No. 16-581

In the Supreme Court of the United States

LEIDOS, INC., FKA SAIC, INC., PETITIONER

v.

INDIANA PUBLIC RETIREMENT SYSTEM, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING RESPONDENTS

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QUESTION PRESENTED

Whether an issuer's submission of a Form 10-K that discloses some but not all of the trends, events, or uncertainties it was required to disclose under Item 303 of SEC Regulation S-K, 17 C.F.R. 229.303, is categorically exempt from liability under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), and SEC Rule 10b-5, 17 C.F.R. 240.10b-5.

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INTEREST OF THE UNITED STATES

The United States, through the Department of Justice and the Securities and Exchange Commission (SEC or Commission), administers and enforces the federal securities laws, including the laws at issue in this case. The question presented here arises in both private civil actions and government enforcement suits.

STATEMENT

1. This case presents a question about Sections 10(b) and 13(a) of the Securities Exchange Act of 1934 (Exchange Act), 15 U.S.C. 78j(b), 78m(a).

a. Section 10(b) makes it unlawful for any person "[t]o use or employ, in connection with the purchase or sale of any security * * * any manipulative or deceptive device or contrivance in contravention of" SEC rules. 15 U.S.C. 78j(b). SEC Rule 10b-5 implements Section

10(b) and makes it unlawful for any person, in connection with the purchase or sale of a security, (a) to "employ any device, scheme, or artifice to defraud"; (b) to "make any untrue statement of a 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"; or (c) to "engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person." 17 C.F.R. 240.10b-5. "Section 10(b) is aptly described as a catchall" anti-fraud provision. *Chiarella* v. *United States*, 445 U.S. 222, 234-235 (1980). And "Rule 10b-5 is coextensive with the coverage of § 10(b)." *SEC* v. *Zandford*, 535 U.S. 813, 816 n.1 (2002).

Section 10(b) and Rule 10b-5 may be enforced by the SEC. Suits to enforce those provisions may also be brought by aggrieved private parties, under an implied private right of action that Congress has "ratified." *Stoneridge Inv. Partners, LLC* v. *Scientific-Atlanta, Inc.*, 552 U.S. 148, 165 (2008). The SEC or a private plaintiff must show (1) a material misrepresentation or omission; (2) made with scienter; (3) in connection with the purchase or sale of a security. *Dura Pharm., Inc.* v. *Broudo*, 544 U.S. 336, 341 (2005). A private plaintiff must in addition prove (4) reliance; (5) economic loss; and (6) loss causation. *Id.* at 341-342.

b. Section 13(a) of the Exchange Act, 15 U.S.C. 78m(a), provides that issuers of registered securities "shall file with the Commission" annual and other periodic reports that contain "such information * * * as the Commission shall require," regarding, *inter alia*, "the organization, financial structure and nature of the busi-

ness." 15 U.S.C. 78*l*(b), 78m(a). The SEC enforces Section 13(a), see 15 U.S.C. 78u-2, but there is no private right of action for its violation.

SEC regulations state that issuers "shall" use Form 10-K for annual reports. 17 C.F.R. 249.310(a). Form 10-K identifies items that issuers must disclose, corresponding to different categories of information. See SEC, *Form 10-K*.[1] Centrally relevant here is Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" (MD&A), where the company must "[f]urnish the information required by Item 303 of Regulation S-K." *Ibid.*; see 47 Fed. Reg. 11,474 (Mar. 16, 1982) (adopting this requirement).

Regulation S-K provides consolidated instructions for disclosures in the non-financial statement portions of Form 10-K and other reports. See 17 C.F.R. 229.10(a)(2). Regulation S-K is intended to ensure "that investors and the marketplace are provided meaningful, nonduplicative information periodically and when securities are sold to the public, while the costs of compliance for public companies are decreased." 45 Fed. Reg. 63,694 (Sept. 25, 1980).

Item 303 states that the issuer "shall provide" certain information. 17 C.F.R. 229.303(a). As relevant here, the issuer must "[i]dentify any known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way," 17 C.F.R. 229.303(a)(1), and "[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

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[1] https://www.sec.gov/files/form10-k.pdf.

or revenues or income from continuing operations," 17 C.F.R. 229.303(a)(3)(ii). This requirement applies only to "currently known trends, events, and uncertainties that are reasonably expected to have material effects." 54 Fed. Reg. 22,429 (May 24, 1989) (citation and emphasis omitted). The "reasonably expects" standard "helps distinguish statements of known facts relating to the future, which are mandatory, from forward-looking statements, which are not required." *Steckman* v. *Hart Brewing, Inc.*, 143 F.3d 1293, 1297 (9th Cir. 1998). Item 303 sets a "lower threshold than 'more likely than not,'" 81 Fed. Reg. 23,944 (Apr. 22, 2016), and "extend[s] considerably beyond [the materiality standard] required by Rule 10b-5," *Oran* v. *Stafford*, 226 F.3d 275, 288 (3d Cir. 2000) (Alito, J.).

