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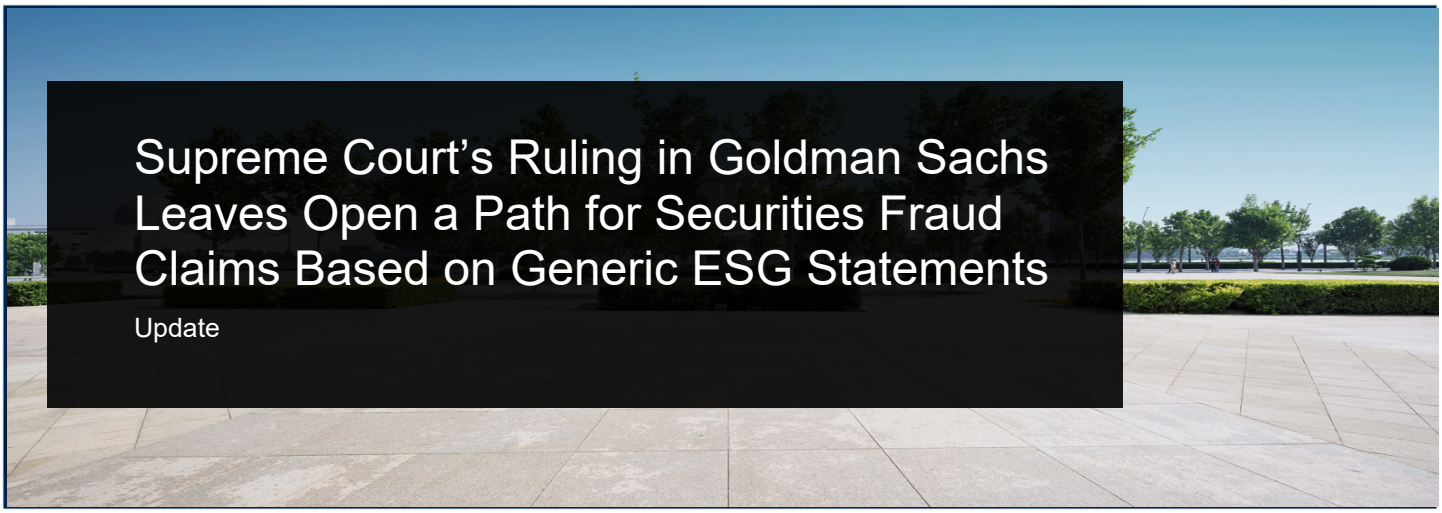

Supreme Court's Ruling in Goldman Sachs Leaves Open a Path for Securities Fraud Claims Based on Generic ESG Statements

Update

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In April, we analyzed whether a corporation's purely generic public statements on environmental, social and governance ("ESG") issues could form the basis of a subsequent securities fraud action. At the time, we identified a case pending before the United States Supreme Court, *Goldman Sachs Group v. Arkansas Teacher Retirement System*, which had the potential to offer significant clues to the future of ESG-related litigation based on generic statements. On June 21, 2021, the Supreme Court released its decision in *Goldman Sachs*. While the decision re-confirms that defendant corporations bear the burden of establishing that their public statements had no impact on their stock price, it also acknowledges that this burden may be lighter for more generic statements.

The *Goldman Sachs* Decision

The plaintiffs in *Goldman Sachs*—a class of Goldman Sachs shareholders led by the Arkansas Teacher Retirement System—alleged that they suffered more than $13 billion in damages when they were misled by generic public statements from Goldman Sachs about avoiding conflicts of interest, such as: "Our clients' interests always come first"; "Integrity and honesty are at the heart of our business"; and "We are dedicated to complying fully with the letter and spirit of the laws, rules, and ethical principles that govern us."

When it was revealed that Goldman Sachs created and sold a group of collateralized debt obligations without disclosing that a hedge fund client—which bet against the CDO—helped pick the underlying securities, Goldman Sachs's share price plummeted. The plaintiffs argued that Goldman Sachs's prior generic statements had artificially maintained an inflated share price, which collapsed when the truth came out. Goldman Sachs responded that the

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public statements under scrutiny were so generic that they could not have had any impact on its share price, and that the stock drop was instead due to the ensuing government enforcement action and negative news coverage. The Second Circuit permitted the case to be certified as a class action, accepting the plaintiff's theory that Goldman Sachs may have perpetrated a "fraud on the market" through its disclosures about avoiding conflicts of interest.

By the time the case reached the Supreme Court, however, the parties' dispute on this question had "largely evaporated." The shareholders—who had earlier argued that the generic nature of a statement is irrelevant at the class certification stage—conceded that a more generic statement is less likely to affect a security's price than a more specific statement. The Court shared the parties' view, stressing in the majority opinion written by Justice Barrett that a generic misrepresentation would be less likely to result in a price correction when the eventual corrective disclosure (in *Goldman Sachs*, news of the enforcement action) came to light. The Court remanded the case to the Second Circuit, directing the lower court to reconsider whether it had "properly considered the generic nature of Goldman's alleged misrepresentations."

The Court also reconfirmed that "defendants in securities-fraud class actions bear the burden of persuasion to prove a lack of price impact" at class certification. However, the Court noted that because the defendant need only demonstrate a lack of price impact by a preponderance of the evidence, "the allocation of the burden is unlikely to make much difference on the ground."

Impact on ESG Litigation

Although *Goldman Sachs*'s determinations on generic disclosures, price impact and class certification did not directly address environmental, social or governance issues, the case's impact on ESG litigation is evident. Many companies that seek to espouse ESG principles declare their public commitments in generic and aspirational prose, never suspecting that their ambitious statements could form the basis of a securities fraud class action.

The Court's holding that a statement's generic nature is relevant to its potential impact on share price implies that there is some measure of safety in generic ESG statements. Whether relying on expert opinion or the court's common sense, the *Goldman Sachs* decision suggests that a future defendant is more likely to defeat class certification based on a generic statement like "We are committed to sustainability," than a specific one such as "We will achieve net-zero carbon emissions by 2025."

However, if a subsequent negative disclosure directly contradicts ESG statements, the burden of persuasion will rest with the company to disprove any impact on the share price. While the Court stated that the burden would often not be outcome determinative because it will only make a difference in cases where the evidence of price impact or lack thereof is equally balanced, Justice

Gorsuch's partial dissent noted that the point of establishing a burden of persuasion is to resolve these close cases.

Conclusion

Goldman Sachs is not over. As the Second Circuit reviews the case on remand, we will continue to provide updates on a decision that could provide a key precedent regarding how ESG disclosures may be vulnerable to the risk of expensive shareholder-driven litigation.

Bracewell has a multi-disciplinary team focused on ESG issues. We advise and support our clients drawing on our expertise in environmental strategies, securities matters, regulatory issues, government enforcement, labor and employment, commercial litigation, and crisis management, and we are at the forefront of the transition to sustainable energy. Please contact your Bracewell team member for more information.