision and with the endorsement of a sophisticated institutional investor . . . is 'entitled to an even greater presumption of reasonableness.'" *In re Veeco Instruments Inc. Sec. Litig.*, 2007 WL 4115809, at *5 (S.D.N.Y. Nov. 7, 2007).

In addition, the judgment of Lead Counsel, which is highly experienced in securities class action litigation, that the Settlement is in the best interests of the Class is entitled to "great weight." *Shapiro v. JPMorgan Chase & Co.*, 2014 WL 1224666, at *2 (S.D.N.Y. Mar. 24, 2014); *accord In re NASDAQ Market-Makers Antitrust Litig.*, 187 F.R.D. 465, 474 (S.D.N.Y. 1998) (courts have consistently given "'great weight' . . . to the recommendations of counsel, who are most closely acquainted with the facts of the underlying litigation").

C. The Relief that the Settlement Provides for the Class is Adequate, Taking into Account the Costs and Risks of Further Litigation and All Other Relevant Factors

In determining whether a class action settlement is "fair, reasonable, and adequate," the Court must consider whether "the relief provided for the class is adequate, taking into account . . . the costs, risks, and delay of trial and appeal" as well as other relevant factors. Fed. R. Civ. P. 23(e)(2)(C). In most cases, this will be most important factor for the Court to consider in its analysis of the proposed settlement. *See Grinnell*, 495 F.2d at 455 ("The most important factor is the strength of the case for plaintiffs on the merits, balanced against the amount offered in settlement.").[6]

"[I]n evaluating the settlement of a securities class action, federal courts, including this Court, 'have long recognized that such litigation is notably difficult and notoriously uncertain.'" *In re FLAG Telecom Holdings, Ltd. Sec. Litig.*, 2010 WL 4537550, at *15 (S.D.N.Y. Nov. 8, 2010) (citation omitted). Accordingly, "[c]lass action suits readily lend themselves to compromise because of the difficulties of proof, the uncertainties of the outcome, and the typical length of the litigation." *In re Luxottica Grp. S.p.A. Sec. Litig.*, 233 F.R.D. 306, 310 (E.D.N.Y. 2006). This case was no exception.

As discussed in detail in the Rizio-Hamilton Declaration and below, continued litigation of the Action presented a number of risks that Lead Plaintiff would be unable to establish liability and damages. ¶¶ 48-75, 79. In addition, continuing the litigation through trial and appeals would

[6] Indeed, this factor under Rule 23(e)(2)(C) essentially encompasses at least six of the nine factors of the traditional *Grinnell* analysis. *See Grinnell*, 495 F.2d at 463 ("(1) the complexity, expense and likely duration of the litigation; . . . (4) the risks of establishing liability; (5) the risks of establishing damages; (6) the risks of maintaining the class action through the trial; . . . (8) the range of reasonableness of the settlement fund in light of the best possible recovery; [and] (9) the range of reasonableness of the settlement fund to a possible recovery in light of all the attendant risks of litigation") (citations omitted).

impose substantial additional costs on the Class and would result in extended delays before any recovery could be achieved. The Settlement, which provides a $54.5 million cash payment for the benefit of the Class, avoids those further costs and delays. Moreover, the Settlement represents approximately 29% to 66% of the likely recoverable damages that could be established at trial (if Lead Plaintiff prevailed on liability issues), and thus represents a very favorable outcome in light of the litigation risks. ¶¶ 76-78

1. The Risks of Establishing Liability and Damages Support Approval of the Settlement

While Lead Plaintiff and Lead Counsel believe that the claims asserted against Defendants in the Action are meritorious, they recognize that this Action presented a number of substantial risks to establishing both liability and damages.

(a) **Risks To Proving Liability**

Defendants had vigorously contested and would have continued to argue that their challenged statements were not false or misleading. While these arguments were not successful at the motion to dismiss stage, Defendants could have succeeded in these arguments at subsequent stages of the litigation when allegations in the Complaint would need to be supported by admissible evidence. ¶ 59.

For example, Defendants would have continued to argue that the alleged misstatements concerning HeartWare's remediation of deficiencies identified in the FDA Warning Letter were either inactionable because they were vague expressions of corporate optimism or puffery or – to the extent they were sufficiently definite – were not false. ¶ 51. Defendants would contend that the statements they made about the progress of the remediation efforts were accurate because had HeartWare had engaged in substantial efforts including hiring a third-party consultant and multiple contractors to address the issue, and had spent more than $10 million dollars on remediation efforts

during the Class Period. *Id*. Defendants would argue that the Company never stated that it had completed the remediation process and had included appropriate caveats that they still had a considerable amount of work ahead. *Id*.

