

Circuit Court Decisions Addressing Disclosure Requirements Under Section 10(b)

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Second Circuit: Under *Omnicare*, Issuers Need Not Disclose Every Piece of Information That Runs Counter to Their Statements of Opinion, Provided Those Opinions “Fairly Align” with the Information in Their Possession at the Time

On March 4, 2016, the Second Circuit held the Supreme Court’s decision in *Omnicare v. Laborers’ Dist. Council Constr. Indus. Pension Fund*, 135 S. Ct. 1318 (2015), “does not impose liability merely because an issuer failed to disclose information that ran counter to an opinion expressed in the registration statement,” provided the opinion “fairly align[ed] with the information in the issuer’s possession at the time.” *Tongue v. Sanofi*, 816 F.3d 199 (2d Cir. 2016) (Parker, J.).

The Second Circuit stated that under *Omnicare*, omissions may render opinions actionable if the omitted information “conflict[s] with what a reasonable investor would take from the statement itself.” *Id.* (quoting *Omnicare*, 135 S. Ct. 1318). However, the Second Circuit observed that the *Omnicare* Court “cautioned against an overly expansive reading of this standard.” The Supreme Court explained that “[r]easonable investors understand that opinions sometimes rest on a weighing of competing facts” and they do not “expect that every fact known to an issuer supports its opinion statement.” *Omnicare*, 135 S. Ct. 1318. Significantly, the Supreme Court made it clear that a statement of opinion “is not necessarily misleading when an issuer knows, but fails to disclose, some fact cutting the other way.”

In the case before it, the Second Circuit found defendants’ opinions regarding the expected timing of FDA approval were not rendered misleading by defendants’ failure to disclose the FDA’s concerns about the company’s clinical testing methodology. The Second Circuit held defendants had no obligation to “disclose[] the FDA feedback merely because it tended to cut against their projections.” *Sanofi*, 816 F.3d 199.

Second Circuit: (1) Item 303 of Regulation S-K Requires the Registrant’s Actual Knowledge of a Trend or Uncertainty; and (2) “Probability” Standard Only Applies to FAS 5’s Disclosure Requirement If There Was No Manifestation of a Potential Claim

On March 29, 2016, the Second Circuit held that Item 303 of Regulation S-K, which mandates the disclosure of certain “known trends or uncertainties” in a public company’s Form 10-Ks and other SEC filings, “requires the registrant’s *actual knowledge* of the relevant trend or

uncertainty” “rather than a lesser standard of recklessness or negligence” (emphasis added).^[1] *Ind. Pub. Ret. Sys. v. SAIC*, 818 F.3d 85 (2d Cir. 2016) (Lohier, J.). Considering the question squarely for the first time, the Second Circuit determined that “Item 303 requires the registrant to disclose only those trends, events, or uncertainties that it actually knows of when it files the relevant report with the SEC.” The court found this interpretation supported by both the “plain language of Item 303” as well as the “SEC’s interpretation of Item 303.” Significantly, the Second Circuit stated that “[i]t is not enough” for purposes of Item 303’s disclosure requirements that the registrant “*should have known* of the existing trend, event, or uncertainty” (emphasis added).

The Second Circuit also considered the standard for claims alleging a failure to disclose a loss contingency for unasserted claims as required under Financial Accounting Standard 5 (“FAS 5”) of the Generally Accepted Accounting Principles (“GAAP”).^[2] The court held that a “probability” standard applies to FAS 5-based claims only if there has been “no manifestation by a potential claimant of an awareness of a possible claim or assessment.” In cases where a potential claimant has manifested awareness of a possible claim, the court held that FAS 5’s disclosure requirements apply if a loss in connection with that claim is a “reasonable possibility.”

Ninth Circuit: Pharmaceutical Company’s Decision to Discuss Certain Studies Supporting a Drug’s Safety Necessitated Disclosure of Another Study Linking the Drug to Cancer

On October 26, 2016, the Ninth Circuit held that once a pharmaceutical company chose to represent that animal studies supported the safety of its new weight loss drug, the company was then required to disclose the existence of an animal study linking the drug to cancer. *Schueneman v. Arena Pharm.*, 840 F.3d 698 (9th Cir. 2016) (Bybee, J.).

The court explained that under the Supreme Court’s decision in *Matrixx Initiatives v. Siracusano*, 563 U.S. 27 (2011), “companies can control what they have to disclose under [the securities laws] by controlling what they say to the market” (quoting *Matrixx*, 563 U.S. 27). Once a company opts to “tout” positive information to the market, however, the company is then “bound to do so in a manner that wouldn’t mislead investors” (quoting *Berson v. Applied Signal Tech.*, 527 F.3d 982 (9th Cir. 2008)). Specifically, the company must “disclos[e] adverse information that cuts against the positive information.”

In the case before it, the Ninth Circuit rejected defendants’ claim that the allegations reflected merely “a good-faith scientific disagreement between the FDA and [the company] about the meaning of” the study linking the drug to cancer. The court reasoned that the company “could have remained silent about the dispute or it could have addressed its discussions with the FDA head-on[,]” but it could not “express confidence by claiming that all of the data was running in [the company’s] favor.”

^[1] Item 303 of Regulation S-K requires a registrant to “[d]escribe any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations.”

^[2] Under FAS 5, an issuer must “disclose a loss contingency when a loss is a ‘reasonable possibility,’ meaning that it is ‘more than remote but less than likely.’” *Id.* (quoting FAS Board, Statement of FAS 5).

Authors and
Contacts

Paul Gluckow

Partner and General Counsel

pgluckow@stblaw.com

+1-212-455-2653

Peter Kazanoff

Partner

pkazanoff@stblaw.com

+1-212-455-3525

Jonathan Youngwood

Partner

jyoungwood@stblaw.com

1-212-455-3539

