The Imperial Securities Fraud Regime

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I. INTRODUCTION

The recent Supreme Court decision, *Goldman Sachs Group, Inc.* v. *Arkansas Teacher Retirement System*,[1] has prompted many finance and business commentators to question whether jurisprudence is trending toward a system in which "everything is securities fraud."[2] This Note will explore whether the expansion of the securities fraud regime is prudent as a matter of policy.

Increasingly plaintiff-friendly securities fraud decisions in the context of generic statements prompt one to wonder whether social and environmental commitments by corporations will be deterred due to the increased potential for liability. This concern is exacerbated by the rise of environmental and social governance (ESG) initiatives. Further, the expansion of the securities fraud regime gives rise to concerns about consumer welfare. Specifically, there is a likelihood that the costs of increased securities fraud litigation will merely be passed down to customers. Such a phenomenon would comport with commonly

1. 141 S. Ct. 1951 (2021).

2. Matt Levine, *Is Everything Securities Fraud?*, BLOOMBERG (Feb. 3, 2021), https://www.bloomberg.com/opinion/articles/2021-02-03/goldman-sachs-goes-to-supreme-court-hedge-funds-won-on-gamestop-kkpoe6ws [https://perma.cc/A7MD-HBTL]; *see also* Emily Strauss, *Is Everything Securities Fraud?*, COLUM. L. SCH. BLUE SKY BLOG (May 19, 2021), https://clsbluesky.law.columbia.edu/2021/05/19/is-everything-securities-fraud/ [https://perma.cc/C72H-NJT2] (reporting that of approximately "500 securities class actions against public firms from 2010–2015," 16.5% "arise from misconduct where the most direct victims are not shareholders. While still a minority of the lawsuits, these cases have a significantly lower dismissal rate and generate higher settlements than cases where the primary victims are shareholders").

understood market dynamics.[3]

Throughout the early years of the 21st century, the Goldman Sachs Group, Inc. (Goldman Sachs) declared, among other *generic* statements, that it would "fully [comply] with the letter and spirit of the law" and that "integrity and honesty are at the heart of [Goldman Sachs'] business."[4] The subsequent recession would reveal that these claims were dubious at best, as Goldman Sachs engaged in subprime lending that contributed to economic upheaval not witnessed since the Great Depression.[5] Arkansas Teacher Retirement System (ATRS)—a series of pension funds invested in the firm—alleged that these were misrepresentations which had an adverse impact on the stock price. Therefore, ATRS, as a class, was entitled to damages for securities fraud under Rule 10b-5 of the Securities Exchange Act of 1934.[6] While *the jurists* are still out as to whether ATRS is entitled to relief in this specific instance (the case was remanded to the Second Circuit U.S. Court of Appeals), Associate Supreme Court Justice Amy Coney Barrett's decision vacating and remanding the Second Circuit's decision left the door open to recovery in such actions.[7] In pertinent part, the Supreme Court held that "*the generic nature* of a misrepresentation often is important evidence of price impact that courts should consider at class certification."[8]

In the analysis that follows, this Note will argue that a line must be drawn in the sand to avert the deterrence of socially conscious corporate commitments as well as inflated consumer costs.[9] Specifically, section 240.10b-5 (Rule 10b-5) of the Securities Exchange Act of 1934[10] should be amended to exclude generic statements as potential subject matter for securities fraud suits. This amendment would protect consumers, who would otherwise internalize the costs of increased litigation. Moreover, it would *encourage* socially

3. William Dunkelberg, *The Insidious Cost of Regulation*, FORBES (April 4, 2017), https://www.forbes.com/sites/williamdunkelberg/2017/04/04/the-insidious-cost-of-regulation/?sh=50481a385c7b [https://perma.cc/SW9C-P5BR].

4. Levine, *supra* note 2.

5. For an overview of the severity of the Great Recession's economic turmoil, see Josh Bivens, *Worst Economic Crisis Since the Great Depression? By a Long Shot.*, ECON. POL'Y INST. (Jan. 27, 2010), https://www.epi.org/publication/snapshot_20100127/ [https://perma.cc/Z8SY-JK9C] (comparing GDP growth since the beginning of the 2008 recession to past recessions); *Chart Book: The Legacy of the Great Recession*, CTR. ON BUDGET & POL'Y PRIORITIES (June 6, 2019), https://www.cbpp.org/research/economy/the-legacy-of-the-great-recession [https://perma.cc/ZZ5F-A2A8] (charting the "course of the economy" from the start of the Great Recession to 2017); Renae Merle, *A Guide to the Financial Crisis – 10 Years Later*, WASH. POST (Sept. 10, 2018), https://www.washingtonpost.com/business/economy/a-guide-to-the-financial-crisis--10-years-later/2018/09/10/114b76ba-af10-11e8-a20b-5f4f84429666_story.html [https://perma.cc/HU3K-4NSY] (answering common questions about the Great Recession and its impact); Michael J. Boyle, *2008 Recession: What the Great Recession Was and What Caused It*, INVESTOPEDIA, https://www.investopedia.com/terms/g/great-recession.asp [https://perma.cc/3JZM-PQ47] (recounting how subprime mortgage lending caused the Great Recession).

6. *See* Goldman Sachs Grp. v. Ark. Tchr. Ret. Sys., 141 S. Ct. 1951, 1957 (2021) (discussing ATRS' claims) ("Plaintiffs say that Goldman's generic statements were false or misleading in light of several undisclosed conflicts of interest, and that once the truth about Goldman's conflicts came out, Goldman's stock price dropped and shareholders suffered losses.").

7. *Id.* at 1963.

8. *Id.* at 1958 (emphasis added).

9. *See infra* Parts III.B. and III.C.

10. 17 C.F.R. § 240.10b-5 (2022).

conscious corporate activism, whereas the Supreme Court's interpretation of the present iteration of Rule 10b-5 deters such behavior insofar as every generic activist statement has the potential to subject a corporation to liability.