Defendants would argue that their statements about MVAD's safety profile were accurate at the time they were made, based on pre-clinical testing that the Company had done at that time. ¶ 52. This was a subject that would have required complicated factual and expert evidence, and turned on arguments about whether certain problems that HeartWare had encountered were sufficiently significant that they should have been disclosed, and whether those problems should have alerted HeartWare to the likelihood that the MVAD would experience a greater incidence of pump thrombosis in clinical trials.

Finally, Defendants would contend that their statement in October 2015 that the adverse events in the MVAD clinical trial were "typical" of adverse events in similar trials was not false because the type of event that occurred (thrombosis) was indeed typical in such trials. ¶ 53. Moreover, Defendants would contend that, in light of the fact that they disclosed that multiple adverse events had occurred in a group of just eleven patients only a few months after the trial commenced, the failure to disclose the exact number and timing of the adverse events did not significantly alter the total mix of information available. *Id*.

In addition to these challenges, Lead Plaintiff would have faced significant challenges in proving scienter. Defendants would have argued that their statements concerned experimental medical technology and an early-stage trial, which are inherently unpredictable, and that if any of their statements were false, the misstatements were innocent rather than intentionally misleading. ¶ 55.

Defendants would also have argued that they had no motive to mislead investors. Defendants would contend that they had no incentive to mislead investors about HeartWare's remediation efforts because the results of those efforts would ultimately become public through the FDA's action regarding the Warning Letter. ¶ 56. They would also have asserted that they had no incentive to rush the MVAD into trials or to misrepresent its safety profile, because they knew that successful completion of clinical trials was required before the device could be marketed, and that the results of those trials would have to be disclosed. *Id*. Defendants would also argue that Defendant Godshall had not engaged in insider trading during the Class Period and, therefore, did not have any financial incentive to inflate the price of HeartWare stock. ¶ 57. *See ECA, Local 134 IBEW Joint Pension Trust of Chicago v. JP Morgan Chase Co.*, 553 F.3d 187, 198 (2d Cir. 2009) ("In order to raise a strong inference of scienter through 'motive and opportunity' to defraud, Plaintiffs must allege that [Defendant] or its officers 'benefitted in some concrete and personal way from the purported fraud.").

In short, it was far from certain that Lead Plaintiff could prove the falsity of Defendants' statements at trial or Defendants' scienter. Moreover, in addressing falsity and scienter issues at trial, Defendants would attempt to portray HeartWare as a sympathetic company that strove to create a highly experimental, complex, and beneficial product for patients who are extremely ill and need to be kept alive until they can obtain a heart transplant. ¶ 60. There was risk that this sympathetic portrayal – and the inherent difficulty in anticipating how such a complex product will perform – might sway a jury and lead them to reject Lead Plaintiff's claims. *Id*.

The highly scientific context in which the alleged misstatements arose also increased the risks that Lead Plaintiff might not succeed at trial. Lead Plaintiff anticipated that substantial expert testimony on topics such as bioengineering, compliance with FDA regulations, and statistics would

be needed to help establish the claims, and there could be no guarantee that the jury would accept the view of Lead Plaintiff's experts. *See In re Telik, Inc. Sec. Litig.*, 576 F. Supp. 2d 570, 579-80 (S.D.N.Y. 2008) (in this "battle of experts, it is virtually impossible to predict with any certainty which testimony would be credited"); *Veeco*, 2007 WL 4115809, at *9 ("a very lengthy and complex battle of the parties' experts likely would have ensued at trial, with unpredictable results. These risks as to liability strongly militate in favor of the Settlement.").

(b) **Risks To Proving Damages and Loss Causation**

Assuming that Lead Plaintiff successfully developed the evidence needed to defeat all of the above risks and established liability at trial, it still faced significant risks in proving damages and loss causation. Those issues played a very important role in determining the reasonable value for the Settlement. ¶ 62.

As the Court is aware, Lead Plaintiff bears the burden of establishing loss causation – that is, that "plaintiff's losses were caused by the disclosure of the truth that Defendants had previously allegedly misrepresented." *Fort Worth Emp'rs' Ret. Fund v. Biovail Corp.*, 615 F. Supp. 2d 218, 229 (S.D.N.Y. 2009); *see, e.g.*, *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 345-46 (2005); *In re FLAG Telecom Holdings, Ltd. Sec. Litig.*, 574 F.3d 29, 36 (2d Cir. 2009).

