Supreme Court Holds That "Pure Omissions" Are Not Actionable Under Rule 10b-5(b)

April 12, 2024

On April 12, 2024, in a highly anticipated decision, the Supreme Court held in *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*[1] that pure omissions are not actionable in private litigation under Rule 10b-5(b). Resolving a circuit split, the Court held that Rule 10b-5(b) does not support a "pure omissions" theory based on an alleged failure to disclose material information required by Item 303 of SEC Regulation S-K (Management's discussion and analysis of financial condition and results of operations, or MD&A). Instead, a "failure to disclose information required by [MD&A] can support a Rule 10b-5(b) claim only if the omission renders affirmative statements made misleading."[2] While the decision arose in the context of Item 303, which requires disclosure of "known trends and uncertainties" that have had or are "reasonably likely" to have a material impact on net sales, revenues or income from continuing operations,[3] the decision stands for the broader principle that Rule 10b-5(b) does not support pure omissions theories based on alleged violation of any disclosure requirement. Such claims remain viable, however, under Section 11 of the Securities Act of 1933. This ruling provides welcome clarity to issuers and eliminates the risk of pure-omission claims under Rule 10b-5(b) based on the judgment-based requirements of MD&A.

The Circuit Split. The Supreme Court's decision resolved a split between the Second Circuit and the Ninth Circuit. In 2014, the Ninth Circuit in *In re NVIDIA Corporation Securities Litigation* held that a violation of Item 303 of Regulation S-K was not actionable by private litigants under Section 10(b) of the Exchange Act.[4] Just a few months later, the Second Circuit in *Stratte-McClure v. Morgan Stanley* held that a violation of MD&A's requirements would be actionable under Section 10(b) and Rule 10b-5 if plaintiffs met the materiality requirements set forth in *Basic Inc. v. Levinson*.[5] The Second Circuit reasoned that courts "have long recognized that a duty to disclose under Section 10(b) can derive from statutes or regulations that obligate a party to

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1 No. 22-1165, slip op. (U.S. Apr. 12, 2024).

2 *Id.* at 7.

3 17 CFR § 229.303(b)(2)(ii).

4 *In re NVIDIA Corp. Securities Litigation*, 768 F.3d 1046 (9th Cir. 2014).

5 *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94 (2d Cir. 2015) (citing *Basic Inc. v. Levinson*, 485 U.S. 224 (1988)).

speak[,]" and that a "reasonable investor would interpret the absence of an Item 303 disclosure to imply the non-existence of 'known trends or uncertainties[.]'"[6]

The Supreme Court's Decision. The *Macquarie* case involved claims under Rule 10b-5(b) based on Macquarie's alleged failure to disclose the impact of prospective regulations, which were expected to dramatically reduce demand for the infrastructure-related business of an affiliate. Plaintiff claimed that the impact of the prospective regulation constituted a "known trend or uncertainty" required to be disclosed under Item 303, but Plaintiff did not identify an affirmative statement by Macquarie that was rendered misleading by the omission of that information. Macquarie argued that a failure to disclose information required by Item 303, alone, could not serve as the basis for private fraud litigation under Section 10(b).

The Second Circuit allowed the investor lawsuit to proceed based on this failure to comply with Item 303. Macquarie appealed, requesting that the Supreme Court clarify that Section 10(b) liability "arises only where a company makes a statement that is untrue or misleading without further disclosure—not when the company allegedly fails to make all disclosures required by SEC rules."[7]

The Supreme Court agreed with Macquarie and vacated the Second Circuit's decision, remanding for further proceedings. The Supreme Court's analysis began with the text of Rule 10b-5(b), which makes it unlawful for issuers to "make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading."[8] The Court explained that this rule "accomplishes two things."[9] It prohibits (i) "false statements or lies" and (ii) "omitting a material fact necessary 'to make the statements made . . . not misleading."[10] The Court determined that the second prohibition bars only "half-truths" and does not extend to pure omissions.[11]

"A pure omission occurs when a speaker says nothing, in circumstances that do not give any particular meaning to that silence."[12] For example, if a company fails to provide all information required by MD&A, the omission of the information required has no special significance because no information was disclosed. "Half-truths, on the other hand, are representations that state the truth only so far as it goes, while omitting

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6 *Id.* at 102 (citing 17 C.F.R. § 229.303(a)(3)(ii)).

7 Petition for Writ of Certiorari at 13, *Macquarie Infrastructure Corp. v. Moab Partners*, No. 22 1165 (May 30, 2023).

8 17 CFR § 240.10b–5(b).

9 Slip op. at 4.

10 *Id.* at 5 (quoting 17 CFR § 240.10b–5(b)).

11 *Id.*

12 *Id.*

critical qualifying information."[13] The "difference between a pure omission and a half-truth is the difference between a child not telling his parents he ate a whole cake and telling them he had dessert."[14]

The Court explained that Rule 10b-5(b) "does not proscribe pure omissions" because it prohibits only the omission of "material facts necessary to make the 'statements made . . . not misleading.'"[15] Thus, issuers need only disclose information necessary to ensure that "statements made are clear and complete."[16] In light of the scope of Rule 10b-5(b)'s prohibitions, the Supreme Court concluded that "the failure to disclose information required by Item 303 can support a Rule 10b-5(b) claim only if the omission renders affirmative statements made misleading."[17]

Impact and Takeaways. The Supreme Court's landmark decision confirms that a failure to make disclosure that is responsive to a disclosure requirement, standing alone, does not give rise to a private right of action under Rule 10b-5(b), and has reach beyond Item 303 of Regulation S-K. In so doing, it removed significant uncertainty and risk of Rule 10b-5(b) liability based on pure omissions theories under the judgment-based disclosure regime of MD&A. The Court's decision, by its terms, applies equally to other disclosure obligations under Regulation S-K, including those related to cybersecurity risk management and climate change. Plaintiffs are now required to identify a statement they allege is rendered misleading by the omitted information, and further litigation will undoubtedly focus on the significance of omitted information to existing statements.

Although the Court declined to expand the scope of the private right of action under Rule 10b-5(b), issuers are also subject to SEC review and enforcement action regarding omissions in MD&A, so must remain vigilant about their disclosures. Moreover, the Court's decision does not foreclose plaintiffs from filing claims concerning Item 303 of Regulation S-K under a "half-truths" theory—i.e., that the information omitted from MD&A renders other statements made misleading. In addition, pure omissions theories remain viable under Section 11 of the Securities Act.

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Please do not hesitate to contact us with any questions.

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13 *Id.*

14 *Id.*

15 *Id.*

16 *Id.*

17 *Id.* at 7.

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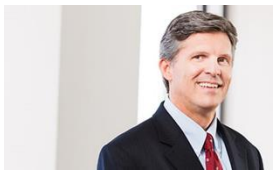

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