# 21-3105-cv

## United States Court of Appeals

*for the*

## Second Circuit

GOLDMAN SACHS GROUP, INC., LLOYD C. BLANKFEIN,
DAVID A. VINIAR, GARY D. COHN,

*Petitioners,*

– v. –

ARKANSAS TEACHERS RETIREMENT SYSTEM, WEST VIRGINIA INVESTMENT MANAGEMENT BOARD, PLUMBERS AND PIPEFITTERS PENSION GROUP,

*Respondents.*

ON PETITION FOR LEAVE TO APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

**BRIEF OF *AMICI CURIAE* FORMER SEC OFFICIALS AND LAW PROFESSORS IN SUPPORT OF PETITION FOR PERMISSION TO APPEAL PURSUANT TO FEDERAL RULE OF CIVIL PROCEDURE 23(f)**

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## INTRODUCTION AND INTEREST OF *AMICI CURIAE*[1]

This case is now subject to the Court's interlocutory review for the third time. But now, the stakes are even higher as fidelity to the command of the United States Supreme Court is at issue.

On remand, the district court disregarded the Supreme Court's clear instruction to consider the degree of "mismatch" between the alleged misstatements and corrective disclosures in inflation-maintenance cases. The lower court thereby nullified a critical safeguard that the Supreme Court designed to protect defendants' right to rebut the presumption of reliance at class certification recognized in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988).

In applying the Supreme Court's new standard, the lower court failed to give proper weight to the generic nature of the statements at issue in this litigation—statements like, "Integrity and honesty are at the heart of our business" (A-233)—in assessing price impact. It wrongly concluded that alleged misrepresentations (however generic) "match" alleged corrective disclosures (however specific) simply because they implicate the same subject matter.

This cannot be. Every class action securities fraud claim asserts that an initial misrepresentation or omission is later resolved through a corrective disclosure

[1] No counsel for a party authored this brief in whole or in part, and no person or entity, other than *amici curiae* or their counsel, contributed money to fund its preparation or submission. *Amici* submit this brief without a motion for leave to file because both petitioners and respondents have consented.

that implicates the same subject matter. Indeed, by definition, a corrective disclosure is not corrective unless it addresses the same subject matter. By the lower court's logic, every class action securities fraud complaint that alleges a corrective disclosure—as they all do—satisfies the mismatch standard. As such, it is difficult to foresee a scenario where a motion for class certification of a complaint that survived a motion to dismiss would ever fail the mismatch standard. This interpretation of the standard renders it meaningless, and is nothing more than a semantic device that prevents the Supreme Court's logic from having any practical effect. For this reason alone, the opinion below cannot stand.

The lower court committed additional error when it impermissibly expanded the inflation-maintenance theory by asking whether a stock price would have declined had defendants made specific statements accusing themselves of wrongdoing. But this court's own rulings establish that issuers have no duty to disclose unadjudicated wrongdoing. The certification of a class cannot rationally be premised on a failure to disclose a fact as to which there was no duty of disclosure.

The lower court's failure properly to follow the Supreme Court's direction, combined with its suggestion of liability for failure to disclose information as to which no concurrent disclosure duty exists, are sufficient cause to grant Rule 23(f) review. Indeed, the review is necessary to provide practitioners with much needed clarity, as well as to ensure that defendants have a meaningful opportunity to rebut the *Basic* presumption of reliance by showing an absence of price impact.

The *amici curiae* are individuals with a strong interest in these issues: former officials of the U.S. Securities and Exchange Commission and law professors whose scholarship and teaching focus on federal securities laws. Although each individual *amicus* may not endorse every statement made herein,[2] this brief reflects *amici*'s consensus that the opinion below is incorrectly decided and that this appeal presents important questions of law as to which guidance from this Court is essential. Reversal and decertification of the plaintiff class by this Court is therefore appropriate. In alphabetical order, *amici curiae* are:

- Brian G. Cartwright – Former General Counsel of the U.S. Securities and Exchange Commission from 2006 to 2009;
- Ronald J. Colombo – Professor of Law and Dean for Distance Education at the Maurice A. Deane School of Law at Hofstra University;
- Elizabeth Cosenza – Associate Professor of Law and Associate Dean of Undergraduate Studies, at Fordham University's Gabelli School of Business;
- Charles C. Cox – Former Commissioner of the U.S. Securities and Exchange Commission from 1983 to 1989;

[2] In addition, the views expressed by *amici* here do not necessarily reflect the views of the institutions with which they are or have been associated, whose names are included solely for purposes of identification.