Defendants would argue that the declines in HeartWare's stock price identified by Lead Plaintiff were not caused by the alleged misstatements because the disclosures that caused these price declines did not directly reveal that the alleged misstatements were false. ¶ 63. For example, Defendants would contend that the announcement of the proposed Valtech transaction on September 1, 2015 did not correct any alleged misstatements about the Company's remediation efforts or the MVAD's prospects. ¶ 67. Defendants would argue that the decline following that announcement was, in fact, a reaction to the dilutive nature of the proposed transaction. *Id*. While Lead Plaintiff believes that the Valtech announcement indirectly disclosed HeartWare's concerns

about the MVAD, Lead Plaintiff acknowledges that the lack of any direct disclosures about MVAD or remediation efforts in the September 1 announcement created a severe risk that the Court on summary judgment or a jury at trial might conclude that price decline following that announcement was not caused by the alleged fraud. ¶¶ 68-69.

Similarly, Defendants contended that the disclosures of adverse events in the MVAD clinical trial did not specifically correct any of the alleged misstatements regarding HeartWare's remediation efforts or MVAD's safety profile. ¶¶ 71-72. Defendants would argue that the negative outcome of the clinical trial did not represent the materialization of a risk obscured by Defendants alleged misstatements, but, instead, was the materialization of a risk that was fully disclosed and understood – that medical devices that are still being tested in clinical trials may sometimes demonstrate adverse events that prevent them from reaching the market. ¶ 72

Moreover, even if Lead Plaintiff could establish that some portion of the stock price declines on those dates were caused by the revelation of the alleged misstatements, Defendants would contend that the non-fraud-related information revealed on each of the dates ***also*** had a substantial negative affect on the price of HeartWare's common stock, and that Lead Plaintiff bore the burden of disaggregating the impact of the unrelated information. *See FLAG Telecom*, 574 F.3d at 36 ("to establish loss causation, *Dura* requires plaintiffs to disaggregate those losses caused by 'changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events,' from disclosures of the truth behind the alleged misstatements"). Defendants would have argued that this "disaggregation" could not be done in this case, and that even if it could, it would substantially reduce damages. ¶¶ 64, 70, 72.

If the litigation had proceeded to trial, Defendants would have advanced a number of other arguments that, if successful, would also have reduced damages. For example, Defendants would

have argued that a large portion of the Class suffered little or no damages from the alleged fraud because HeartWare was acquired shortly after the Class Period at a price that vastly exceeded the share price at the end of the Class Period. ¶ 75.

Finally, in order to resolve all of these disputed issues regarding damages and loss causation, the Parties would have had to rely on expert testimony. As noted above, this creates further litigation risk because Lead Plaintiff could not be certain whether a jury would accept the view of its experts or of the well-qualified experts that Defendants would no doubt be able to present at trial. *See Facebook*, 2015 WL 6971424, at *5 ("[D]amages would be subject to a battle of the experts, with the possibility that a jury could be swayed by experts for Defendants, who could minimize or eliminate the amount Plaintiffs' losses. Under such circumstances, a settlement is generally favored over continued litigation.").

In short, these risks posed a real possibility that Lead Plaintiff and the Class would not be able to recover at all or would have recovered a lesser amount, if the Action proceeded through summary judgment, trial, and appeals. In light of these risks, Lead Plaintiff and Lead Counsel respectfully submit that it is in the best interests of the Class to accept the immediate and substantial benefit conferred by the Settlement.

2. The Settlement Represents a Substantial Percentage of Likely Recoverable Damages

Lead Plaintiff submits that the $54.5 million Settlement is also a very favorable result when considered in relation to the likely amount of damages that could be established at trial. Assuming that Lead Plaintiff prevailed on liability issues at trial (which was far from certain), the damages that Lead Plaintiff would be reasonably likely to be able to prove was approximately $190 million. ¶ 77. If Defendants succeeded with respect to certain other of their loss causation and damages arguments, damages would be reduced to approximately $82 million. *Id.* Accordingly, the

Settlement represents approximately 29% to 66% of the likely recoverable damages. Notably, however, if certain other of Defendants' loss causation and damages arguments had been accepted, damages could have been significantly lower than that amount, or eliminated entirely. *Id*. And, even if Lead Plaintiff were successful at trial, Defendants could have challenged the damages of each and every large class member in post-trial proceedings, substantially reducing any aggregate recovery. ¶ 79.