II. BACKGROUND

A. Goldman Sachs and the Financial Crisis

At the time, Goldman Sachs' 1999 initial public offering (IPO) was among the largest in U.S. history.[11] Subsequent thereto, Goldman and its directors assumed a number of additional responsibilities—primarily to newly minted shareholders.[12] Over the course of the next decade, Goldman released proxy statements reiterating its commitment to engaging in ethical conduct and adhering to existing law.[13] Goldman specifically stated that "[i]ntegrity and honesty are at the heart of our business. We expect our people to maintain high ethical standards in everything they do, both in their work for [Goldman Sachs] and in their personal lives."[14] Shareholders have called Goldman Sachs' adherence to such commitments into question on the basis of its activity that led to the financial crisis of 2007 to 2009.[15]

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11. At its IPO, Goldman offered a 15% stake and raised nearly $3.7 billion. *In a Paradigm Shift*, *Goldman Sachs Decides to Go Public*, GOLDMAN SACHS, https://www.goldmansachs.com/our-firm/history/moments/1999-ipo.html [https://perma.cc/2Q47-2YWT]. At the time, Goldman's IPO was the second biggest of all firms in U.S. history, trailing only Conoco Inc's $4.4 billion IPO. *End of an Era for Goldman*, CNN MONEY (May 3, 1999), https://money.cnn.com/1999/05/03/markets/goldman/ [https://perma.cc/8SMU-U9CF]. Tom Taulli, *The 25 Biggest U.S. IPOs of All Time*, KIPLINGER (Oct. 19, 2018), https://www.kiplinger.com/slideshow/investing/t052-s001-the-25-biggest-ipos-in-u-s-history/index.html.

12. *See* Pepper v. Litton, 308 U.S. 295, 311 (1939) ("He who is in . . . a fiduciary position cannot serve himself first and his cestuis second. He cannot manipulate the affairs of his corporation to their detriment and in disregard of the standards of common decency and honesty."); *see also* Milton Friedman, *A Friedman Doctrine—The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES (Sept. 13, 1970), https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html [https://perma.cc/S2EM-FW68] (stating that corporate directors and officers should maximize shareholder value); Richard A. Epstein, *What is the Purpose of a Corporation?*, HOOVER INST. (Aug. 26, 2019), https://www.hoover.org/research/what-purpose-corporation [https://perma.cc/AB9K-P4TM] (reiterating Friedman's concept of shareholder primacy).

13. *See, e.g.*, GOLDMAN SACHS GRP., 2003 PROXY STATEMENT para. 2 (2003), https://www.goldmansachs.com/investor-relations/financials/archived/proxy-statements/docs/proxy-statement-2003.pdf [https://perma.cc/ZE9G-SPSJ] ("It has never been more evident that business leaders must hold themselves and their companies to the highest ethical standards."); GOLDMAN SACHS GRP. INC., 2004 PROXY STATEMENT para. 2 (2004), https://www.goldmansachs.com/investor-relations/financials/archived/proxy-statements/docs/proxy-statement-2004.pdf [https://perma.cc/UEF9-KD2Z] ("[W]e have continued to take steps to promote and protect the interests of our shareholders."); GOLDMAN SACHS GRP. INC., THE GOLDMAN SACHS APPROACH: 2005 ANNUAL REPORT 17 (2006), https://www.goldmansachs.com/investor-relations/financials/archived/annual-reports/attachments/annual-report.pdf [https://perma.cc/GFS7-M6XC] ("Market growth and the complexity of our business require us to meet the highest ethical standards wherever we do business.").

14. GOLDMAN SACHS GRP., 2003 PROXY STATEMENT E-1 (2003), https://www.goldmansachs.com/investor-relations/financials/archived/proxy-statements/docs/proxy-statement-2003.pdf [https://perma.cc/TV6K-A5RQ].

15. Jess Bravin, *Supreme Court Weighs Merit of Goldman Sachs Ethics Statements*, WALL ST. J. (Mar. 29, 2021), https://www.wsj.com/articles/supreme-court-weighs-merit-of-goldman-sachs-ethics-statements-

In the early 2000s, low interest rates caused an influx in mortgages, fueling a housing bubble predicated on subprime lending.[16] During this period, Goldman Sachs, like many other financial institutions, profited from mortgage-backed securities in which it knowingly packaged subprime-loan obligations into collateralized debt obligations (CDOs).[17] CDOs are "complex investment securit[ies] built on a pool of underlying assets, such as mortgage-backed securities. Crucially, each CDO is sliced up and sold in 'tranches'[18] that pay different interest rates."[19] Goldman Sachs sold extremely risky packages while assuring buyers that they were highly safe and secure investment vehicles.[20] Meanwhile, the firm bet against them through its purchase of default credit swaps.[21]

The problematic nature of Goldman's activity came to the fore when the housing bubble burst in 2007.[22] The previous year, Goldman internally recognized that the mortgage market outlook was negative, though it continued to pedal an optimistic outlook

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11617050980 [https://perma.cc/Q94M-GHJK]; Robert Zafft, *Lessons from Goldman Sachs: Empty Promises Bring Troubles by the Boatload*, FORBES (Mar. 31, 2021), https://www.forbes.com/sites/robertzafft/2021/03/31/lessons-from-goldman-sachs-empty-promises-bring-troubles-by-the-boatload/?sh=4386c2125770 [https://perma.cc/H63V-GS8R].

16. BRIAN KEELEY & PATRICK LOVE, FROM CRISIS TO RECOVERY: THE CAUSES, COURSE AND CONSEQUENCES OF THE GREAT RECESSION 19–20 (OECD 2010).

17. Press Release, U.S. Dep't of Just., Goldman Sachs Agrees to Pay More than $5 Billion in Connection with Its Sale of Residential Mortgage Backed Securities (Apr. 11, 2016), https://www.justice.gov/opa/pr/goldman-sachs-agrees-pay-more-5-billion-connection-its-sale-residential-mortgage-backed [https://perma.cc/748E-PQH2] [hereinafter Goldman Sachs Press Release].