- Richard A. Epstein – The Laurence A. Tisch Professor of Law at the New York University School of Law, the Peter and Kirsten Bedford Senior Fellow at The Hoover Institution, and the James Parker Hall Distinguished Service Professor of Law, Emeritus, and Senior Lecturer at the University of Chicago Law School;
- The Honorable Joseph A. Grundfest – William A. Franke Professor of Law and Business at Stanford Law School, and Commissioner of the U.S. Securities and Exchange Commission from 1985 to 1990;
- Simon Lorne – Former General Counsel of the U.S. Securities and Exchange Commission from 1993 to 1996;
- Paul G. Mahoney – David and Mary Harrison Distinguished Professor of Law, at the University of Virginia School of Law, and Dean of the same from 2008 to 2016;
- Adam C. Pritchard – The Frances and George Skestos Professor of Law at the University of Michigan Law School;
- Amanda M. Rose – FedEx Research Professor (2021-2022) and Professor of Law at Vanderbilt University Law School, and Professor of Management at Vanderbilt University Owen Graduate School of Management;
- Matthew Turk – Assistant Professor of Business Law and Ethics at Indiana University's Kelley School of Business;

- Andrew N. Vollmer – Senior Affiliated Scholar, Mercatus Center at George Mason University; former Professor of Law, General Faculty, University of Virginia School of Law; former Deputy General Counsel of the U.S. Securities and Exchange Commission; and
- Karen E. Woody – Associate Professor of Law at Washington & Lee University School of Law.

## ARGUMENT

### I. THE DISTRICT COURT'S OPINION NEGATES THE SUPREME COURT'S "MISMATCH" SAFEGUARD FOR INFLATION-MAINTENANCE LITIGATION.

"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." *Goldman Sachs Grp., Inc. v. Ark. Tchr. Ret. Sys.*, 141 S. Ct. 1951, 1961 (2021). The generic quality of the alleged misrepresentation is "important evidence" because, as the Supreme Court instructs, to prove inflation, plaintiffs typically "point to a negative disclosure about a company and an associated drop in its stock price; allege that the disclosure corrected an earlier misrepresentation; and then claim that the price drop is equal to the amount of inflation maintained by the earlier misrepresentation." *Id.* But 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," which "may occur when the earlier misrepresentation is generic . . . and the later corrective disclosure is specific." *Id.* This "mismatch" between the generality of the alleged misrepresentation and the specificity of the alleged corrective disclosure must be properly assessed by district courts in making a price impact determination if they are to respect the Supreme Court's instruction. *See id.*

The "mismatch" standard establishes an important guardrail to avoid near-automatic class certification in price maintenance cases. Absent this guardrail, the inference that the "back-end price drop equals front-end inflation," *id.*, is generally irrefutable, even where, as here, the front-end inflation was supposedly maintained by generic statements and the back-end price decline involves substantially more detailed information than the allegedly defective front-end disclosures.

The district court erred by misconstruing the "mismatch" standard to require only that "corrective disclosures" generally "implicate" the same subject matter as the "alleged misrepresentations." (A-27.) Under the district court's approach, a "comfortable . . . gap in genericness" is still a match, provided that it is not "boundless." (A-28.) That approach is irreconcilable with the Supreme Court's decision, which emphasized that the generic quality of an alleged misstatement is "important evidence" of a lack of price impact, and so directed courts to assess whether the content and specificity of the alleged front-end misrepresentations and back-end corrective disclosures "match." *Goldman*, 141 S. Ct. at 1961. In so ruling, the district court nullified the core rationale of the Supreme Court's directive.

The corporate statements submitted in this case are common in corporate America, and their generic, anodyne quality underscore that the lower court's opinion is not faithful to the Supreme Court's directive. The statements include: "[w]e're known for operating with high ethical standards everywhere we do business" (Walt Disney); "[m]aintaining GE's reputation for exceptional leadership is key to our renewal" (General Electric); and "[o]ur reputation for quality is critical . . ." (Verizon). (A-325–40.) If a "match" exists whenever a specific negative news event "implicates" generic statements such as these, then it is difficult to conceive of any circumstance where negative corporate news is not a "match."

The district court's misreading of the Supreme Court's mismatch standard must be corrected. As applied below, the result is effectively preordained: a match exists whenever negative corporate news implicates the same subject matter of a generic statement of corporate principle, such as ethics, integrity, or quality. This is especially alarming considering that, as Judge Sullivan recognized in his dissent from this Court's affirmation of the certification of the class in 2020, the challenged statements here (and likely those in future cases) are so generic that "no reasonable investor would have attached any significance" to them. *Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc.*, 955 F.3d 254, 278 (2d Cir. 2020) ("*Goldman II*"), *vacated*, 141 S. Ct. 1951 (2021). In short, this cannot be what the Supreme Court envisioned when it vacated the prior ruling affirming recertification of the class.

Nor was the recent *Goldman Sachs* decision the first time the Supreme Court has emphasized the right of defendants to rebut the presumption of reliance at class certification. *Halliburton Co. v. Erica P. John Fund, Inc.*, 573 U.S. 258 (2014) ("*Halliburton II*"), makes clear that defendants are entitled to an opportunity to rebut the *Basic* presumption at class certification by presenting evidence that severs the link between the alleged misrepresentations and the stock price. *Id.* at 279–80. In so holding, the *Halliburton II* court cited *Basic*'s expansive articulation of the standard for securities fraud class action defendants when seeking to break that link: "[*a*]*ny* showing that severs the link between the alleged misrepresentation and . . . the price received (or paid) by the plaintiff" for the shares in question. *Id.* at 281 (citing *Basic*, 485 U.S. at 248) (emphasis added). Again, by refusing properly to consider evidence that the alleged misstatements and corrective disclosures in this case are clearly mismatched, which is important evidence of a lack of price impact, the district court's decision fails to adhere to the Supreme Court's clear direction.

