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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN FRANCISCO DIVISION

CAT BROOKS and RASHEED SHABAZZ, individually and on behalf of all others similarly situated,

Plaintiffs,

v.

THOMSON REUTERS CORPORATION,

Defendant.

Case No. 3:21-cv-01418-EMC

DEFENDANT THOMSON REUTERS' REPLY IN SUPPORT OF ITS MOTION TO EXCLUDE TESTIMONY OF FINANCE SCHOLARS GROUP, INC. (DR. TERRY LLOYD)

REDACTED - PUBLICLY FILED VERSION OF DOC. 177-2 PURSUANT TO COURT ORDER, DATED MARCH 30, 2023 (DOC. 190)

Date: April 20, 2023
Time: 1:30 p.m.
Place: Courtroom 5, 17th Floor
Judge: Hon. Edward M. Chen

I. INTRODUCTION

As Thomson Reuters ("TR") explained in its motion, in purporting to offer an opinion on methodology to calculate disgorgement in this case, Dr. Lloyd did not even attempt to undertake the pertinent inquiry. He disregarded clear and uniform legal authority holding that net profit (and not gross profit) is the proper measure of disgorgement, and he made no effort to subtract profit that is attributable to the unchallenged aspects of CLEAR. He then invented an *ad hoc* and unreliable method of calculating gross profit that nobody else in his field seems to have used. Making matters worse, he allocated TR's revenue to California based on variables that have nothing to do with TR's sales.

Plaintiffs' response is that the Court need not address these issues now, and that if it does, it should simply defer to Dr. Lloyd because he is an experienced accountant. But the Court must address the admissibility of Dr. Lloyd's opinion at class certification and must assess *for itself* whether that testimony is relevant and reliable. Because it is not, Dr. Lloyd's opinion should be excluded.

II. DR. LLOYD'S OPINION IS INADMISSIBLE BECAUSE HE DID NOT ATTEMPT TO UNDERTAKE THE PERTINENT INQUIRY.

The proper measure of disgorgement in California and under the Restatement is the defendant's "net profit attributable to the underlying wrong." *Am. Master Lease LLC v. Idanta Partners, Ltd.*, 225 Cal. App. 4th 1451, 1491 (2014) (quoting Restatement (Third) of Restitution and Unjust Enrichment § 51(4) (Am. L. Inst. 2011)), *as modified* (May 27, 2014). Despite this clear guidance, Dr. Lloyd calculated gross profit, not net profit, and made no effort to isolate only the profit attributable to the alleged wrong. Because Dr. Lloyd did not conduct "the pertinent inquiry," his testimony is inadmissible. *Daubert v. Merrell Dow Pharms., Inc.*, 509 U.S. 579, 591-92 (1993).

A. Dr. Lloyd's failure to conform his model to California law cannot be ignored at class certification.

Plaintiffs suggest that Dr. Lloyd's failure to create a model that is consistent with California law is a merits issue that is not relevant at class certification, and that Dr. Lloyd can cure these deficiencies by offering a new methodology at the merits stage. *See* Doc. 167-3 ("Opp.") at 10. Plaintiffs are incorrect. At *class certification*, a plaintiff must provide a model for awarding monetary relief that is consistent with the plaintiff's theory of liability. *Comcast Corp. v. Behrend*, 569 U.S. 27, 35 (2013); *see* Opp. at 4 (conceding same). Thus, the court must assess at class certification whether the plaintiff's proposed model is "consistent with its liability case . . . *even when that requires inquiry into the merits of the claim*." *Comcast*, 569 U.S. at 35 (emphasis added). Plaintiffs' argument that the Court need not address the mismatch between California law and Dr. Lloyd's analysis because TR did not "argue that estimating net profits for purposes of classwide disgorgement is an impossible task" also misses the mark. *See* Opp. at 1. The question is not whether it is theoretically possible to produce a disgorgement model consistent with California law; it is whether Plaintiffs have done so. *See Comcast*, 569 U.S. at 36. They have not.

B. Dr. Lloyd's opinion is inadmissible because his model is designed to estimate TR's gross profit instead of its net profit.

"Gross profit and net profit are different things." Doc. 157-07 ("Lloyd Dep.") at 56:12-13. Both experts agree on this distinction, and decades of California precedent–including the cases Dr. Lloyd cites–is in accord. *See* Mot. at 6-8. California law and the Restatement provide that *net* profit is the proper measure of disgorgement, meaning all costs of producing the revenue–not just the costs of goods sold–must be deducted. *See id.* Despite this overwhelming consensus, Dr. Lloyd admits that his model estimates gross profit instead of net profit. Lloyd Dep. at 57:21-58:2 ("Q: And in this case, did you calculate gross profits for CLEAR or net profits for CLEAR? A: We calculated the gross profits as I describe."); *see also* Mot. at 7; Opp. at 6 ("Lloyd measured the relevant gross profit").