18. "Tranches" can be defined as follows:

> Tranches are segments created from a pool of securities—usually debt instruments such as bonds or mortgages—that are divvied up by risk, time to maturity, or other characteristics in order to be marketable to different investors. Each portion or tranche of a securitized or structured product is one of several related securities offered at the same time, but with varying risks, rewards and maturities to appeal to a diverse range of investors.

James Chen, *Tranches*, INVESTOPEDIA, https://www.investopedia.com/terms/t/tranches.asp [https://perma.cc/E7KG-RPWE].

19. *See* KEELEY & LOVE, *supra* note 16, at 25 ("The safest tranche, usually given a rating of AAA, pays the lowest rate of interest; riskier tranches, rated BBB or less, pay a higher interest rate – in effect, the bigger the risk you're willing to take, the bigger your return. CDOs blew up during the subprime crisis because some of these risky tranches were subsequently packaged up into new CDOs, which were then sliced up into tranches, including "safe" AAA tranches. As mortgage defaults grew, even cautious investors who thought they were making a safe AAA investment found they were left with nothing, or almost nothing.").

20. *See* Goldman Sachs Press Release, *supra* note 17 (elaborating on the DOJ's investigation into Goldman Sachs and, specifically, key statements of facts and case details).

21. *See generally* Gretchen Morgenson & Louise Story, *Banks Bundled Bad Debt, Bet Against It and Won*, N.Y. TIMES (Dec. 23, 2009), https://www.nytimes.com/2009/12/24/business/24trading.html [https://perma.cc/7BDA-XKJQ] ("[Goldman Sachs] allowed investors to bet for or against the mortgage securities that were linked to the deal. The [CDOs] didn't contain actual mortgages. Instead, they consisted of credit-default swaps, a type of insurance that pays out when a borrower defaults. These swaps made it much easier to place large bets on mortgage failures.").

22. *See* Greg Gordon, *How Goldman Secretly Bet on the U.S. Housing Crash*, MCCLATCHY NEWSPAPERS (June 16, 2015), https://www.mcclatchydc.com/news/politics-government/article24561376.html [https://perma.cc/8PQ6-2YDX] (noting that Goldman "became the only major Wall Street player to extricate itself from the subprime securities market before the housing bubble burst").

to the public.[23] Systematic mortgage defaults caused clients to lose money on their CDO investments,[24] though the firm profited through the sale of those CDOs and their betting that the CDOs' value would eventually crash.[25] With the crash in CDO values came a global recession, a domestic housing crisis, and sky-high unemployment rates.[26]

Goldman Sachs later admitted wrongdoing, and settled with the Department of Justice (DOJ) in 2016.[27] Pursuant to the terms of the settlement, Goldman Sachs stipulated to a "statement of facts," which included—among other stipulations—a confession that it "typically did not . . . identify and eliminate any additional loans with credit exceptions."[28] Goldman's activity would be a boon for the rise of populist sentiments across the country, including the Occupy Wall Street movement,[29] which "aims to fight back against the richest 1% of people that are writing the rules of the unfair global economy."[30] In the time since, the U.S. government has imposed a number of reforms to combat recklessness in the financial sector.[31]

B. Efficient Market Theory and Securities Fraud

The elements for a securities fraud action under Rule 10b-5 are "(1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation."[32] The reason for the law's existence is to deter fraud and compensate non-trading shareholders whose holdings may be adversely impacted by untrue statements.[33] Moreover, some scholars have argued that the doctrine has a punitive component that should be enhanced.[34]

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23. Morgenson & Story, *supra* note 21.

24. Andy Smith, *Were Collateralized Debt Obligations Responsible for the Financial Crisis?*, INVESTOPEDIA, https://www.investopedia.com/ask/answers/032315/were-collateralized-debt-obligations-cdo-responsible-2008-financial-crisis.asp [https://perma.cc/D62W-DX73].

25. Morgenson & Story, *supra* note 21.

26. *See generally* Douglas W. Arner, *The Global Credit Crisis of 2008: Causes and Consequences*, 43 INT'L. LAW. 91 (2009) (describing the context of the global recession in 2008).

27. Goldman Sachs Press Release, *supra* note 17.

28. *Id.*

29. *See generally* Lauren Tara LaCapra, *How Wall Street is Responding, or Not, to Protests*, REUTERS (Oct. 11, 2011), https://www.reuters.com/article/us-usa-wallstreet-bankers/how-wall-street-is-responding-or-not-to-protests-idUSTRE79A4LF20111011 [https://perma.cc/KY2B-5HUE] (detailing Wall Street's response to the Occupy Wall Street movement).

30. MOHAN J. DUTTA, VOICES OF RESISTANCE: COMMUNICATION AND SOCIAL CHANGE 46 (2012).

31. *See, e.g.*, Dodd–Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C. § 5301. The Dodd–Frank Wall Street Reform and Consumer Protection Act supplied the financial sector with increased oversight and regulation. It was a direct response to the reckless activity (such as that described above) which catalyzed the financial crisis of 2008. *See* Adam Hayes, *Dodd–Frank Act: What It Does, Major Components, Criticisms*, INVESTOPEDIA, https://www.investopedia.com/terms/d/dodd-frank-financial-regulatory-reform-bill.asp [https://perma.cc/M2V3-RD5L] (summarizing legislation passed in direct response to the 2007-2008 financial crisis).

32. *In re* Mun. Mortg. & Equity, L.L.C., Sec. & Derivative Litig., 876 F. Supp. 2d 616, 625 (D. Md. 2012) (quoting Matrix Cap. Mgmt. Fund, L.P. v. BearingPoint, Inc., 576 F.3d 172, 181 (4th Cir. 2009)).