The SEC has explained that, without Item 303's required narrative, a company's numerical financial statements and accompanying footnotes "may be insufficient for an investor to judge the quality of earnings and the likelihood that past performance is indicative of future performance." 54 Fed. Reg. at 22,428; see *ibid.* (required narrative "give[s] the investor an opportunity to look at the company through the eyes of management"). The required disclosure is "[o]ne of the most important elements necessary to an understanding of a company's performance." 68 Fed. Reg. 75,061 (Dec. 29, 2003).

2. Petitioner is an issuer subject to Section 13(a)'s reporting requirements. See 15 U.S.C. 78*l*(a); J.A. 68. Respondents are investors in petitioner's stock and the lead plaintiffs in a putative securities-fraud class action against petitioner. Pet. App. 2a-3a.

Respondents' proposed second amended complaint is the operative pleading here. See Pet. App. 3a. In it,

respondents alleged that petitioner had artificially inflated its stock price by filing a Form 10-K that disclosed some known trends and uncertainties but did not disclose an additional known uncertainty that Item 303 required to be disclosed: that petitioner had been implicated in a fraudulent overbilling scheme in the "City-Time" project with the City of New York. *Id.* at 9a, 19a. Respondents further alleged that petitioner had acted with scienter in omitting that additional information from the MD&A, and that the omitted information was material to investors. *Id.* at 19a-20a, 72a; J.A. 278-279; cf. Pet. App. 8a (noting that petitioner's "stock price fell from $17.21 to $12.97 per share" after the risk was fully disclosed). Respondents sought to certify a class of all persons who had purchased petitioner's stock between petitioner's filing of its Form 10-K on March 25, 2011 and its full disclosure of the omitted information on September 1, 2011. Pet. App. 6a, 8a, 14a.

The district court denied a motion to dismiss with respect to respondents' initial Section 10(b) claim premised on alleged omissions from petitioner's March 2011 Form 10-K. Pet. App. 73a-74a. The court later dismissed that claim, however, on the grounds that it did not adequately plead that petitioner's MD&A had violated Item 303 or that petitioner had acted with scienter. *Id.* at 46a-48a. The court denied leave to amend, concluding that the proposed second amended complaint suffered from the same flaws. *Id.* at 35a-37a.

The court of appeals reversed. Pet. App. 1a-26a. Following circuit precedent, the court stated that "Item 303 imposes an 'affirmative duty to disclose'" that "'can serve as the basis for a securities fraud claim under Section 10(b).'" *Id.* at 16a n.7 (quoting *Stratte-McClure* v. *Morgan Stanley*, 776 F.3d 94, 101 (2d Cir. 2015)). The

court then held that respondents' proposed second amended complaint had alleged sufficient facts to establish an Item 303 violation and the additional elements required for Section 10(b) liability, including materiality and scienter. *Id.* at 16a-23a.

SUMMARY OF ARGUMENT

I. It is undisputed in this Court that respondents have adequately pleaded that petitioner's MD&A omitted information required by Item 303; that the omission was material under *Basic Inc.* v. *Levinson*, 485 U.S. 224 (1988); and that petitioner acted with scienter. Petitioner contends, however, that an MD&A can give rise to liability under Section 10(b) and Rule 10b-5 only if it contains an affirmative false statement or a misleading half-truth. Petitioner argues (*e.g.*, Br. 3) that it cannot be held liable under that standard because, it claims, its own violation of Item 303 involves "pure omissions."

Petitioner thus does not dispute that respondents would have stated a claim under Section 10(b) and Rule 10b-5 if petitioner's MD&A had opened with the statement, "This section discloses all the information required by Item 303." The absence of such an express statement of compliance should not change the result, however, because a reasonable investor understands the MD&A section of a Form 10-K to make the same representation implicitly. This case therefore involves a half-truth rather than a "pure omission": Petitioner's MD&A appeared to be complete and thus conveyed to a reasonable investor that it disclosed all of the information Item 303 required. If (as respondents allege) the MD&A omitted information that Item 303 required to be disclosed, the MD&A was therefore misleading.

