Simpson Thacher

Memorandum

Second Circuit De-Certifies Class in Long-Running *Goldman* Securities Price Impact Dispute

August 17, 2023

On August 10, 2023, the Second Circuit vacated a Southern District of New York court order certifying a Goldman Sachs' investor class in a securities fraud class action brought under Section 10(b), applying the guidance recently set forth by the Supreme Court in *Goldman Sachs Group v. Arkansas Teacher Retirement System*, 141 S. Ct. 1951 (2021) (Barrett, J.). The Second Circuit's decision provides guidance going forward as to when a defendant has rebutted the presumption of reliance established in *Basic v. Levinson*, 485 U.S. 224 (1988).

In seeking to certify a securities fraud shareholder class, plaintiff stockholders relied on stock price inflation-maintenance theory, asserting that certain alleged generic misrepresentations—such as "Integrity and honesty are at the heart of our business"—caused the bank's stock price to remain inflated until detail about certain conflicts of interest was revealed in subsequent media coverage and other disclosures, causing the bank's stock price to fall. Defendants have sought to defeat class certification by rebutting the presumption of reliance established in *Basic* with evidence that the alleged misrepresentations had no stock price impact.

This case has a long and winding procedural history. After the district court first certified the plaintiff class in September 2015, that decision and two subsequent class certification decisions have been appealed to the Second Circuit with one going up to the Supreme Court.[1] In 2021, the Supreme Court vacated the Second Circuit's affirmance of the district court's second class certification decision. The Supreme Court unanimously held that a court must consider all probative evidence, including the nature of the alleged misrepresentations, in assessing price impact at the class certification stage, and cautioned that the "final inference—that the back-end price drop equals front-end inflation—starts to break down when there is a mismatch between the contents of the misrepresentation and the corrective disclosures." An eight-justice majority of the Court further held that it was not clear that the Second Circuit properly considered the generic nature of the alleged misrepresentations at issue and for that reason vacated and remanded back to the Second Circuit, with instructions to take into account "all record evidence relevant to price impact, regardless [of] whether that evidence overlaps with materiality or any other merits issue." *Goldman Sachs Grp., Inc. v. Ark. Tchr. Ret. Sys.*, 141 S. Ct. 1951 (2021). Following the

[1] During the course of the case, Simpson Thacher filed amici curiae briefs on behalf of the Securities Industry and Financial Markets Association, the U.S. Chamber of Commerce, the Bank Policy Institute, the American Bankers Association, and the American Property Casualty Insurance Association in support of defendants-appellants.

Supreme Court's decision in *Goldman*, the Second Circuit vacated the district court's class certification order and remanded for further proceedings.

For a third time the district court certified the plaintiff class, finding that defendants had not rebutted the *Basic* inference of price impact. The district court found that to measure whether an alleged misstatement impacted stock price, the impact of the alleged misstatement must be compared with the impact as if the company had made a "truthful, contrary" statement. Relying on plaintiffs' expert, the court concluded that such a truthful contrary statement is "precisely what happened" when the details of Goldman's conflicts of interest emerged and the stock price dropped.

Defendants again filed a Rule 23(f) petition for appeal, which the Second Circuit granted. In its August 2023 opinion, the Second Circuit reversed the district court's order and remanded with instructions to decertify the class, concluding that the district court failed to properly apply the Supreme Court's mismatch framework. The Second Circuit found that when determining what impact a truthful disclosure would have had in comparison with the alleged misstatement, the "truthful substitute" for the alleged misstatement "should align in genericness with the alleged misrepresentation." The district court erred by measuring the detailed disclosures against the generic misstatements. Rather, the court should have asked what would have happened to the stock price had the company spoken truthfully "at an *equally generic level*." Alternatively, where a corrective disclosure expressly identifies or implicates particular prior misstatements such that "the truthful substitute for the lie was identified by the corrective disclosure itself," price impact may be found with less alignment on the statement's specificity, but this was not applicable to the statements and disclosures at issue in the underlying decision.

Going forward, the Second Circuit instructed that a "searching price impact analysis" must be conducted in cases such as the instant case where: (1) there is a considerable gap in front-end–back-end genericness; (2) the corrective disclosure does not directly refer to the alleged misstatement; and (3) the plaintiff claims that a company's generic risk-disclosure was misleading by omission. Courts must consider "the generic nature of both the misstatements and corrective disclosures, whether they match in specificity, and, if not, whether truthful, equally generic substitutes for the challenged statements would have impacted the stock price."

For further information regarding this memorandum, please contact one of the following:

CONTACTS

Martin S. Bell
+1-212-455-2542
martin.bell@stblaw.com

Stephen P. Blake
+1-650-251-5153
sblake@stblaw.com

Michael J. Garvey
+1-212-455-7358
mgarvey@stblaw.com

Bo Bryan Jin
+1-650-251-5068
bryan.jin@stblaw.com

Meredith Karp
+1-212-455-3074
meredith.karp@stblaw.com

Peter E. Kazanoff
+1-212-455-3525
pkazanoff@stblaw.com

Chet A. Kronenberg
+1-310-407-7557
ckronenberg@stblaw.com

Laura Lin
+1-650-251-5160
laura.lin@stblaw.com

Linton Mann III
+1-212-455-2654
lmann@stblaw.com

Joseph M. McLaughlin
+1-212-455-3242
jmclaughlin@stblaw.com

Lynn K. Neuner
+1-212-455-2696
lneuner@stblaw.com

Joshua Polster
+1-212-455-2266
joshua.polster@stblaw.com

Rachel S. Sparks Bradley
+1-212-455-2421
rachel.sparksbradley@stblaw.com

Alan C. Turner
+1-212-455-2472
aturner@stblaw.com

Craig S. Waldman
+1-212-455-2881
cwaldman@stblaw.com

Alicia N. Washington
+1-212-455-6074
alicia.washington@stblaw.com

George S. Wang
+1-212-455-2228
gwang@stblaw.com

Jonathan K. Youngwood
+1-212-455-3539
jyoungwood@stblaw.com

David Elbaum
+1-212-455-2861
david.elbaum@stblaw.com

Janet A. Gochman
+1-212-455-2815
jgochman@stblaw.com

Simona G. Strauss
+1-650-251-5203
sstrauss@stblaw.com

The contents of this publication are for informational purposes only. Neither this publication nor the lawyers who authored it are rendering legal or other professional advice or opinions on specific facts or matters, nor does the distribution of this publication to any person constitute the establishment of an attorney-client relationship. Simpson Thacher & Bartlett LLP assumes no liability in connection with the use of this publication. Please contact your relationship partner if we can be of assistance regarding these important developments. The names and office locations of all of our partners, as well as our recent memoranda, can be obtained from our website, www.simpsonthacher.com.