33. HOLGER SPAMANN, SCOTT HIRST & GABRIEL RAUTERBERG, CORPORATIONS IN 100 PAGES 85 (2020).

34. *See* Richard H. Gilden, *Punitive Damages in Implied Private Actions for Fraud Under the Securities Laws*, 55 CORNELL L. REV. 646, 658 (1970) ("A plaintiff's remedies in private actions under section 17(a) and

According to the efficient market theory:

> If a market is generally efficient in incorporating publicly available information into a security's market price, it is reasonable to presume that a particular public, material misrepresentation will be reflected in the security's price. Furthermore, it is reasonable to presume that most investors—knowing that they have little hope of outperforming the market in the long run based solely on their analysis of publicly available information—will rely on the security's market price as an unbiased assessment of the security's value in light of all public information. Thus, courts may presume that investors trading in efficient markets indirectly rely on public, material misrepresentations through their "reliance on the integrity of the price set by the market."[35]

Accordingly, in such actions, "allegations and proof of reliance . . . supply the necessary causal connection between a defendant's alleged misconduct and a plaintiff's decision to trade. Plaintiffs must show that 'but for' the alleged misrepresentations . . . of material fact, they would not have entered into the securities transaction that allegedly resulted in a loss."[36] Moreover, "[i]f applicable at trial and unrebutted, the presumption is that each class member, relying on the integrity of the market price, purchased the stock at an inflated price."[37] Courts impose such a presumption to "mitigate the difficulty in proving 'reliance.'"[38]

Commentary regarding the vastness of the doctrine's applicability has emerged since Goldman Sachs' shareholders prevailed in lower courts regarding *generic* statements.[39]

Indeed, Goldman Sachs is unlikely to be considered a sympathetic defendant. But bad facts make bad law—or so the old adage goes. The consensus among finance and business commentators is that a system in which "everything is securities fraud" is emerging.[40]

C. The Scienter Requirement

"An essential element of a claim under [SEC] Rule 10b-5 is that the defendant acted with scienter."[41] Under *Ernst & Ernst v. Hochfelder*, the requisite scienter for a viable

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rule 10b-5 are potent, but there are areas where additional punitive and deterrent devices are needed.").

35. Amgen Inc. v. Conn. Ret. Plans & Tr. Funds, 568 U.S. 455, 462 (2013) (quoting Basic Inc., v. Levinson, 485 U.S. 224, 245 (1988)).

36. 1 MCLAUGHLIN ON CLASS ACTIONS § 5:26 (19th ed. 2022) (footnote omitted).

37. *Id.*

38. Anthony J. Anscombe & Mary Elizabeth Buckley, *Presumptions of Reliance: What They Really Mean and How to Defeat Them*, BLOOMBERG L. (Jan. 2, 2014), https://news.bloomberglaw.com/us-law-week/presumptions-of-reliance-what-they-really-mean-and-how-to-defeat-them [].

39. Levine, *supra* note 2; Theodore Frank, *Courthouse Steps Decision Webinar:* Goldman Sachs Group, Inc. v. Arkansas Teacher Retirement System, FEDERALIST SOC'Y (July 1, 2021), https://fedsoc.org/events/courthouse-steps-decision-webinar-goldman-sachs-group-inc-v-arkansas-teacher-retirement-system [https://perma.cc/4492-GSY3].

40. Levine, *supra* note 2.

41. Allan Horwich, *An Inquiry into the Perception of Materiality as an Element of Scienter Under SEC Rule 10b-5* 1 (Nw. Univ. Sch. of L. Fac., Working Paper No. 15, 2011), https://scholarlycommons.law.northwestern.edu/cgi/viewcontent.cgi?article=1014&context=facultyworkingpap

securities fraud claim is a "mental state embracing intent to deceive, manipulate, or defraud."[42] Ascribing intent to a corporate entity is a difficult task, since the corporation is not an individual, but a legal fiction that cannot harbor intent. Pursuant to *Teamsters Local 445 Freight Division Pension Fund v. Dynex Capital Inc.*, "the most straightforward way to raise such an inference for a corporate defendant will be to plead it for an individual defendant."[43] The issue of how precisely to ascertain corporate scienter has been deemed an "open issue."[44] A CEO's scienter can, however, typically bind a corporation.[45]

A substantial portion of U.S. law is a mix of statute and judicial decision.[46] Securities fraud actions, sanctioned by Congress through statute, provide judges with deference in the development of their particularities.[47] Accordingly, judges are afforded a broad amount of discretion. Professor Jill Fisch writes that "Congress and the Supreme Court have developed the scope of federal securities fraud litigation through a collaborative process."[48]

D. Generic Statements as Liabilities: Arkansas Teacher Retirement System v. Goldman Sachs Group, Inc.

Arkansas Teacher Retirement System filed suit against Goldman Sachs in the U.S. District Court for the Southern District of New York, alleging that it violated the Securities Exchange Act of 1934.[49] Specifically, ATRS brought the claim under Rule 10b-5, which precludes corporations from defrauding or deceiving "any person in connection with the purchase or sale of any security."[50] Plaintiffs predicated their action on misrepresentations which were described as "generic statements."[51] The *generic nature* of the statements at

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ers [https://perma.cc/U97Y-ALNP]; *Id.* at 1 n.2 ("In a typical § 10(b) private action a plaintiff must prove (1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation.") (quoting Stoneridge Inv. Partners v. Scientific-Atlanta, Inc., 552 U.S. 148, 157 (2008)).

42. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193 n.12 (1976).

43. Teamsters Loc. 445 Freight Div. Pension Fund v. Dynex Cap. Inc., 531 F.3d 190, 195 (2d Cir. 2008).

44. Daniel A. McLaughlin & Mark Taticchi, *Corporate Scienter Under Section 10(b) and Rule 10b-5*, BLOOMBERG BNA: SEC. REG. & L. REP. 1, 1 (May 5, 2014), https://www.sidley.com/-/media/files/publications/2014/05/corporate-scienter-under-section-10b-and-rule-10b5/files/view-article/fileattachment/bloomberg-bnacorporate-scienter-under-section-10__.pdf?la=en [https://perma.cc/5HJ2-ABSP].