II. Not every misrepresentation made in connection with a securities transaction gives rise to liability under

Section 10(b), however. Both the SEC and private plaintiffs must also prove that the omission was material under *Basic* and that the defendant acted with scienter. Private plaintiffs must further establish reliance, loss, and loss causation. Those additional elements provide important protection to issuers, and ensure that the large majority of Item 303 violations do not give rise to liability for securities fraud.

The court of appeals' decision here thus does not give private plaintiffs the practical equivalent of a private cause of action to enforce Item 303 or Regulation S-K. Instead, it provides a critical backstop to prevent unscrupulous issuers from exploiting the trust that reasonable investors place in submissions made in purported compliance with SEC disclosure requirements. Indeed, a partial disclosure is particularly likely to create a false impression of completeness when it is offered in an MD&A, which reasonable investors understand must disclose the information that Item 303 requires.

Petitioner's various policy arguments provide no sound basis for shielding this form of fraud from liability under Section 10(b). Petitioner's arguments "overstate[] both the looseness of the inquiry * * * and the breadth of liability" that the court of appeals' approach "threatens." *Omnicare, Inc.* v. *Laborers Dist. Council Constr. Indus. Pension Fund*, 135 S. Ct. 1318, 1332 (2015). If petitioner's approach were accepted, however, it would create a significant loophole in Section 10(b) by transforming a disclosure obligation "designed to protect investors even when there is no fraud" into "a shelter or sanctuary for those who defraud investors." *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783, 787 (2d Cir. 1951) (Frank, J.).

ARGUMENT

I. An MD&A That Omits Information That Item 303 Requires To Be Disclosed Can Be The Predicate For A Section 10(b) Violation

A reasonable investor, reading an MD&A in the applicable legal context, understands it to contain all of the information required by Item 303. An MD&A that discloses only some of the information Item 303 requires therefore is misleading. Such a filing may trigger liability under Section 10(b) if, but only if, the plaintiff pleads and proves the additional elements of a Section 10(b) cause of action.

A. An MD&A That Omits Information That Item 303 Requires To Be Disclosed Is A Misleading Half-Truth

1. Petitioner repeatedly asserts (Br. 3-4, 15-17, 20, 22-24, 26, 31-32, 34, 38, 43-44, 48-49 & n.6), that this case involves "pure omissions," relying on this Court's statement that "[s]ilence, absent a duty to disclose, is not misleading under Rule 10b-5." *Basic Inc.* v. *Levinson*, 485 U.S. 224, 239 n.17 (1988). Petitioner contends that it was both silent and under no "duty to disclose."

That argument would lack merit even if petitioner had been silent, because (as alleged here) petitioner breached its disclosure obligations under Item 303. See pp. 15-21, *infra*. The more fundamental flaw in petitioner's argument, however, is that petitioner was not silent. Rather, petitioner filed a Form 10-K with an MD&A section that disclosed various known trends and uncertainties, J.A. 898-942; see J.A. 1037-1045 (incorporated by reference), but that did not disclose petitioner's implication in the CityTime fraud. See also J.A. 1121-1122 (certification of the chief executive officer and chief financial officer that, "to the best of [their]

knowledge," the filing "fully complie[d] with the requirements of Section 13(a)"). Petitioner submitted that filing despite Item 303's requirement that an issuer disclose *all* known trends, events, or uncertainties that are reasonably likely to affect the issuer's financial condition and prospects.

This case therefore involves a half-truth rather than a "pure omission." See *Universal Health Servs., Inc.* v. *United States*, 136 S. Ct. 1989, 2000 (2016) (*Universal Health Services*) ("[H]alf-truths—representations that state the truth only so far as it goes, while omitting critical qualifying information—can be actionable misrepresentations."). Rule 10b-5 encompasses not only affirmative falsehoods, but also half truths: It reaches the failure "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." 17 C.F.R. 240.10b-5(b). Here, petitioner made "statements": It filed an MD&A providing a narrative description of various trends and uncertainties. See *Janus Capital Grp., Inc.* v. *First Derivative Traders*, 564 U.S. 135, 142 (2011) ("One 'makes' a statement by stating it."); *Webster's Third New International Dictionary* 2229 (2002) ("statement" means "something stated," such as "a report or narrative"). And further disclosure was "necessary" to make those statements "not misleading" "in light of the circumstances," 17 C.F.R. 240.10b-5(b), because a reasonable investor would understand the MD&A section of petitioner's filing as implicitly representing that the issuer had disclosed all the information Item 303 required.

