

## Circuit Court Decisions Addressing Actionable Misstatements and Omissions

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### **Third Circuit: A Company Has No Stand-Alone Obligation to Disclose Alleged Regulatory Violations by an Affiliated Entity**

On November 14, 2018, the Third Circuit affirmed dismissal of a securities fraud action alleging that a company failed to disclose regulatory violations by an affiliated entity. [City of Cambridge Ret. Sys. v. Altisource Asset Mgmt. Corp.](#), 908 F.3d 872 (3d Cir. 2018) (Fisher, J.). The Third Circuit found “no authority to support the conclusion that [the defendant company] was obligated to disclose the flaws of a separate entity in its own filings.”

The Third Circuit further determined that alleged misstatements made by any entities affiliated with the defendant company had no “legal significance” with respect to plaintiffs’ Rule 10b-5 claims under the Supreme Court’s decision in *Janus Capital Grp. v. First Derivative Traders*, 564 U.S. 135 (2011), which limits Rule 10b-5(b) liability to “the person or entity with ultimate authority over the statement.”<sup>[1]</sup>

### **Fourth Circuit: Once a Company Decides to Speak on a Topic, the Company Has a Duty to Disclose All Material Information Concerning That Topic**

On February 22, 2018, the Fourth Circuit revived a dismissed securities fraud action alleging that a medical device company failed to disclose its fraudulent insurance coding scheme. [Singer v. Reali](#), 883 F.3d 425 (4th Cir. 2018) (King, J.). Because the company chose “to speak about its reimbursement practices,” the court found plaintiffs adequately alleged that the company had “a duty to disclose its alleged illegal conduct” in connection with those practices.

The Fourth Circuit rejected defendants’ argument that there were no allegations that any court or government agency had deemed the reimbursement scheme illegal. The court explained that “the duty to disclose may extend to uncharged and unadjudicated illegal conduct.”

The Fourth Circuit also found meritless defendants’ contention that the company had never “specifically asserted it was complying with a particular law.” The court noted that plaintiffs did not rely on “mere generic assertions of legal compliance.” Rather, plaintiffs based their claim on “the [c]ompany’s choice to speak about its reimbursement practices . . . without telling the whole, material truth.”

### **Fifth Circuit: Statements Concerning Transparency, Quality and Corporate Responsibility Are Inactionable Puffery**

On October 3, 2018, the Fifth Circuit affirmed dismissal of a securities fraud action alleging that a grocery retailer made misstatements concerning the company’s “commitment to transparency, quality and corporate responsibility,” among other alleged misstatements. *Emps. Ret. Sys. v. Whole Foods Mkt.*, 905 F.3d 892 (5th Cir. 2018) (King, J.). The court held these “generalized statements” constituted inactionable puffery even though the retailer had “built a brand around holding itself to higher ethical standards than its competitors.” The court found that a “reasonable investor” would not assess the company’s value based on such “self-serving statements.” Rather, reasonable investors would “rely on facts to determine whether” the company is in fact “transparent and otherwise holds itself to high standards.”

**Tenth Circuit: A Company Has No Duty to Disclose Preliminary Merger Discussions Provided It Does Not Say Anything “Inconsistent” With the Existence of Such Discussions**

On May 11, 2018, the Tenth Circuit held that an energy company and its executives had no duty to disclose preliminary merger discussions with a competing energy firm because defendants had not made any statements that were “inconsistent” with the possibility that the company was engaging in such discussions. *Emps. Ret. Sys. of Rhode Island v. Williams Cos.*, 889 F.3d 1153 (10th Cir. 2018) (Hartz, J.). The court emphasized that “Rule 10b-5 does ‘not create an affirmative duty to disclose any and all material information.’” *Id.* (quoting *Matrixx Initiatives v. Siracusano*, 563 U.S. 27 (2011)). Rather, Rule 10b-5 requires disclosure “only when necessary to make statements made, in the light of the circumstances in which they were made, not misleading.” *Id.* (quoting *Matrixx*, 563 U.S. 27).

The court further found that the merger discussions were not material under the probability/magnitude test set forth in *Basic v. Levinson*, 485 U.S. 224 (1988). The Tenth Circuit explained that *Basic*’s “fact-specific” inquiry requires courts to “analyze the probability that a merger will succeed and the magnitude of the transaction.” The Tenth Circuit stated that “merger discussions are generally not material in the absence of a serious commitment to consummate the transaction.” In the case before it, the court noted that there were no allegations of “concrete offers, specific discussions, or anything more than vague expressions of interest.” The Tenth Circuit determined that the allegations were “fully consistent with there being no commitment whatsoever.”

[1] Please [click here](#) to read our discussion of the Supreme Court’s decision in *Janus*.

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