45. *See* Makor Issues & Rts., Ltd. v. Tellabs Inc., 513 F.3d 702, 712 (7th Cir. 2008) (citing CEO's scienter as grounds to justify plaintiff's allegations of security fraud); *see also* Jonathan Richman, *Corporate Scienter Requires Link Between Employees with Knowledge and the Alleged Misstatements*, JDSUPRA (May 28, 2020), https://www.jdsupra.com/legalnews/corporate-scienter-requires-link-67107/ [https://perma.cc/W8H2-6NZP] ("[A CEO's] scienter usually can bind a corporation.").

46. *See generally* Marcus P. Knowlton, *Legislation and Judicial Decision: In Their Relations to Each Other and to the Law*, 11 YALE L.J. 95, 99 (1901) ("[T]he courts have gone forward hand in hand with the law-making power to create a system of jurisprudence . . . .").

47. Jill E. Fisch, *Federal Securities Fraud Litigation as a Lawmaking Partnership*, 93 WASH. U. L. REV. 453, 455 (2015).

48. *Id.*

49. *In re* Goldman Grp., Inc. Sec Litig., No. 10 Civ. 3461, 2015 WL 5613150, at *1 (S.D.N.Y. Sept. 24, 2015).

50. 17 C.F.R. § 240.10b-5 (2022).

51. Goldman Sachs Grp., Inc. v. Ark. Tchr. Ret. Sys., 141 S. Ct. 1951, 1957 (2021).

issue distinguishes this case from prior securities actions.[52]

Initially, the district court dismissed Goldman Sachs' motion to dismiss the claims regarding generic misstatements—thus ratifying the notion that such could be tried under Rule 10b-5.[53] The ATRS class was then certified in 2015.[54] The U.S. Court of Appeals for the Second Circuit affirmed that ATRS had "established the preliminary elements to invoke the *Basic* elements of reliance" but remanded the case for consideration of whether Goldman Sachs had rebutted the *Basic* presumption by a preponderance of the evidence.[55] Such elements of reliance are derived from the U.S. Supreme Court case of *Basic v. Levinson*,[56] and include (1) public misrepresentations, (2) the occurrence of trades in an efficient market, and (3) purchase of stock from the instant defendant by putative class members.[57] The issue presented was "whether defendants bear the burden of production or persuasion to rebut the *Basic* presumption."[58] The Second Circuit determined that defendants did bear such a burden.

On remand from the Second Circuit's findings, the Southern District of New York considered whether Goldman Sachs had met the *Basic* presumption "with evidence that the defendants' misrepresentation had no price impact."[59] The district court determined that Goldman Sachs failed to do so, reasoning that Goldman Sachs failed to demonstrate (1) that the stock price was not artificially maintained by the relevant misstatements; and (2) that price declines following the "disclosures were due *entirely* to the news of enforcement actions."[60] "The Court accept[ed an expert witness's] opinion that the news of Goldman's conflicts on the three corrective disclosure dates negatively impacted Goldman's stock price."[61] Moreover, the court did not agree that another expert witness' study demonstrated that the mere news of enforcement had an impact on Goldman's stock price in itself.[62] Therefore, the court found in favor of ATRS.[63] Goldman appealed, but such was futile.[64]

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52. Keith Blackman, Joshua Klein & Rachel B. Goldman, *Supreme Court's Ruling in* Goldman Sachs *Leaves Open a Path for Securities Fraud Claims Based on Generic ESG Statements*, BRACEWELL (June 28, 2021), https://bracewell.com/insights/supreme-courts-ruling-goldman-sachs-leaves-open-path-securities-fraud-claims-based-generic [https://perma.cc/6M7A-WCNY].

53. Richman *ex rel.* v. Goldman Sachs Grp., Inc., 868 F. Supp. 2d 261, 284 (S.D.N.Y. 2012).

54. *In re* Goldman Sachs Grp., Inc. Sec. Litig., No. 10 Civ-3461, 2015 WL 5613150, at *3 (S.D.N.Y. Sept. 24, 2015) ("The Court determines that the putative class meets the requirements of Rule 23(a): the class members are numerous; there are common questions of law and fact; the claims of the representative parties are typical of the class; and the representative parties will fairly and adequately protect the interests of the class.").

55. Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc., 879 F.3d 474, 484–85 (2d Cir. 2018).

56. Basic Inc. v. Levinson, 485 U.S. 224 (1988).

57. *See Ark. Tchr. Ret. Sys.*, 879 F.3d at 484 ("The parties agree that plaintiffs established the preliminary elements to invoke the *Basic* presumption of reliance: defendants' misrepresentations were public, Goldman's shares traded in an efficient market, and the putative class members purchased Goldman stock at the relevant time (after the misstatements were made but before the truth was revealed).").

58. *Id.*

59. *In re* Goldman Sachs Grp., Inc. Sec. Litig., No. 10 Civ. 3461, 2018 WL 3854757, at *2 (S.D.N.Y. Aug. 14, 2018).

60. *Id.* at *3–4.

61. *Id.* at *4.

62. *Id.* at *5–6.

63. *Id.* at *6.

64. Ark. Tchr. Ret. Sys. v. Goldman Sachs Grp., Inc., 955 F.3d 254, 275 (2d Cir. 2020).

The Second Circuit affirmed the lower court's decision,[65] and, subsequently, Goldman filed a petition for certiorari.[66] The U.S. Supreme Court granted Goldman's petition.[67]

In a decision penned by Associate Justice Barrett, the Court held that (1) "*the generic nature of a misrepresentation often is important evidence of price impact that courts [in securities-fraud class actions] should consider at class certification*;" and (2) "defendants [in securities-fraud class actions] bear the burden of persuasion to prove a lack of price impact by a preponderance of the evidence [at class certification]."[68]

Pursuant to the first holding, the potential for securities fraud liability has been vastly expanded, such that any number of perfunctory corporate statements may now provide plaintiffs with a basis to bring a claim pursuant to Rule 10b-5.

III. ANALYSIS

The implications of enabling liability for deviations from generic statements, as was the case for Goldman, are broad and sweeping. Negative implications for consumer welfare and socially conscious corporate initiatives are likely due to the costliness of class action litigation.

