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Supreme Court Rules that MD&A Omission Does Not Give Rise to a Claim for Securities Fraud

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On April 12, 2024, the Supreme Court issued a highly-anticipated decision in *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, ruling that a "pure omission" is not actionable in private litigation under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5(b) thereunder, even if the omitted information was required to be disclosed pursuant to other SEC rules. Writing for a unanimous Court, Justice Sotomayor's opinion nevertheless makes clear that "half-truths," as distinguished from pure omissions, remain actionable under Item 303 of Regulation S-K.

Background

Macquarie, at the time a publicly-traded corporation, owns infrastructure-related businesses, including bulk liquid storage terminals that handle commodities such as petroleum, biofuels, and other chemicals. Changes in international maritime regulations in 2016 led to a reduction in the use of No. 6 fuel oil in the shipping industry, which in turn led to a reduction in storage of that fuel at Macquarie's facilities. Macquarie did not discuss the change in maritime regulations in its SEC filings, but did disclose in February 2018 that its storage capacity had contracted in part due to the structural decline in the No. 6 fuel oil market. The company's stock price fell approximately 41%, and Moab Partners sued Macquarie and various officers and directors alleging, among other things, violation of the general antifraud provisions under the federal securities laws, Section 10(b) of the Securities Exchange Act and Rule 10b-5.

Moab argued that Macquarie's disclosures were false and misleading because they concealed from investors that its largest product, No. 6 fuel oil, had effectively been banned due to the change in maritime regulations. Moab asserted that Macquarie had a duty to disclose the changes in its storage capacity under Item 303 of Regulation S-K (Management's Discussion and Analysis of Financial Condition and Results of Operation, or MD&A), and by failing to do so, also violated Section 10(b) and Rule 10b-5. Item 303 requires companies to disclose, among other things, "known trends or uncertainties that have had or that are reasonably likely to have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations." Although the district court

dismissed Moab's complaint, the Second Circuit reversed, concluding that Macquarie's Item 303 violation also gave rise to an actionable claim under Section 10(b) and Rule 10b-5(b). The Second Circuit's decision reflected a circuit split as to whether a failure to make a disclosure required under SEC rules—and Item 303 in particular—could support a claim under Section 10(b) and Rule 10b-5(b) in the absence of an affirmative statement that was rendered misleading.

The Supreme Court's Ruling

Employing a textual approach, the Court concluded that a pure omission is not actionable under Rule 10b-5. The Court observed that Rule 10b-5 prohibits "any untrue statement of a material fact" or omitting a material fact necessary "to make the statements made . . . not misleading." The case therefore turned on whether the second prohibition bars only half-truths or also extends to pure omissions if another SEC rule requires disclosure of the omitted information.

The Court explained that a pure omission occurs "when a speaker says nothing, in circumstances that do not give any particular meaning to that silence," whereas half-truths are "representations that state the truth only so far as it goes, while omitting critical qualifying information." The Court then likened "the difference between a pure omission and a half-truth" to "the difference between a child not telling his parents he ate a whole cake and telling them he had dessert."

With this distinction in mind, the unanimous Court concluded that Rule 10b-5 does not extend to pure omissions. The Court contrasted the language of Rule 10b-5(b) with the language of Section 11(a) of the Securities Act of 1933, which prohibits a registration statement that "contain[s] an untrue statement of a material fact or omit[s] to state a material fact required to be stated therein or necessary to make the statements therein not misleading." By its terms, Section 11 creates liability for pure omissions, but there is no similar text in Section 10(b) or Rule 10b-5(b). "Logically and by its plain text," the Court declared, Rule 10b-5(b) requires "identifying affirmative assertions (i.e., 'statements made') before determining if other facts are needed to make those statements 'not misleading'." Thus, Rule 10b-5(b) does not proscribe pure omissions.

Implications

Macquarie represents an important reaffirmation that Section 10(b) and Rule 10b-5 are antifraud provisions that do not require disclosure of all material information. Private claims based on alleged omissions under Item 303 had proliferated in the Second Circuit—the country's busiest circuit for securities litigation—since the Second Circuit's decision in *Stratte-McClure* v. *Morgan Stanley*, 776 F.3d 94 (2d Cir. 2015), which gave rise to the circuit split that *Macquarie* resolved. The Supreme Court had already granted certiorari on this issue once before only to have the case settle before it could be argued. With the issue now decided, issuers no longer face the risk of being sued for securities fraud based on pure omission claims.

With that said, the Court was careful not to tread beyond the narrow question of pure omissions. The unanimous opinion did not address what constitutes "statements made," when a statement is misleading as a half-truth, or whether either Rule 10b-5(a) or 10b-5(c) support liability for pure omissions. The Court also left the door open for private plaintiffs to bring claims based on Item 303 if an omission creates misleading half-truths, which is likely to be the approach going forward for the plaintiffs' bar. The SEC also remains free to enforce its rules or issue new rules to address violations of Item 303 by pure omission.

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