## II. THE DISTRICT COURT IMPERMISSIBLY EXPANDED THE INFLATION-MAINTENANCE THEORY.

Issuers have no "duty to disclose uncharged, unadjudicated wrongdoing." *City of Pontiac Policemen's & Firemen's Ret. Sys. v. UBS AG*, 752

F.3d 173, 184 (2d Cir. 2014) (internal quotation marks omitted).[3] Defendants thus cannot be held liable for failing to disclose later arising claims of wrongdoing. Yet that is precisely the basis for the class certification order entered below.

Rather than considering a hypothetically truthful statement at the same level of specificity as the challenged generic statements—as occurred with the misstatements and corrections about liquidity in *Vivendi*[4]—the district court assumed that the comparator statement should be as specific as the alleged corrective disclosures. (*See* A-21.) By so reaching beyond the approach taken by other courts, and effectively comparing apples to oranges, the district court ignored the theoretical underpinnings of the inflation-maintenance doctrine.

That a specific disclosure led to a stock price decline cannot establish that an earlier generic statement maintained an inflated stock price. By embracing that flawed assumption, the district court creates an unwarranted conflict between the inflation-maintenance doctrine and the fundamental premise recognized by the Second Circuit, and other circuits, that, as explained above, issuers have no "duty to disclose uncharged, unadjudicated wrongdoing."[5]

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[3] Other federal courts to consider the question have reached the same result. *See, e.g.*, *Anderson v. Abbott Lab'ys*, 140 F. Supp. 2d 894, 906 (N.D. Ill. 2001), *aff'd sub nom. Gallagher v. Abbott Lab'ys*, 269 F.3d 806 (7th Cir. 2001) ("SEC rules do not create a duty to confess contested charges."); *United States v. Crop Growers Corp.*, 954 F. Supp. 335 (D.D.C. 1997) (finding that defendants had no duty to disclose uncharged criminal conduct).

[4] *In re Vivendi, S.A. Sec. Litig.*, 838 F.3d 223 (2d Cir. 2016).

[5] *See* note 3, *supra*.

This doctrinal error is no minor matter. Publicly traded corporations commonly issue generic statements about business principles and practices. These statements are increasingly common as ESG disclosures become more prevalent. *See, e.g.*, A-327–34 ("We . . . protect the environment" (Chevron); "We are responsible . . . to the environments we inhabit, and to the societies we serve worldwide" (Merck & Co., Inc.); and "[W]e have a vested interest in good schools, safe neighborhoods and strong local economies" (Verizon)).

As a result, public companies face a stark choice: either they must now disclose the granularities of all actual or potential violations of those principles and practices—including their "details and severity" (A-21)—or accept that they cannot contest that their generic statements had price impact in order to defeat the certification of classes seeking enormous securities fraud damages. Chevron would thus be fraudulently maintaining an inflated stock price by stating, "We . . . protect the environment," unless it also disclosed all unadjudicated suspicions of employees illegally dumping waste or committing environmental crimes. The district court's assumption that issuers making even generic statements are required to issue detailed disclosures of unadjudicated wrongdoing cannot be squared with this Court's unequivocal pronouncements that "[t]ime and again, we have said that disclosure is not a rite of confession . . . ." *In re ProShares Tr. Sec. Litig.*, 728 F.3d 96, 103 (2d Cir. 2013) (Wesley, J.) (internal quotation marks omitted).

The heart of the Supreme Court's ruling was that the "generic nature" of an alleged misrepresentation is often "important evidence of price impact" because "a more-general statement will affect a security's price less than a more-specific statement on the same question." *Goldman Sachs Grp., Inc. v. Ark. Tchr. Ret. Sys.*, 141 S. Ct. 1951, 1960 (2021). But in the district court's application of the inflation-maintenance theory, the "generic nature" of any statement becomes irrelevant. Rather than assess whether a generic statement has price impact, the lower court determined that the stock price would have declined had defendants made very specific statements accusing themselves of wrongdoing.

This approach is fundamentally incompatible with the Supreme Court's instruction because it relies on a hypothetical precise disclosure that never occurred, and that defendants were clearly not required to make. The lower court's logic thereby erases the generic nature of the alleged misstatement from the equation and creates an inflation-maintenance standard that fundamentally conflicts with the Supreme Court's decision and with this Circuit's precedent.

For the foregoing reasons, the *amici curiae* believe that the Court should grant this Petition.

Dated: New York, New York
December 29, 2021

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## CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitation of Fed. R. App. P. 29 because it contains 2,484 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(f).

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Dated: December 29, 2021
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