A. Oversight and Litigation Costs

It is a long-standing principle in corporate law that the board of directors is responsible for overseeing the activities of their respective corporations.[69] While the board has traditionally not been responsible for all activity that occurs, it is expected to keep itself reasonably apprised of corporate happenings.[70] The purpose of this semi-detached duty of attention is to shield corporations, and their top management, against an unreasonable amount of litigation and the costs that come with it.[71] Litigation is costly for corporations, and it has become even more common as a result of the COVID-19 pandemic.[72]

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65. *Id.* at 275.

66. *See generally* Petition for a Writ of Certiorari, Goldman Sachs Grp., Inc. v. Ark. Tchr. Ret. Sys., 141 S. Ct. 1951 (2021) (No. 20-22220-222).

67. Press Release, Sullivan & Cromwell LLP, S&C Representing Goldman Sachs in Supreme Court Securities Case (Dec. 18, 2020), https://www.sullcrom.com/client-highlight-sandc-representing-goldman-sachs-in-supreme-court-securities-case [https://perma.cc/2N67-7TN9].

68. Goldman Sachs Grp., Inc. v. Ark. Tchr. Ret. Sys., 141 S. Ct. 1951, 1958 (2021) (emphasis added).

69. *See* AM. BAR ASS'N, MODEL BUS. CORP. ACT § 8.01 (AM. BAR ASS'N 2002) ("All corporate powers shall be exercised by or under the authority of the board of directors, and the business and affairs of the corporation shall be managed by or under the direction of, its board of directors . . . .").

70. *See In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 970 (Del. Ch. 1996); *Id.* at 968 ("Where a director *in fact exercises a good faith effort to be informed and to exercise appropriate judgment*, he or she should be deemed to satisfy fully the duty of attention. If the shareholders thought themselves entitled to some other quality of judgment than such a director produces in the good faith exercise of the powers of office, then the shareholders should have elected other directors.").

71. *See* Kenneth B. Davis, Jr., Dean, Univ. of Wisc. Sch. of Law, Presentation at the International Conference to Commemorate the Fortieth Anniversary of the Korean Commercial Code: The Director's Duty of Oversight – Pre-Enron; Post-Enron 3 (Sept. 2002), https://media.law.wisc.edu/m/jrjnz/oversight.pdf [https://perma.cc/HGY5-A49A] (stating that one argument against imposing a heightened duty is that it "might cost the corporation and its shareholders millions or billions of dollars").

72. *2020 Litigation Trends Survey*, NORTON ROSE FULBRIGHT (Feb. 10, 2021),

Historically, enhancements to corporate-governance requirements have been extremely expensive for America's biggest companies.[73] J.P. Morgan, for example, spends billions on compliance and oversight every year.[74] Retail companies, too, spend an exorbitant amount of money on oversight.[75] The expansion of the securities fraud regime will render corporations all the more wary of potential missteps that may give rise to costly class action litigation, and it is likely that they will assume additional compliance measures.

Corporate litigation expenses, too, are exorbitant. J.P. Morgan, Bank of America, and Citi Bank have each spent in excess of a billion dollars per year on litigation.[76] In a 2009 survey of Fortune 200 companies, the Lawyers for Civil Justice (LCJ) found that the average outside litigation cost per respondent was nearly $115 million.[77] Moreover, "[b]etween 2000 and 2008, average annual litigation costs as a percent of revenues increased 78 percent for the 14 companies providing data on average litigation costs as a percent of revenues for the full survey period."[78] According to the survey conducted by LCJ, litigation costs incurred by companies in the United States are four to nine times the amount incurred by their foreign counterparts.[79] Defending class action litigation is particularly expensive.[80] Historically, increased costs to U.S. corporations have prompted them to depart the country and establish themselves elsewhere, thereby harming domestic economic development.[81]

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https://www.nortonrosefulbright.com/en-us/knowledge/publications/0cd56e49/2020-litigation-trends-annual-survey [https://perma.cc/U4SY-FC2Z] (reporting that "31 percent of corporations reported an increase in disputes as a direct result of COVID-19").

73. *See* Deborah Solomon & Cassell Bryan-Low, *Companies Complain About Cost of Corporate-Governance Rules*, WALL ST. J. (Feb. 10, 2004), https://www.wsj.com/articles/SB107636732884524922 [https://perma.cc/M5QN-BHQ2] ("A survey of 321 companies . . . shows that businesses with more than $5 billion in revenue expect to spend an average of $4.7 million each implementing [additional oversight measures] . . . .").

74. Monica Langley & Dan Fitzpatrick, *Embattled J.P. Morgan Bulks Up Oversight*, WALL ST. J. (Sept. 12, 2013), https://www.wsj.com/articles/SB10001424127887324755104579071304170686532 [https://perma.cc/AVX4-G8TC].

75. Robert Thomason, *Walmart's $900 Million Compliance Costs Caused FCPA Probe's Major Financial Impact*, MLEX (June 25, 2019), https://mlexmarketinsight.com/news-hub/editors-picks/area-of-expertise/anti-bribery-and-corruption/walmarts-$900-million-compliance-costs-caused-fcpa-probes-major-financial-impact [https://perma.cc/C7M5-9PJH]; *see also* Kevin Lane & Matt Birk, *Enterprise Compliance for Retail Companies: Changing Requirements*, DELOITTE, https://www2.deloitte.com/us/en/pages/audit/articles/enterprise-compliance-retail-companies-video.html [https://perma.cc/8YBB-VRCR] ("The cost of compliance is always increasing.").

76. Langley & Fitzpatrick, *supra* note 74.

77. Laws. for Civ. Just., Civ. Just. Reform Grp. & U.S. Chamber Inst. for Legal Reform, Presentation at Duke Law School 2010 Conference on Civil Litigation: Litigation Cost Survey of Major Companies 2 (May 10–11, 2010), https://www.uscourts.gov/sites/default/files/litigation_cost_survey_of_major_companies_0.pdf [https://perma.cc/45ZP-P8LX] [hereinafter Litigation Cost Survey of Major Companies].