3. The Costs and Delays of Continued Litigation Support Approval of the Settlement

The substantial costs and delays that would be required before any recovery could be obtained through litigation also strongly support approval of the Settlement. Courts recognize that "[s]ecurities class actions are generally complex and expensive to prosecute." *In re Gilat Satellite Networks*, *Ltd*., 2007 WL 1191048, at *10 (E.D.N.Y. Apr. 19, 2007).

While this case settled after certification of the Class and after substantial document discovery had occurred, achieving a litigated verdict in the Action would have required substantial additional time and expense. In the absence of the Settlement, achieving a recovery for the Class would have required (i) the conclusion of fact discovery (including taking numerous depositions, of which four had already been scheduled and for which substantial preparations had already been made at the time the Settlement was reached); (ii) conducting complex and expensive expert discovery; (iii) briefing an expected motion for summary judgment; (iv) a trial on complex subject matter involving substantial fact and expert testimony; and (v) post-trial motions, including a contested individual claims procedure. Finally, whatever the outcome at trial, it is virtually certain that appeals would be taken from any verdict. The foregoing would pose substantial expense for the Class and delay the Class's ability to recover – assuming, of course, that Lead Plaintiff and the Class were ultimately successful on their claims.

In contrast to costly, lengthy, and uncertain litigation, the Settlement provides an immediate, significant, and certain recovery of $54.5 million for members of the Class.

4. All Other Factors Set Forth in Rule 23(e)(2)(C) Support Approval of the Settlement

Rule 23(e)(2)(C) also instructs courts to consider whether the relief provided for the class is adequate in light of "the effectiveness of any proposed method of distributing relief to the class, including the method of processing class-member claims;" "the terms of any proposed award of attorney's fees, including timing of payment;" and "any agreement required to be identified under Rule 23(e)(3)." Fed. R. Civ. P. 23(e)(2)(C)(ii)-(iv). Each of these factors also supports approval of the Settlement or is neutral and does not suggest any basis for inadequacy of the Settlement.

First, the procedures for processing Class Members' claims and distributing the proceeds of the Settlement to eligible claimants are well-established, effective methods that have been widely used in securities class action litigation. Here, the proceeds of the Settlement will be distributed to class members who submit eligible Claim Forms with required documentation to the Court-appointed Claims Administrator, Analytics Consulting, LLC. ("Analytics"). Analytics, an independent company with extensive experience handling the administration of securities class actions, will review and process the claims under the supervision of Lead Counsel, will provide claimants with an opportunity to cure any deficiencies in their claims or request review of the denial of their claim by the Court, and will then mail or wire claimants their *pro rata* share of the Net Settlement Fund (as calculated under the Plan of Allocation) upon approval of the Court.[7] This type of claims processing is standard in securities class actions and has long been used and

[7] The Settlement is not a claims-made settlement. If the Settlement is approved, Defendants will have no right to the return of any portion of Settlement based on the number or value of Claims submitted. *See* Stipulation ¶ 14.

found to be effective. Such claim filing and processing is necessary because neither Lead Plaintiff nor HeartWare possess individual investors' trading data that would allow the Parties to create a "claims-free" process to distribute Settlement funds.

Second, the relief provided for the Class in the Settlement is also adequate when the terms of the proposed award of attorney's fees are taken into account. As discussed in the accompanying Fee Memorandum, the proposed attorneys' fees of 24% of the Settlement Fund, to be paid upon approval by the Court, are reasonable in light of the efforts of Lead Counsel and the risks in the litigation. Most importantly with respect to the Court's consideration the fairness of the Settlement, is the fact that approval of attorneys' fees are entirely separate from approval of the Settlement, and neither Lead Plaintiff nor Lead Counsel may terminate the Settlement based on this Court's or any appellate court's ruling with respect to attorneys' fees. *See* Stipulation ¶ 17.

Lastly, the amended Rule 23 asks the court to consider the fairness of the proposed settlement in light of any agreements required to be identified under Rule 23(e)(3). *See* Fed. R. Civ. P. 23(e)(2)(C)(iv). Here, the only such agreement (other than the Stipulation itself) is the Parties' confidential Supplemental Agreement, which sets forth the conditions under which HeartWare would be able to terminate the Settlement if the number of Class Members who request exclusion from the Class reaches a certain threshold. This type of agreement is a standard provision in securities class actions and has no negative impact on the fairness of the Settlement.