"[W]hether a statement is 'misleading' depends on the perspective of a reasonable investor: The inquiry * * * is objective." *Omnicare, Inc.* v. *Laborers Dist.*

Council Constr. Indus. Pension Fund, 135 S. Ct. 1318, 1327 (2015). "The reasonable investor understands a statement * * * in its full context." *Id.* at 1330. When an issuer submits a filing in purported compliance with its disclosure obligations under the Exchange Act and SEC regulations, the nature and scope of those obligations will affect the inferences that a reasonable investor draws from the filing. See *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1432 (3d Cir. 1997) (a reasonable investor's understanding depends on "the background regulatory structure," including "the existing federal securities disclosure apparatus").

In particular, a reasonable investor knows that issuers file Forms 10-K because Section 13(a) and SEC regulations require them. See 15 U.S.C. 78m(a) ("shall file"); 17 C.F.R. 249.310(a) ("shall" use Form 10-K). A reasonable investor also knows that issuers include an MD&A section disclosing known trends and uncertainties because Form 10-K requires the issuer to include an MD&A section "[f]urnish[ing] the information required by Item 303," SEC, *Form 10-K* (Item 7), and because Item 303 requires an MD&A to disclose "any" known trends or uncertainties that qualify, 17 C.F.R. 229.303(a)(1) and (3)(ii). A reasonable investor in turn would expect the MD&A section of a Form 10-K to disclose all the information that Item 303 requires, at least in the absence of language specifically disclaiming that implication. See Resps. Br. 25. If (as respondents have alleged) petitioner omitted facts that Item 303 required to be disclosed, petitioner's MD&A was the sort of misleading half-truth that may constitute actionable securities fraud if the other prerequisites to liability can be established.

2. Examples help to illustrate the point. If SEC regulations required a Form 10-K to identify every pending lawsuit against the issuer in which the plaintiff sought more than $10 million in damages, and an issuer filed a Form 10-K listing ten such lawsuits, a reasonable investor would understand the filing as a representation that the list was exhaustive. Cf. 17 C.F.R. 229.103 (requiring disclosure of certain legal proceedings). If an additional suit seeking $20 million was actually pending, the filing would be misleading even though it did not explicitly deny the existence of the eleventh suit.

Similarly, if SEC regulations required a Form 10-K to disclose any pending personal bankruptcy petitions filed by a director, and an issuer filed a Form 10-K that omitted that section or left it blank, a reasonable investor likewise would understand the filing to represent implicitly that no director had filed for bankruptcy. If one of the company's directors actually had, the Form 10-K would be misleading. Cf. *In re Ciro, Inc.*, Exchange Act Release No. 34,767, 57 SEC Docket 1893 (Sept. 30, 1994).

The conclusion that such half-truths are misleading would leave open questions of materiality or scienter. If the undisclosed eleventh lawsuit sought $20 million in damages but was frivolous and immaterial under *Basic*, it would not be actionable under Section 10(b). The company's Form 10-K still would be misleading, however, because it would lead a reasonable investor to believe that the list of ten suits was exhaustive. If the issuer omitted the eleventh lawsuit through an innocent mistake, its lack of scienter likewise would prevent the imposition of liability under Section 10(b), but the form would still be misleading, because "whether a statement

is 'misleading' depends on the perspective of a reasonable investor." *Omnicare*, 135 S. Ct. at 1327.

The same principles apply here. An incomplete MD&A is misleading because a reasonable investor knows that an issuer must include an MD&A section to comply with an SEC mandate (Item 303) that requires disclosure of *all* the known trends and uncertainties that meet the regulatory ("reasonable expectation") threshold. In light of that mandate, a reasonable investor understands an MD&A as implicitly representing that no additional qualifying trends or uncertainties exist. "[T]he reader of the disclosure sees that the issuer is responding to the disclosure obligation and is entitled to assume that the response is not only accurate but complete as well." Donald C. Langevoort & G. Mitu Gulati, *The Muddled Duty to Disclose Under Rule 10b-5*, 57 Vand. L. Rev. 1639, 1680 (2004).