Plaintiffs have been unable to muster a single case holding that gross profit is the proper measure of disgorgement, and though they contend that the authority TR cited "does not account for the more nuanced guidance from the Restatement," Opp. at 10, that assertion is plainly incorrect because the authority on which TR relies *quotes from and interprets the Restatement*. *See, e.g.*, *Am. Master Lease*, 225 Cal.App.4th at 1487-88, 1491-92.

In the absence of legal authority, Plaintiffs resort to suggesting that Dr. Lloyd is entitled to decide for himself the meaning of California law–or at least that the meaning of California law is a factual matter for the experts to debate at trial. *See* Opp. at 10. But the proper measure of profit for an unjust enrichment claim is a *legal* issue for the Court to decide, and a matter on which the Court will need to instruct the jury. *See, e.g.*, California Civil Jury Instruction 4410 Unjust Enrichment for Misappropriation of Trade Secrets ("subtract . . . [name of defendant]'s reasonable expenses, including the value of the [specific categories of expenses in evidence, such as labor, materials, rents, interest on invested capital]"); Ninth Circuit Model Civil Jury Instruction 17.34 Copyright–Damages–Defendant's Profits ("The defendant's profit is determined by [deducting] [subtracting] all expenses from the defendant's gross revenue."). As TR demonstrated earlier, the Court must determine at class certification whether Plaintiffs' damages model is consistent with their theory of liability. *See* Section II(A). To do so, the Court must first identify the governing law.

C. Dr. Lloyd's opinion is inadmissible because his model does not even attempt to isolate only the profit attributable to the alleged wrong.

In addition to failing to calculate net profit, Dr. Lloyd's opinion should be excluded because his model does not make any attempt to isolate only the profit attributable to the alleged wrong. Plaintiffs contend that Dr. Lloyd was not required to do so because it is TR's burden to demonstrate costs and because CLEAR would be "worthless without the underlying [California] data." *See* Opp. at 10. Neither argument is persuasive.

California adopted the legal standard from the Restatement, which assigns "the *claimant* . . . the burden of producing evidence from which the court may make at least a reasonable approximation of the defendant's unjust enrichment." *Am. Master Lease*, 225 Cal.App.4th at 1487-88 (emphasis added). Once the plaintiff meets this threshold burden, the defendant is "free . . . to introduce evidence tending to show that the true extent of unjust enrichment is something less." *Id.* at 1488. California adopted this framework instead of the framework in the copyright context where "the claimant has the burden of proving revenues and the defendant has the burden of proving deductions." *Id.* at 1487. Thus, Plaintiffs bore the initial burden of identifying at least a reasonable approximation of only the profit attributable to the alleged wrong. Because Dr. Lloyd admits that he did not even attempt to do so, Plaintiffs did not carry that burden. *See* Mot. at 9; *Comcast*, 569 U.S. at 35 (reversing class certification because the plaintiffs' damages expert "[did] not even attempt" to "measure only those damages attributable to [their] theory" of liability).

Plaintiffs' second argument–that they were not required to provide a reasonable approximation of only the profit attributable to the alleged wrong because CLEAR would be "worthless" without information about Californians–is equally unavailing. Plaintiffs do not cite any authority for the proposition that the fact that a particular component of a product is important–or even essential–means that all of the profit earned from that product is attributable to that component.

Plaintiffs' theory is not only unsupported by precedent, but also contrary to the Restatement and common sense. Imagine a lawsuit exactly like this one, except instead of complaining about collecting and sharing information, a plaintiff complained about an automobile manufacturer including gas tanks in its vehicles. While a car might be "worthless" without a gas tank, it does not follow that 100% of the manufacturer's profits were attributable to the gas tank. Many components of a vehicle are essential (e.g., the brakes, the drivetrain, the steering wheel), and if any one of them were removed the product would be "worthless," but each one of them cannot be responsible for 100% of the profits. And many non-essential components, like air conditioning or a navigation system, plainly contribute to the manufacturer's profits too. The same is true here; CLEAR is like the car, and the many essential components of CLEAR (e.g., the organization of the data, the search function, etc.) are like the brakes and the steering wheel. Even if CLEAR would be "worthless" without information about Californians, it would be equally "worthless" without other essential components of the product. CLEAR would not have generated revenue, for instance, if TR did not organize the information and maintain an effective search function and user interface. *See* Doc. 151-17 ("Kidder Rep.") at 19-20.

