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Supreme Court Holds That Securities Fraud Statute Does Not Proscribe Pure Omissions

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The U.S. Supreme Court recently held that the anti-fraud provision of the Securities Exchange Act does not prohibit "pure omissions," but only false statements or misleading half-truths. The unanimous decision in *Macquarie Infrastructure Corp. v. Moab Partners, L.P.* (April 12, 2024) holds that § 10(b) of the Exchange Act and the SEC's Rule 10b-5(b) require a *statement* that is false or misleading. A pure omission that does not render a *statement* false or misleading is not actionable, at least in private actions.

Factual Background

The *Macquarie* case involved the impact of an impending regulation known as IMO 2020, the International Maritime Organization's global limit on sulfur content in marine fuel. Plaintiffs alleged that defendants had concealed the extent of their exposure to No. 6 fuel oil (which was subject to IMO 2020), the regulation's potential impact on defendants' customer base, the capital expenditures that would be needed to repurpose No. 6 fuel-oil storage tanks for other uses, and the related risks to defendants' revenues and dividends.

The District Court dismissed the case, holding that defendants had not made any actionable misstatements or omissions. The Second Circuit, in a summary order, reversed and remanded as to some of the alleged omissions.

The Second Circuit started with the familiar principle that a duty to speak generally arises where (*i*) a statute or regulation affirmatively requires disclosure or (*ii*) a failure to disclose would make other statements false or misleading even in the absence of an independent disclosure duty. The court held that plaintiffs had sufficiently pled both types of disclosure obligations.

- Relying on Circuit precedent, the court held that Item 303 of SEC Regulation S-K – which requires disclosure of "presently known" trends or uncertainties that are

"reasonably likely to have material effects" on the issuer – creates a disclosure duty that can serve as the predicate for a private action alleging material omissions under the Securities Act and the Exchange Act if the other elements of those claims are sufficiently pled. The court concluded that plaintiffs had sufficiently alleged that defendants had been aware of IMO 2020's likely impact and could not have been "objectively reasonable" in determining that the impact would not be material.

- The court also held that, "[h]aving chosen to speak about their base of customers, Defendants had a duty to speak accurately, giving all material facts in addressing those issues to permit investors to evaluate the potential risks." At the pleading stage, plaintiffs had sufficiently pled that defendants had not "revealed the information necessary for the investing public to make a proper assessment of the alleged risks" of customer loss.

Defendants petitioned for certiorari, asking the Supreme Court to consider whether an issuer's alleged failure to make a disclosure required by Item 303 can support a private claim for securities fraud under § 10(b) of the Exchange Act "even in the absence of an otherwise-misleading statement." The Court granted certiorari and reversed.

Supreme Court's Decision

The Court's opinion focused on the language of Rule 10b-5(b), which prohibits making "any untrue *statement* of a material fact" or failing "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" (emphasis added). Thus, Rule 10b-5(b) prohibits only two things: false statements (lies) and half-truths (statements that are misleading because a material fact has been omitted).

But although Rule 10b-5(b) prohibits half-truths, it "does not proscribe pure omissions," which occur "when a speaker says nothing, in circumstances that do not give any particular meaning to that silence." The Court contrasted the Rule's language with that of § 11(a) of the Securities Act, which expressly imposes liability for pure omissions.

Turning to Item 303, which requires disclosure of known trends and uncertainties, the Court held 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 misleading." The Court rejected plaintiffs' contention that the omission of a known trend or uncertainty (here, the alleged failure to disclose IMO 2020's impact) necessarily makes an issuer's Item 303 disclosures misleading on the theory that reasonable investors would expect those disclosures to include *all* known trends and uncertainties. That argument, said the Court, "reads the words 'statements made' out of Rule 10b-5(b) and shifts the focus of that Rule and § 10(b) from fraud to disclosure."

The Court observed that the SEC has authority to prosecute violations of its regulations, including Item 303, but a private party cannot use Item 303 to challenge pure omissions. Private parties can sue only if the alleged Item 303 violations "create misleading half-truths."

Implications

The unanimous decision in *Macquarie* drives a stake into the heart of Exchange Act liability theories based on pure omissions, but the ruling might have only limited impact in the real world. If plaintiffs can frame their claims as based on half-truths (which satisfy Rule 10b-5(b)'s "statement" requirement), rather than on pure omissions, *Macquarie*'s restriction of liability does not apply.

In fact, the Court noted that plaintiffs here spent much time "insisting that this case is about half-truths rather than pure omissions," and the Second Circuit had sustained the half-truth claim at the pleading stage. But the Court did not address that liability theory because the grant of certiorari had been addressed only to "the Second Circuit's pure omission analysis, not its half-truth analysis."

Nevertheless, the Court's rejection of liability based solely on a failure to disclose something allegedly required by Item 303 could make a difference in some cases.

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