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The Supreme Court Agrees to Hear Appeal on Defendants' Ability to Rebut the *Basic* Presumption of Reliance at Class Certification

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On December 11, 2020, the U.S. Supreme Court granted a petition for writ of certiorari in the case *Goldman Sachs Group, Inc., et al., Petitioners v. Arkansas Teacher Retirement System, et al.*, No. 20-222. The certiorari petition asked the Court to decide whether a defendant in a securities class action may rebut the presumption of classwide reliance that sometimes exists in federal securities cases by pointing to the generic nature of the underlying alleged misrepresentations and thereby show that the statements at issue had no ability to impact the trading price of the security.

Overview of the Presumption of Reliance

In 1988, the Supreme Court held in *Basic, Inc. v. Levinson* that, if certain conditions were satisfied, plaintiffs in putative securities class actions may invoke a presumption of classwide reliance on the alleged misrepresentations pled in the case to satisfy the requirement for class certification that common issues must predominate.[1] One of the requirements to invoke this presumption is the existence of an "efficient" trading market for the stock at issue. The *Basic* Court reasoned that in an efficient market, all material information available to the public about a company should be reflected in the trading price of its stock, and so purchasers of securities are presumed to have relied on all publicly available information about a company (including any alleged misstatements) if they relied on the market price in making their investing decisions.

Today, this concept – known as the "fraud on the market" theory – is routinely invoked by plaintiffs in securities class actions to certify a class of investors who can pursue federal securities law claims. The availability of the presumption of reliance is critical because without its existence, no class of investors could ever be certified. Individualized reliance issues would always predominate because actual reliance on the alleged misstatements is a required element of a private securities fraud claim. In addition to sanctioning the use of the presumption of reliance, *Basic* also held that defendants may rebut the presumption, and thereby

[1] 485 U.S. 224 (1988).

defeat class certification, through "[a]ny showing that severs the link between the alleged misrepresentation and either the price received (or paid) by the plaintiff, or his decision to trade at a fair market price…."[2]

Several years later, the Supreme Court reaffirmed in *Halliburton v. Erica P. John Fund, Inc.* ("*Halliburton II*") that defendants must be given the opportunity at the class certification stage to attempt to rebut the *Basic* presumption and that defendants can do so by showing that the alleged misrepresentations had no impact on the trading price of the securities at issue.[3] The *Halliburton II* Court did not, however, specifically address the question that is now squarely before the Court in *Goldman* – namely, what type of evidence on the absence of price impact would be sufficient to rebut the presumption. In the absence of guidance from the Supreme Court on this point, the lower courts have largely found that the evidence on price impact offered by defendants is either insufficient to rebut the presumption or cannot be considered at class certification.

Summary of the *Goldman* Case on Appeal

The *Goldman* appeal arises out of a 2011 securities class action brought against Goldman Sachs Group, Inc. and three of its executives in the U.S. District Court for the Southern District of New York. The plaintiffs alleged that the company's aspirational statements concerning its procedures and controls designed to identify potential conflicts of interest were false and misleading and that those statements artificially "inflated" Goldman's stock price until certain conflicts were allegedly revealed to the market.

After the district court twice certified the shareholder class, and on the second appeal to the Second Circuit, a divided three-judge panel affirmed the order granting class certification.[4] The majority rejected Goldman's attempt to rebut the *Basic* presumption based on an argument that the alleged misstatements were too generic to have impacted share price, which the majority found was a question of materiality common to all class members and therefore not properly before the court at class certification. In addition, the majority relied on the Supreme Court's prior decision in *Amgen*, which held that a plaintiff need not prove the materiality of the alleged misstatements to prevail at class certification.[5]

Judge Sullivan dissented, arguing that Goldman had presented "persuasive and uncontradicted evidence" to rebut the *Basic* presumption and that such evidence must be considered at class certification under *Halliburton II*, even if it was also relevant at the merits stage to materiality.[6] Under the majority's decision, Judge Sullivan concluded, the *Basic* presumption would be "truly irrebuttable."

Goldman filed a petition for a writ of certiorari with the U.S. Supreme Court in August 2020, arguing that the Second Circuit's decision "effectively strips defendants of any ability to rebut the *Basic* presumption in class actions…."The holding, Goldman argued, would all but guarantee certification whenever shareholder plaintiffs argue that the share price "had been improperly maintained by boilerplate aspirational statements that nearly all companies make." Goldman's petition was supported by a number of amici industry groups

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2 *Id.* at 248.

3 573 U.S. 258 (2014).

4 *Ark. Teacher Ret. Sys. v. Goldman Sachs Grp., Inc.*, 955 F.3d 254 (2d Cir. 2020). Judges Richard C. Wesley, Denny Chin, and Richard J. Sullivan sat for the panel, with Judge Wesley authoring the majority opinion and Judge Sullivan dissenting.

5 *Amgen Inc. v. Conn. Ret. Plans & Tr. Funds*, 568 U.S. 455 (2013).

6 *Id*. at 275.

that foreshadowed the potentially deleterious impact of the Second Circuit's holding, which, they argued, would create undue pressure on defendants to settle even meritless claims.

Potential Impact of the Court's Ruling

The Court's grant of Goldman's certiorari petition is significant for several reasons. As noted above, the Court in *Halliburton II* said that defendants must be given the opportunity to rebut the presumption of reliance at class certification, but then gave no guidance as to what type of evidence would be sufficient. In the wake of *Halliburton II*, other decisions from the Supreme Court such as *Amgen* have been used successfully by plaintiffs to argue that certain types of evidence directly relevant to an absence of price impact cannot be considered at class certification. It often happens in securities cases that certain facts can be relevant to more than one element of a securities fraud claim. Even though the Supreme Court said in *Amgen* that a plaintiff does not have to prove materiality at the class certification stage, the Court never said in *Amgen* (or any decision since then) that evidence of no price impact, which might also illustrate a lack of materiality, cannot be considered if offered to rebut the presumption. Rather, *Halliburton II* seems to make clear that a defendant many offer any "salient evidence showing that an alleged misrepresentation did not actually affect the stock's price."[7]

As things stand currently, it is very difficult for defendants to successfully rebut the presumption of reliance, and we think it is a positive development that the Court wishes to hear this appeal. It is clear from *Basic* and *Halliburton II* that the Court meant for the presumption of reliance to be "rebuttable," not impenetrable. The practical reality is, however, that the presumption is almost never rebutted because district courts are often not willing to consider compelling evidence of a lack of price impact submitted by defendants based on the notion that there is a perceived overlap with the underlying "merits" of the claim, which they conclude means that such matters are for another day. Of course that day never comes for most companies that feel the pressure to settle rather than litigate meritorious defenses in the wake of a certification decision. The Supreme Court now has the opportunity with the Goldman appeal to provide much-needed guidance to the lower courts that will hopefully change the dynamics at class certification such that there will be a more rigorous examination of all evidence potentially relevant to price impact, which would be consistent with the Court's prior directives in *Basic* and *Halliburton II*.

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7 *Halliburton II*, 573 U.S. at 263.

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