Recognizing this commonsense principle, the Restatement provides that one must assess what portion of the net profit "is properly attributable to the underlying wrong" and what portion is "the product of legitimate contributions by the defendant that should not, in justice, be awarded to the claimant." Restatement § 51 cmt. *f.* Nothing in the Restatement says that a plaintiff is entitled to all of the profits if he complains about an important or essential component of a product. *See also Sheldon v. Metro-Goldwyn Pictures Corp.*, 309 U.S. 390, 397-98, 408-09 (1940) (affirming conclusion that no more than 20% of the film's profits were attributable to the copied story).

Since Dr. Lloyd admits that his model does not even attempt to estimate net profit attributable to the underlying wrong, which is the only acceptable measure of disgorgement in California, his opinion is irrelevant, and it should be excluded. *See Oracle Am., Inc. v. Google, Inc.*, No. C 10-03561 WHA, 2016 WL 2342365, at *7 (N.D. Cal. May 3, 2016) (excluding Oracle's expert's testimony because his model "simply ignore[d] the numerous critical non-infringing elements of Android to which some of the profits should be apportioned").

III. DR. LLOYD HAS NOT DEMONSTRATED THAT HIS METHODS WERE RELIABLE.

A. Dr. Lloyd has not identified any external source that validates his *ad hoc* method of calculating gross profit.

Even if gross profit *were* the proper measure of disgorgement, Dr. Lloyd's novel method of calculating it is unreliable. *See* Mot. at 9-11. For the revenue side of his analysis, Dr. Lloyd included *all* revenue TR earned from CLEAR over the relevant period, while for the cost side he deducted only costs that vary per search. *See id.* Dr. Lloyd did not cite any authority recognizing this mixing and matching as a reliable method of calculating gross profit, and, despite what Plaintiffs claim, his say-so is not enough. *See Daubert v. Merrell Dow Pharms.*, 43 F.3d 1311, 1319 (9th Cir. 1995) ("*Daubert II*") (excluding expert testimony because plaintiffs were unable to "point to any external source to validate [the] methodology" and instead presented the court with "only the experts' qualifications, their conclusions, and their assurances of reliability").

It is unsurprising that Plaintiffs were unable to find any independent support for Dr. Lloyd's bespoke method of calculating gross profit because it is nonsensical. Dr. Lloyd reasons that if the only cost of an additional search is a transactional royalty fee, then transactional royalty fees are the only costs TR incurred in producing the revenue *over the entire four-year period*. But that is plainly incorrect. For example, TR has paid a flat-rate royalty to the [redacted].[1] *See* Kidder Rep. at 30-31. If Plaintiffs had their way and TR were unable to provide access to *any* information about Californians (including this information that is required to be made available upon request by statute), then TR would save the flat-rate royalty costs it incurs to license that information. That those costs do not vary by search does not mean that one can pretend they do not exist. As another example, the fact that TR's sales representatives' salaries do not vary per search does not mean that TR did not incur any sales costs attributable to California over the four-year period Dr. Lloyd examined. Plaintiffs have not identified any authority to support Dr. Lloyd's methodology.

Plaintiffs attempt to paper over the lack of support for Dr. Lloyd's method by citing two cases, neither of which were relied upon by Dr. Lloyd, and neither of which endorse his novel approach. In *Brown v. Google*, No. 20-CV-3664-YGR, 2022 WL 17961497, at *1 (N.D. Cal. 2022), the plaintiffs contended that Google's tracking of the web-browsing of individuals using Google Chrome's "Incognito Mode" was unlawful. Google earned revenue from this practice by serving targeted advertisements to these individuals. *Id.*[2] When estimating Google's net profit from those advertisements the plaintiffs' expert did not deduct any costs because a separate plaintiffs' expert and two Google witnesses testified that Google did not incur costs in serving targeted advertisements to those using Incognito mode. *Id.* at *6. The court held that the expert's decision not to deduct costs was reasonable under the circumstances, and that a factual dispute raised by a third Google witness about whether Google actually incurred costs would need to be resolved at trial. *Id.* at *7. The key difference between *Brown* and this case is that everyone in *Brown* agreed that if Google *did* incur costs in tracking individuals using Incognito mode and serving them advertisements, they would need to be deducted. In other words, everyone in *Brown*

[1] Section 102230(c)(5) of California's Health & Safety Code provides that this information "shall be made available to financial institutions . . . [their] representatives or contractors, consumer credit reporting agencies . . . [their] representatives or contractors, [and] those entities providing information services for purposes of law enforcement or preventing fraud."

