

[Securities Regulation Daily Wrap Up, TOP STORY—U.S.: Issue of generic nature of statements at class certification sent back to Second Circuit, \(Jun. 21, 2021\)](#)

Securities Regulation Daily Wrap Up

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The generic nature of a misrepresentation is important evidence of price impact that should be considered at the class certification stage.

The Supreme Court has issued an opinion in the *Goldman Sachs* case confirming that the generic nature of an alleged misrepresentation is important evidence of price impact. At issue was the rebuttal of the *Basic* presumption in class actions premised on the inflation-maintenance theory. Since the parties no longer disputed whether the generic nature of the alleged misrepresentations was relevant to price impact, the only disagreement was whether the Second Circuit properly considered the nature of Goldman Sachs's statements. It was unclear to the court whether the Second Circuit did so; as a result, the court vacated the judgment and remanded it for the Second Circuit to consider all record evidence relevant to price impact. Justice Barrett delivered the opinion, in which Justices Roberts, Breyer, Kagan and Kavanaugh joined in full ([Goldman Sachs Group, Inc. v. Arkansas Teacher Retirement System](#), June 21, 2021, Barrett, A.).

At issue before the Court was *Basic*'s rebuttable presumption of reliance based on the fraud-on-the-market theory. The presumption may be rebutted by, as held in *Halliburton II*, showing that the alleged misrepresentation had no impact on the market price of the stock. In this case, the plaintiffs relied on the "inflation maintenance" theory, alleging that Goldman's repeated misrepresentations in SEC filings and annual reports about its business practices prevented the inflation from dissipating. For its part, Goldman asserted that the statements at issue were generic and aspirational and sought to rebut the *Basic* presumption by showing a lack of price impact. The Supreme Court [granted certiorari](#) on December 11, 2020.

Two tries to certify. The district court certified the class, concluding that the *Basic* presumption applied because there was no real dispute that the market for Goldman's stock was efficient and because the plaintiffs demonstrated an obvious link between the release of information revealing the misstatements to the market and the subsequent drop in stock price. On interlocutory appeal, however, the Second Circuit vacated and remanded after concluding that the district court had not properly applied the preponderance-of-the-evidence standard under the Supreme Court's 2014 *Halliburton II* opinion. On remand, the district court again [certified](#) the class, and this time a divided panel of the Second Circuit [affirmed](#). The court rejected Goldman Sachs's effort to rebut the *Basic* presumption by pointing to the generic and aspirational nature of the alleged misstatements in an attempt show that the statements had no impact on the price of the security.

Remand to consider price impact record. Before the Supreme Court, [Goldman](#) argued that the Second Circuit erred by holding that the generic nature of the alleged misrepresentations was irrelevant to the price impact query. As the briefing proceeded, and by the time [oral argument](#) occurred, the parties came to agree that the nature of the statements was important evidence of price impact—as Justice Barrett put it, the "dispute has largely evaporated." The parties (and the Court) agreed that the generic nature of an alleged misrepresentation is important evidence of price impact, particularly in cases proceeding under an inflation maintenance theory. If an earlier alleged misrepresentation is generic and the later corrective disclosure is specific, it is less likely that the disclosure corrected the generic misrepresentation, and there is also less reason to infer price impact. In a footnote, Justice Barrett observes that while some appellate courts accept it, the validity or contours of the inflation-maintenance theory were not before the court.

The only remaining disagreement, then, was whether the Second Circuit properly considered the generic nature of Goldman's alleged misrepresentations. The Court concluded that the Second Circuit's opinions left sufficient doubt on this question to require remand for consideration of "*all* [emphasis in original] record evidence relevant to price impact, regardless whether that evidence overlaps with materiality or any other merits issue."

With the exception of Justice Sotomayor, all of the justices joined in this holding. In her dissent to this portion of the opinion, Justice Sotomayor explained that in rejecting Goldman's (later abandoned) argument that generic statements cannot have a price impact, the Second Circuit did not hold that the generic nature of an alleged misstatement cannot serve as evidence of price impact. Nothing in the Second Circuit's opinion misstates the law, she said, and affirmance is appropriate under these circumstances.

Burden of persuasion. The second question presented in this case concerned the burden of persuasion on price impact at class certification. Goldman argued here that the Second Circuit erred by requiring Goldman to bear the burden of persuasion on price impact at class certification. According to Goldman, Federal Rule of Evidence 301 applies to the Basic presumption at class certification. So, once a defendant discharges its burden of production and rebuts the presumption, the plaintiff must carry the burden of persuasion to show price impact.

The majority disagreed with Goldman's interpretation of the rule, stating that the Court has the authority to assign defendants the burden of persuasion to prove a lack of price impact. The issue then, was whether that authority was exercised in establishing the *Basic* framework pursuant to the securities laws: "*Basic* and *Halliburton II* did just that," the court said. These cases refer to a defendant's "showing" that a misrepresentation did not affect the stock price. This "showing," Justice Barrett wrote, goes beyond mere production of evidence because the defendant must sever the link between a misrepresentation and the price, and mere evidence would rarely accomplish this. Therefore, the best reading of the Court's precedents is that the defendant bears the burden of persuasion to prove a lack of price impact—the opinion acknowledges that the allocation of this burden "is unlikely to make much difference on the ground."

The Court accordingly held that the Second Circuit correctly put the burden of proving a lack of price impact on Goldman. As noted above, since it was not clear that the Second Circuit considered the generic nature of the alleged misrepresentations in reviewing the district court's price impact determination, the judgment of the Second Circuit was vacated, and the case remanded for further proceedings.

Gorsuch dissents on burden of persuasion. Justice Gorsuch, joined by Justices Thomas and Alito, dissented from the portion of the opinion holding that the defendant bears the burden of persuasion on price impact. The dissent argued that the references to "showing" refer only to the defendant's burden of production. Traditionally, presumptions operate by shifting the burden of production to the defendant to rebut the presumption—the burden of persuasion, however, never shifts from the plaintiff. In the 30 years since *Basic*, Justice Gorsuch wrote, the Court has never even suggested that plaintiffs are relieved from carrying the burden of persuasion, and the majority relied on a "handful of words" to create "spliced clauses" that "cannot begin to carry the weight the Court assigns them."

The case is [No. 20-222](#).

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