D. The Settlement Treats Class Members Equitably Relative to Each Other

The proposed Settlement treats members of the Class equitably relative to one another. As discussed below in Part II, pursuant to the Plan of Allocation, eligible claimants approved for payment by the Court will receive their *pro rata* share of the recovery based on the transactions in HeartWare stock. Lead Plaintiff will receive precisely the same level of *pro rata* recovery (based on the Recognized Claim as calculated under the Plan of Allocation) as all other Class Members.

E. The Reaction of the Class to the Settlement

One factor set forth in *Grinnell* but not included in Rule 23(e)(2) that should be considered is the reaction of the Class to the proposed Settlement, which is an important factor to be weighed in considering its fairness and adequacy. *See, e.g.*, *In re Bear Stearns Companies, Inc. Sec., Derivative, & ERISA Litig*., 909 F. Supp. 2d 259, 266 (S.D.N.Y. 2012); *FLAG Telecom*, 2010 WL 4537550, at *16; *Veeco*, 2007 WL 4115809, at *7.

Pursuant to the Preliminary Approval Order, Analytics began mailing copies of the Notice Packet (consisting of the Notice and Claim Form) to potential Class Members and nominees on January 4, 2019. *See* Declaration of Michelle Kopperud Regarding (A) Mailing of Notice and Claim Form; (B) Publication of the Summary Notice; and (C) Report on Requests for Exclusion Received to Date (Ex. 1), at ¶¶ 2-4. As of March 8, 2019, Analytics had sent a total of 19,644 copies of the Notice Packet to potential Class Members and nominees. *See id*. ¶ 7. In addition, the Summary Notice was published in *The Wall Street Journal* and transmitted over the *PR Newswire* on January 22, 2019. *See id*. ¶ 8. The Notice set out the essential terms of the Settlement and informed potential Class Members of, among other things, their right to opt out of the Class or object to any aspect of the Settlement, as well as the procedure for submitting Claim Forms.

While the deadline set by the Court for Class Members to exclude themselves or object to the Settlement has not yet passed, to date, no objections to the Settlement or the Plan of Allocation and no requests for exclusion have been received. The deadline for submitting objections and requesting exclusion from the Class is March 22, 2019. As provided in the Preliminary Approval Order, Lead Plaintiff will file reply papers no later than April 5, 2019 addressing any requests for exclusion and objections that may be received.

* * *

In sum, all of factors to be considered under Rule 23(e)(2) support a finding that the Settlement is fair, reasonable, and adequate.

II. THE PLAN OF ALLOCATION IS FAIR AND REASONABLE AND SHOULD BE APPROVED

A plan for allocating settlement proceeds, like the settlement itself, should be approved if it is fair, reasonable and adequate. *See In re IMAX Sec. Litig.*, 283 F.R.D. 178, 192 (S.D.N.Y. 2012); *Bear Stearns*, 909 F. Supp. 2d at 270. A plan of allocation is fair and reasonable as long as it has a "rational basis." *FLAG Telecom*, 2010 WL 4537550, at *21; *In re Initial Pub. Offering Sec. Litig.*, 671 F. Supp. 2d 467, 497 (S.D.N.Y. 2009). Generally, a plan of allocation that reimburses class members based on the relative strength and value of their claims is reasonable. *See IMAX*, 283 F.R.D. at 192. A plan of allocation, however, need not be tailored to fit each and every class member with "mathematical precision." *In re PaineWebber Ltd. P'ship Litig.*, 171 F.R.D. 104, 133 (S.D.N.Y. 1997). In determining whether a plan of allocation is fair and reasonable, courts give great weight to the opinion of experienced counsel. *See Giant Interactive*, 279 F.R.D. at 163.

Here, the proposed plan of allocation (the "Plan of Allocation"), which was developed by Lead Counsel in consultation with Lead Plaintiff's damages expert, provides a fair and reasonable method to allocate the Net Settlement Fund among Class Members who submit valid Claim Forms. In developing the Plan of Allocation, Lead Plaintiff's damages expert calculated the amount of estimated artificial inflation in the price of HeartWare common stock which allegedly was proximately caused by Defendants' alleged false and misleading statements by considering the price changes in HeartWare common stock in reaction to the alleged corrective disclosures, adjusting for price changes attributable to market and industry factors. Notice ¶¶ 52-53.