78. *Id.* at 3.

79. *Id.*

80. John H. Besiner et al., *The Class Action Chronicle*, SKADDEN (July 2021), https://www.skadden.com/insights/publications/2021/07/the-class-action-chronicle [https://perma.cc/MA22-K75D].

81. Zachary Green & Ivette Feliciano, *Corporations Go Overseas to Avoid U.S. Taxes*, PBS (Apr. 29, 2017), https://www.pbs.org/newshour/show/corporations-go-overseas-avoid-u-s-taxes [https://perma.cc/8NYF-WZQ2];. "If U.S. litigation costs are significantly higher than other countries, and the situation is left unchecked

Consistent with the foregoing, corporations are likely to impose extreme, costly oversight measures in order to avert multi-million-dollar litigation.[82] There is no mystery as to how a corporation might make up for these costs: by passing them on to consumers.[83]

B. Consumer Welfare

It is a fundamental economic principle that increased corporate costs will be reflected in consumer prices.[84] "The federal regulatory burden on businesses has increased by 28 percent in the last 15 years, according to a recent study released by the Mercatus Center at George Mason University."[85] The "study found that, on average, every 10 percent increase in regulatory restrictions produces a 0.687 percent increase in consumer prices. The correlation between regulations and prices was statistically significant across numerous industries."[86] Consumerism accounts for 70% of the United States' GDP,[87] though wages have effectively stagnated over the past several decades.[88] Reduced consumer spending is a contributing factor in every recession.[89] Accordingly, corporations are not the only parties likely to suffer from enhanced liability for securities fraud. Rather, the American public at large, by way of customers and economic participants, will be susceptible to its ills.

C. The Deterrence of Socially Conscious Corporate Initiatives

In recent years, corporations have engaged in an increasing amount of social

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as economic differences between countries narrow, the United States will be unable to compete effectively in the global marketplace." Litigation Cost Survey of Major Companies, *supra* note 77, at 3.

82. Davis, *supra* note 71.

83. *Infra* Part III.A.B.

84. Dunkelberg, *supra* note 3; *see, e.g.*, Gillian Friedman, *Diapers, Cereal and, Yes, Toilet Paper Are Going to Get More Expensive*, N.Y. TIMES (Apr. 29, 2021), https://www.nytimes.com/2021/04/29/business/consumer-goods-prices.html [https://perma.cc/NM3A-PZFE] ("Procter & Gamble is raising prices on items like Pampers and Tampax in September. Kimberly-Clark said in March that it will raise prices on Scott toilet paper, Huggies and Pull-Ups in June, a move that is 'necessary to help offset significant commodity cost inflation.'").

85. Tanya Xu, *Regulations Could be Increasing Consumer Prices*, REGUL. REV. (Sept. 29, 2016), https://www.theregreview.org/2016/09/29/xu-regulations-could-be-increasing-consumer-prices/ [https://perma.cc/L4CQ-3BNT].

86. *Id.*

87. Kai Ryssdal & Maria Hollenhorst, *What's Gonna Happen to the Consumer Economy?*, MARKETPLACE (Apr. 6, 2020), https://www.marketplace.org/2020/04/06/whats-gonna-happen-to-the-consumer-economy/ [https://perma.cc/GP72-EMZY].

88. *See* John Pavlus, *What's Causing Wage Stagnation in America*, KELLOGG INSIGHT?, KELLOGGINSIGHT (Dec. 2, 2019), https://insight.kellogg.northwestern.edu/article/wage-stagnation-in-america [https://perma.cc/7ZJK-KBSU] ("Since the 1970s, growth in 'real wages' (that is, the value of the dollars paid to employees after being adjusted for inflation) has slowed compared to overall economic productivity. . . . Wage growth has been slowing since the early 1970s, but 'the competition with China starts somewhere in the 1990s, and the process of automation is a product of the last ten or fifteen years.'").

89. Peter Cohan, *Consumer Spending is Keeping the Economy from Shrinking–But a New Survey of 10,000 Americans Says That Might End in 2020*, INC. (Dec. 4, 2019), https://www.inc.com/peter-cohan/consumer-spending-is-keeping-economy-from-shrinking-but-a-new-survey-of-10000-americans-says-that-might-end-in-2020.html [https://perma.cc/277S-VKGB].

activism.[90] For instance, a number of banks have made commitments to the promotion of racial justice.[91] Imagine a hypothetical scenario in which a bank's CEO is caught making derogatory remarks towards racial minorities—contrary to that bank's commitments. Now picture a CEO who frequently uses private jets, despite the fact that the company she helms has publicly committed to protecting the environment.[92] Further imagine the news reports of that misconduct spreading like wildfire across the media. Concurrent with these hypothetical scenarios, stock prices for the respective corporations take a nosedive.

Under the Supreme Court's decision in *Goldman Sachs*, a corporation could potentially face securities fraud liability in both of the aforementioned situations. Recall that the CEO of a corporation's scienter may bind that corporation in securities actions.[93] As a result, one CEO's reckless moment could cost their company and, later, its customers, millions of dollars.

IV. RECOMMENDATION

It is now incumbent upon the legislature to review the potential for adverse social effects and potential relocation of America's companies wrought by *Goldman Sachs v. ATRS* and revise Rule 10b-5, such that broad and generic statements may no longer give rise to securities fraud liability. In the interim, jurists ought to proceed cautiously and interpret the *Goldman* holding as narrowly as possible, consistent with the enhanced discretion provided to the judiciary in securities fraud cases.[94] Otherwise, corporate flight, inflated consumer prices, and corporate disregard for social activity could ensue.