[2] The court incorporated by reference this background from a previous order. *See Brown v. Google*, No. 20-CV-03664-LHK, 2021 WL 6064009, at *3 (N.D. Cal. 2021).

agreed with TR (and the Restatement) that *all* costs a defendant incurs in producing the revenue must be deducted. *See* Restatement § 51 cmt. *h* (providing that one must deduct "all marginal costs incurred in producing the revenues that are subject to disgorgement"). That is why both experts and the court in *Brown* examined all costs "associated with Google generating revenue," including those that did not vary with each advertisement served, like the cost of "maintaining the advertising infrastructure." *Brown*, 2022 WL 17961497 at *6-7.

Plaintiffs' citation to *In re Actiq Sales & Marketing Practices Litigation*, No. 07–4992, 2014 WL 3572932 (E.D. Pa. 2014), fares no better. In that case, the plaintiffs claimed that the defendant's sale of a drug was unlawful and the parties' experts attempted to estimate the net profit attributable to those sales. *See id.* at *1-2, *7-9. The plaintiffs' expert–the one Plaintiffs contend endorses Dr. Lloyd's new method–agreed *with TR's position* that the expert's task in estimating net profit is to subtract *all* "costs that would specifically go away if the product went away." *Id.* at *8 n.12. Sunk costs or costs that the business would bear even if the product went away, like a CEO's salary, would not be deducted, but other costs that *would* go away must be deducted, even if they did not vary with each unit sold. *Id.* Thus, the plaintiffs' expert deducted numerous costs that did not vary with each sale of Actiq, including "marketing expenditures, field sales costs," and "clinical trials and regulatory costs." *Id.* at *5. Dr. Lloyd did not deduct any costs like these. Indeed, he did not deduct a cent for sales or marketing expenses because he claims that simply ignoring any costs that did not vary per search is an appropriate method of calculating gross profit. Doc. 127-12 ("Lloyd Rep.") at 14-17. *Actiq* does not support that proposition–nor does any other authority.

Plaintiffs' failure to identify any authority endorsing Dr. Lloyd's novel method of mixing and matching total revenue over the four-year period while deducting only costs that varied per search, means that they failed to meet their burden of demonstrating that Dr. Lloyd's method of calculating gross profit is "practiced by (at least) a recognized minority of [experts] in [his] field," and thus Dr. Lloyd's testimony is inadmissible.[3] *Daubert II*, 43 F.3d at 1319.

[3] Plaintiffs attempt to distract from the lack of support for Dr. Lloyd's approach by contending that TR has not demonstrated that it is unreliable. *See, e.g.*, Opp. at 6 n.5. That is incorrect, but it is also irrelevant, as it is Plaintiffs' burden to demonstrate that Dr. Lloyd's method is reliable, not TR's

B. Dr. Lloyd has not demonstrated that his method of allocating revenue to California is reliable.

Dr. Lloyd's method of apportioning revenue to California is also unreliable because he did so based on an average of California's share of U.S. GDP in 2021 and California's share of U.S. arrests from 2018 without ever explaining or demonstrating why those variables have anything to do with TR's revenue from CLEAR. *See* Mot. at 10-11. Plaintiffs double down on Dr. Lloyd's assertion that he was trying to assess "what data was actually of interest to CLEAR subscribers," Opp. at 2 n.1, but he never analyzed or explained why an average of California's shares of GDP and national arrests answers that question. *See* Mot. at 10-11. While experts may make reasonable assumptions, they must explain *why* their assumptions are reasonable. Simply making an assumption without any explanation or supporting analysis does not suffice. *Gen. Elec. Co. v. Joiner*, 522 U.S. 136, 144 (1997) ("[N]othing in either *Daubert* or the Federal Rules of Evidence requires a district court to admit opinion evidence that is connected to existing data only by the *ipse dixit* of the expert."); *see also Oracle Am.*, 2016 WL 2342365, at *7 (excluding expert testimony based on assumption that Google's revenue would grow at the same rate from 2011 through 2015 as it had in 2009 and 2010 without any analysis justifying the assumption).

IV. CONCLUSION

In the end, Dr. Lloyd did not even attempt to undertake the pertinent inquiry. He disregarded clear and uniform legal authority holding that net profit (and not gross profit) is the proper measure of disgorgement, and he made no effort to subtract profit that is attributable to the unchallenged aspects of CLEAR. He then devised an *ad hoc* and unreliable method of calculating gross profit that is not used by others in his field. This irrelevant and unreliable testimony is precisely what *Daubert* is designed to avoid, and it should not be admitted.

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burden to demonstrate it is not. *Daubert*, 509 U.S. at 592 n.10.

Dated: March 20, 2023

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