Under the Plan of Allocation, a "Recognized Loss Amount" will be calculated for each purchase or acquisition of HeartWare common stock during the Class Period that is listed in the Claim Form and for which adequate documentation is provided. Notice ¶¶ 56-57. In general, the Recognized Loss Amount will be the difference between the estimated artificial inflation on the date of purchase and the estimated artificial inflation on the date of sale, or the difference between the actual purchase price and sales price of the stock, whichever is less. *Id*. ¶¶ 55, 57. Claimants who purchased and sold all their HeartWare shares before the first alleged corrective disclosure on September 1, 2015, or who purchased and sold all their HeartWare shares between two consecutive disclosure dates, will have no Recognized Loss Amount under the Plan of Allocation for those transactions because any loss suffered on those sales would not be the result of the alleged misstatements. *Id*. ¶ 55. The Plan of Allocation also limits Claimants based on whether they had an overall market loss in their transactions in HeartWare common stock during the Class Period. *Id*. ¶¶ 65-66.

Lead Counsel believes that the Plan of Allocation provides a fair and reasonable method to equitably allocate the Net Settlement Fund among Class Members who suffered losses as result of the conduct alleged in the Action. ¶ 95. Moreover, as noted above, as of March 8, 2019, more than 19,600 copies of the Notice, which contains the Plan of Allocation, and advises Class Members of their right to object to the Plan of Allocation, have been sent to potential Class Members and their nominees. *See* Kopperud Decl. ¶ 7. To date, no objections to the proposed Plan of Allocation have been received. ¶ 96.

III. NOTICE TO THE CLASS SATISFIED THE REQUIREMENTS OF RULE 23 AND DUE PROCESS

The Notice to the Class satisfied the requirements of Rule 23(c)(2)(B), which requires "the best notice that is practicable under the circumstances, including individual notice to all members

who can be identified through reasonable effort." Fed. R. Civ. P. 23(c)(2)(B); *see also Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 173-75 (1974). The Notice also satisfied Rule 23(e)(1), which requires that notice of a settlement be "reasonable" – *i.e.*, it must "fairly apprise the prospective members of the class of the terms of the proposed settlement and of the options that are open to them in connection with the proceedings." *Visa*, 396 F.3d at 114.

Both the substance of the Notice and the method of its dissemination to potential members of the Class satisfied these standards. The Court-approved Notice includes all the information required by Federal Rule of Civil Procedure 23(c)(2)(B) and the PSLRA, 15 U.S.C. § 78u-4(a)(7), including: (i) an explanation of the nature of the Action and the claims asserted; (ii) the definition of the Class; (iii) the amount of the Settlement; (iv) a description of the Plan of Allocation; (v) an explanation of the reasons why the Parties are proposing the Settlement; (vi) a statement indicating the attorneys' fees and costs that will be sought; (vii) a description of Class Members' right to opt-out of the Class or to object to the Settlement, the Plan of Allocation or the requested attorneys' fees or expenses; and (viii) notice of the binding effect of a judgment on Class Members.

As noted above, in accordance with the Court's Preliminary Approval Order, Analytics, the Court-approved Claims Administrator, began mailing copies of the Notice Packet to potential Class Members on January 4, 2019. *See* Kopperud Decl. ¶¶ 3-4. As of March 8, 2019, Analytics had disseminated 19,644 copies of the Notice Packet to potential Class Members and nominees. *See id*. ¶ 7. In addition, Lead Counsel caused the Summary Notice to be published in *The Wall Street Journal* and transmitted over the *PR Newswire* on January 22, 2019. *See id*. ¶ 8. Copies of the Notice, Claim Form, and Stipulation were made available on the settlement website maintained by Analytics beginning on January 4, 2019, and copies of the Notice and Claim Form were also made available on Lead Counsel's website. *See* Kopprud Decl. ¶ 10; Rizio-Hamilton Decl. ¶ 85.

This combination of individual mail to all Class Members who could be identified with reasonable effort, supplemented by notice in an appropriate, widely-circulated publication, transmitted over the newswire, and set forth on internet websites, was "the best notice . . . practicable under the circumstances." Fed. R. Civ. P. 23(c)(2)(B); *see, e.g.*, *In re Advanced Battery Techs.*, 298 F.R.D. 171, 182-83 (S.D.N.Y. 2014); *In re Marsh & McLennan Cos. Sec. Litig.*, 2009 WL 5178546, at *12-13 (S.D.N.Y. Dec. 23, 2009).

CONCLUSION

For the foregoing reasons, Lead Plaintiff respectfully requests that the Court approve the proposed Settlement and Plan of Allocation as fair, reasonable and adequate.

Dated: March 8, 2019

Respectfully submitted,

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