LEGAL UPDATES

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Supreme Court Holds Pure "Omissions" in MD&A Disclosure Cannot Support Liability Under Rule 10b-5

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On April 12, 2024, the U.S. Supreme Court held in *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, in a unanimous opinion authored by Justice Sonia Sotomayor, that "pure omissions" made in required disclosures do not support a private right of action under the anti-fraud provisions of Securities and Exchange Commission (SEC) Rule 10b-5. The issue presented to the Court in *Macquarie Infrastructure* was whether the failure to disclose information required by Item 303 of Regulation S-K can support a private securities fraud claim under Securities Exchange Act of 1934 (Exchange Act) Section 10(b) and Rule 10b-5(b), when the omission does not render any "statements made" misleading.

Generally, Item 303 requires companies to disclose certain information in the Management's Discussion and Analysis (MD&A) section of filings with the SEC, such as 10-Ks and 10-Qs, with the objective to "provide material information relevant to an assessment of the financial condition and results of operations" of the company, focusing on "material events and uncertainties" that are "reasonably likely to cause reported financial information not to be necessarily indicative of" the company's current or future financial condition. In deciding *Macquarie Infrastructure*, the Court eliminated significant regulatory uncertainty that had arisen concerning the scope of private liability under Section 10(b) and Rule 10b-5 following the Second Circuit's expansion of such liability to cover allegedly omitted "trends" and "uncertainties" in Item 303 disclosure. *Macquarie Infrastructure* settled a split on this issue between the Second Circuit and the Third, Ninth, and Eleventh Circuits, which held in similar cases that Item 303 does not create an affirmative duty to disclose

under Section 10(b) and therefore does not automatically give rise to Section 10(b) liability where an Item 303 disclosure violation may exist.

The Court reversed and vacated the Second Circuit's decision in *Macquarie Infrastructure*, clarifying and reiterating that an omission violates Section 10(b) and Rule 10b-5(b) only when the omission renders other "affirmative statements" made misleading. In other words, the Court found that while Rule 10b-5(b) "prohibits 'any untrue statement of a material fact'—i.e., false statements or lies— [and] also prohibits 'omitting a material fact necessary to make statements made … not misleading," the mere failure to disclose information required by Item 303 does not automatically give rise to Section 10(b) and Rule 10b-5 liability.

The facts

A subsidiary of Macquarie Infrastructure Corporation operated terminals storing bulk liquid commodities, including No. 6 fuel oil, which has a sulfur content close to 3%. In 2016, the United Nations' International Maritime Organization (IMO) adopted IMO 2020, a regulation that capped the sulfur content of fuel oil used in shipping at 0.5% by 2020. Macquarie did not discuss IMO 2020 in its public disclosure documents. However, in 2018 Macquarie announced a decrease in storage contracts in part due to the decline in the No. 6 fuel oil market. Macquarie's stock price fell about 41%.

Moab Partners, L.P. sued Macquarie and various officer defendants, alleging a violation of Section 10(b) and Rule 10b-5(b), claiming that Macquarie's public filings were false and misleading because they did not disclose to investors a "known trend or uncertainty" regarding the impact of IMO 2020 on the demand for storage capacity for No. 6 fuel oil, which should have been disclosed under Item 303.

The District Court dismissed Moab's complaint, and the Second Circuit reversed, holding that the "failure to make a material disclosure required by Item 303 can serve as a basis…for a claim under Section 10(b)."

The Court's analysis

Section 10(b) makes it unlawful for any person to use or employ, in connection with the purchase or sale of a security, any manipulative or deceptive device or contrivance. Rule 10b–5 implements Section 10(b) by making it unlawful for issuers of securities to "make any untrue statement of 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." Because Rule 10b–5(b) applies to "statements made," it has generally been accepted—as the Court previously articulated in the landmark disclosure case of *Basic Inc. v. Levinson*—that "[s]ilence, absent a duty to disclose, is not misleading under Rule 10b–5."

The Court unanimously reversed and vacated the Second Circuit's decision in *Macquarie Infrastructure*, holding that Rule 10b-5 prohibits falsehoods (untrue statements of a material fact) and half-truths (omissions of material facts necessary to make statements made not misleading) but does not "create an affirmative duty to disclose any and all material information." Instead, the Court explained that Rule 10b-5 requires identifying affirmative assertions (i.e., "statements made") before determining whether additional facts must be disclosed in order to make those statements "not misleading." Additionally, the Court reiterated that companies can control what they are required to disclose under Section 10(b) and Rule 10b-5(b) by controlling what they say to the market and that a duty to disclose does not automatically render silence misleading. The Court summarized its holding as "confirm[ing] 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."

The Court's decision also drew a distinction between liability for "pure omissions" under Section 10(b) and Rule 10b-5(b) and liability for "pure omissions" under Section 11(a) of the Securities Act of 1933 (Section 11(a)). Unlike Section 10(b) and Rule 10b-5(b), Section 11(a) imposes liability for "pure omissions" by prohibiting registration statements that "contain an untrue statement of material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein not misleading." The Court also emphasized that the SEC may independently pursue enforcement action where it determines an issuer has failed to comply with Item 303, pursuant to the requirements of Section 13(a) of the Exchange Act that issuers provide investors with public disclosure "in accordance with such rules and regulations as the Commission may prescribe."

What this means to you

As the Society for Corporate Governance argued in its *amicus* brief, the Court's rejection of the Second Circuit's approach in *Macquarie Infrastructure* will help to reinforce the SEC's intention that MD&A disclosures under Item 303 should "give the investor the opportunity to look at the company through the eyes of management"—rather than promoting "a counterproductive paradigm shift" to litigation-averse drafting emphasizing the over-disclosure of potentially immaterial "trends" and "uncertainties" that would not benefit investors.

While "pure omissions" will not give rise to private liability under Rule 10b-5(b), the Court reiterated in *Macquarie Infrastructure* that private parties remain free to bring claims based on Item 303 violations that create misleading "half-truths," and the SEC retains authority to prosecute violations of its own regulations. Accordingly, companies must continue to evaluate whether a decision not to speak on a particular known trend or uncertainty could render affirmative statements in other required disclosures "misleading," remembering also that pure omissions may still be actionable under Section 11(a) of the Securities Act.

Contact us

Husch Blackwell's Securities & Corporate Governance team regularly advises our clients concerning SEC reporting disclosures and related issues. Should you have any questions, please do not hesitate to contact Craig Adoor, Steve Barrett, Robert Joseph, Victoria Sitz, Andrew Spector, Ashley Inbau, or your Husch Blackwell attorney.