



## Supreme Court Tells Second Circuit To Clarify Securities Class Certification Ruling, And Holds That Defendants Have The Burden Of Persuasion In Rebutting The *Basic* Presumption

***Goldman Sachs Group Inc. v. Arkansas Teacher Retirement System*, No. 20-222**

Decided June 21, 2021

Today, the Supreme Court held 8-1 that the Second Circuit must clarify its reasoning in its certification of a securities class action against Goldman Sachs, and held 6-3 that the defendant bears the burden of persuasion when attempting to rebut the “fraud on the market” presumption.

### Background:

Goldman Sachs was sued under the securities laws for making statements suggesting that it did not have any conflicts of interest in the management of its mortgage business. The plaintiffs sought to certify a class of investors in Goldman stock and invoked the “fraud on the market” presumption, recognized in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), to show that every class member relied on Goldman’s alleged misrepresentations in buying or selling at the market price. Goldman tried to rebut this presumption of reliance by pointing to the generic nature of its challenged statements (e.g., “Integrity and honesty are at the heart of our business”). As Goldman saw it, no investors could have truly relied on such statements in buying their shares because the statements were too generic to impact the stock’s price. The district court rejected that argument and certified the class.

The Second Circuit initially reversed the class-certification order and remanded, after which the district court recertified the class; the Second Circuit then affirmed that second certification order. The Second Circuit held that the generic nature of the statements was

*“The generic nature of a misrepresentation often will be important evidence of a lack of price impact, particularly in cases proceeding under the inflation maintenance theory.”*

Justice Barrett,  
writing for the Court

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irrelevant at the class-certification stage, and instead should be litigated at trial.



### Issues:

Can a defendant in a securities class action rebut the presumption of classwide reliance recognized in *Basic* by arguing that the statements were too generic to have had any impact on the price of the security?

Does a defendant seeking to rebut the *Basic* presumption with evidence of a lack of price impact bear only the burden of production or also the ultimate burden of persuasion?

### Court's Holdings:

A court should consider the generic nature of the statements at the class certification stage, and the Second Circuit must clarify on remand whether it in fact did so here.

The defendant bears the ultimate burden of persuasion when attempting to rebut the *Basic* presumption.

### What It Means:

- Today's decision is the first time the Supreme Court has discussed the "inflation-maintenance" theory of securities fraud, although the Court expressly noted that it was taking no view on the "validity" or "contours" of that theory. Under the inflation-maintenance theory, a misrepresentation causes a stock price to remain inflated by preventing inflation from dissipating from the price. The theory, which has become increasingly common in securities class actions, often depends on an inference that a negative disclosure about the company corrected an earlier misrepresentation, and that a drop in the stock price associated with the disclosure is equal to the amount of inflation maintained by the earlier misrepresentation.
- The Court's decision suggests important limitations on the theory. The Court explained that the 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 disclosure," and this occurs "when the earlier misrepresentation is generic . . . and the later corrective disclosure is specific."
- The decision thus holds that defendants in securities class action suits may rebut the *Basic* presumption by arguing that the allegedly fraudulent statements are too generic to have impacted the price of the security, even if those arguments overlap with the ultimate merits of the case.

- The Court also clarified that its prior decisions in *Basic* and *Erica P. John Fund, Inc. v. Halliburton Co.*, 563 U. S. 804, 813 (2011), established that securities-fraud defendants bear the ultimate burden of persuading the court that the *Basic* presumption does not apply. The Court's decision thus underscores the importance of defendants offering factual and expert evidence at the class certification stage to rebut the *Basic* presumption.

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The Court's opinion is available [here](#).

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding developments at the Supreme Court. Please feel free to contact the following practice leaders:

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