The ESG movement is on the rise.[95] Should a corporation make *specific* statements

90. Gayle Markovitz & Samantha Sault, *What Companies Are Doing to Fight Systemic Racism*, WORLD ECON. F. (June 24, 2020), https://www.weforum.org/agenda/2020/06/companies-fighting-systemic-racism-business-community-black-lives-matter/ [https://perma.cc/KR84-7JVH]; *see also* Nadia Reckmann, *What is Corporate Social Responsibility?*, BUS. NEWS DAILY, https://www.businessnewsdaily.com/4679-corporate-social-responsibility.html [https://perma.cc/4KFV-QMCP] ("Corporate social responsibility (CSR) is a type of business self-regulation with the aim of being socially accountable. . . . There is no one way a company can embrace CSR . . . many companies focus on four broad categories. In today's socially conscious environment, employees and customers place a premium on working for and spending their money with businesses that prioritize CSR.").

91. *Making Progress Toward Racial Equality*, GOLDMAN SACHS, https://www.goldmansachs.com/our-commitments/diversity-and-inclusion/racial-equity/ [https://perma.cc/RSP2-FHSF]; *see also* Levi Sumagaysay, *Hours After CEO Decried Inequality, JPMorgan Seeks to Quash Call for Racial-Equity Audit*, MARKETWATCH (Apr. 8, 2021), https://www.marketwatch.com/story/hours-after-ceo-decried-inequality-jp-morgan-seeks-to-quash-call-for-racial-equity-audit-11617838297 [https://perma.cc/P3FX-C6K2]) ("JPMorgan Chase & Co. Chief Executive Jamie Dimon addressed inequality, racism and corporate responsibility in his annual letter to shareholders . . . .").

92. Private jets are terrible for the environment. A "report has revealed that UK private jet travel contributes 1 million ton[s] of CO2 to the atmosphere per year – the same amount that 450,000 cars create in the same timeframe." Megan C. Hills, *How Bad for the Environment is Taking a Private Jet? New Report Calls for a UK Ban by 2025*, EVENING STANDARD (Nov. 4, 2019), https://www.standard.co.uk/insider/living/how-bad-for-the-environment-is-taking-a-private-jet-a4217286.html [https://perma.cc/2M29-R6N2].

93. Richman, *supra* note 45.

94. Fisch, *supra* note 47.

95. Lizzy Gurdus, *ESG Investing to Reach $1 Trillion by 2030, Says Head of iShares Americas as Carbon Transition Funds Launch*, CNBC (May 9, 2021), https://www.cnbc.com/2021/05/09/esg-investing-to-reach-1-

regarding future conduct, its blatant deviations should result in liability (e.g., a corporation promises never to use fossil fuels, and is found to propel operations with such). The newfound development in securities law may, however, impose liability well beyond what is reasonable. Therefore, it would be prudent to amend § 240.10b-5 (and thus Rule 10b-5) to read that "it shall be unlawful . . . to make *any untrue statement* of a *specific material* fact," thereby shrinking the law's applicability so as not to encompass generic statements.

Of course, "specific" is an amorphous term, and judges would have to resolve its inherent ambiguities. This system of jurisprudence comports with the historical development of securities fraud law insofar as it has long been characterized by a judicial-legislative interplay.[96] A useful test for specificity would incorporate the following elements: (1) the statement does not govern merely *general* conduct, and (2) there is a reasonable expectation that the statement commands *particular* action.

The proposed amendment would stave off a potential influx of litigation, as well as costly preventative compliance measures[97] that the board of directors might otherwise impose. As a result, consumers would not have to bear the burden of inflated costs caused by an individual's reckless behavior that bears no relation to a firm's chief mission.[98] Instead, they would benefit from the cost savings.

Social justice activists need not worry that the recommended amendment would stifle the growth of socially conscious corporate behavior. Conversely, it would insulate corporations against the fear that a reckless executive might act out and subject the firm to liability. Rather than deter socially conscious behavior, *corporations would be empowered to make broad commitments and strive to achieve them*.

Companies would not risk liability for the unilateral acts of their CEOs that contradict a broad ESG statement; however, they could still incur liability for failure to conform their activity to a specific promised action. This would strike a reasonable balance between the tripartite policy governing securities law—the protection of investors, fairness in the market, and the reduction of systemic risk[99]—without unreasonably encumbering and restricting corporations. Moreover, to the extent that securities law exists to punish bad actors,[100] the existing framework only incentivizes companies to minimize the circumstances in which they may be punished and to refrain from making commitments regarding social activism.

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trillion-by-2030-head-of-ishares-americas.html [https://perma.cc/5GB5-GSF3]; Michael Wursthorn, *Tidal Wave of ESG Funds Brings Profit to Wall Street*, WALL ST. J. (Mar. 16, 2021), https://www.wsj.com/articles/tidal-wave-of-esg-funds-brings-profit-to-wall-street-11615887004 [https://perma.cc/DAM6-GSKP].

96. Fisch, *supra* note 47.

97. Langley & Fitzpatrick, *supra* note 74.

98. *See* Friedman, *supra* note 12 (stating that corporate directors and officers should maximize shareholder value). There may be instances in which fighting for racial or environmental justice is the chief aim of a given corporation. However, the existence of these objectives does not negate the utility of the proposed amendment, as offending behavior in such circumstances would almost certainly be encompassed by the proposed "specific material statement" language.

99. INT'L ORG. SEC. COMM'N, OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION I (May 2003), https://www.iosco.org/library/pubdocs/pdf/IOSCOPD154.pdf [https://perma.cc/39KK-AQ7C].

100. *See* Gilden, *supra* note 34 (discussing the need for punitive damages).

V. CONCLUSION

The continuous expansion of the securities fraud regime under Rule 10b-5 will give rise to adverse consequences for consumers, companies, social progress, and the American economy. The present iteration of Rule 10b-5, which enables liability for conduct contrary to general statements, provides little to no cognizable benefit. Rather, it provides an exploitable loophole for activist plaintiffs, who may overcome motions to dismiss and proceed on to the costly discovery process with ease. The continuation of this doctrine operates to the detriment of society insofar as companies are disincentivized from making commitments to social and environmental progress. Implementation of the revised regulation would alleviate each of these concerns and enable the further evolution of the socially conscious corporation.