To be sure, unlike the hypothetical requirement that an issuer disclose all lawsuits against it seeking more than $10 million in damages, Item 303 does not establish a bright-line rule. Item 303 requires the issuer to disclose any known trends or uncertainties that are "reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way," or that "the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income." 17 C.F.R. 229.303(a)(1) and (3)(ii). Although Item 303 applies only to trends or uncertainties that are presently known to the issuer, it sometimes requires judgment to determine whether a given trend or uncertainty satisfies the "reasonably likely to have material effect" standard. See 2 Thomas Lee Hazen, *Treatise on the Law of Securities Regulation* § 9:50 (7th ed. 2016).

Because Item 303 sometimes requires judgment calls, it may be unclear whether Item 303 actually required disclosure of particular information, and thus whether the issuer's omission of that information was misleading in context. See Resps. Br. 52 n.23 (collecting cases dismissed on ground that Item 303 did not require disclosure). Furthermore, even in cases where the omission is misleading, uncertainty about whether Item 303 requires disclosure makes it more difficult for a Section 10(b) plaintiff to plead or prove that the issuer omitted the information with scienter, rather than due to a good-faith (but erroneous) decision about the scope of its disclosure obligation. This difference, however, provides no sound basis for petitioner's proposed categorical rule that an incomplete MD&A can *never* give rise to liability under Section 10(b). When an issuer acted with scienter in disclosing only some (but not all) required information, and the omitted information is also material under *Basic*, imposition of liability is wholly consistent with the text of Section 10(b) and Rule 10b-5, as well as this Court's precedents.

3. The recognition that a half-truth can be misleading "recurs throughout the common law." *Universal Health Services*, 136 S. Ct. at 2000 n.3; *e.g.*, Restatement (Second) of Torts § 529 (1977) ("A representation stating the truth so far as it goes but which the maker knows or believes to be materially misleading because of his failure to state additional or qualifying matter is a fraudulent misrepresentation."); W. Page Keeton et al., *Prosser and Keeton on the Law of Torts* § 106, at 738 (5th ed. 1984) ("[H]alf of the truth may obviously amount to a lie, if it is understood to be the whole.").

The Court in *Universal Health Services* observed that "[a] classic example of an actionable half-truth in

contract law is the seller who reveals that there may be two new roads near a property he is selling, but fails to disclose that a third potential road might bisect the property." 136 S. Ct. at 2000 (citing *Junius Constr. Co.* v. *Cohen*, 178 N.E. 672, 674 (N.Y. 1931) (Cardozo, J.)). The Court thus recognized that the disclosure of certain information is often reasonably understood as an implicit representation that no additional risks or obstacles of the same general sort exist. There is no sound basis for refusing to apply that principle to statements made in a securities filing submitted in purported compliance with Item 303 or other SEC regulations that require the issuer to disclose all of some kind of information. To the contrary, it is *particularly* reasonable to draw such an inference from such statements, because the background legal context further strengthens the already natural inference that the statements made deal comprehensively with the matter at hand.

In *Universal Health Services*, this Court relied in part on the surrounding legal context in holding that a healthcare provider's claims for Medicaid reimbursement were misleading, and thus potentially actionable under the False Claims Act, 31 U.S.C. 3729 *et seq.*, even though the claims did not contain any affirmative false statement. See 136 S. Ct. at 2000-2001. The Court explained that, "by submitting claims for payment using payment codes that corresponded to specific counseling services, Universal Health represented that it had provided individual therapy, family therapy, preventive medication counseling, and other types of treatment." *Id.* at 2000. The Court observed that "[a]nyone informed that a social worker at a Massachusetts mental health clinic provided a teenage patient with individual counseling services would probably—but wrongly—conclude

that the clinic had complied with core Massachusetts Medicaid requirements," including requirements that the provider be licensed and have specialized training. *Ibid.* The Court concluded that, "[b]y using payment and other codes that conveyed this information without disclosing [its] many violations of basic staff and licensing requirements for mental health facilities, Universal Health's claims constituted misrepresentations." *Id.* at 2000-2001.

Similarly here, a reasonable investor would construe petitioner's MD&A in light of the legal context in which such filings are submitted, and would understand the MD&A as implicitly representing that no additional trends or uncertainties that met the regulatory threshold existed. If (as respondents allege) those representations were inaccurate, and if respondents can establish the remaining prerequisites for a private Rule 10b-5 action, petitioner can properly be held liable for the misleading omission in its MD&A.

B. Even If An Incomplete MD&A Were Viewed As "Silence," It Could Still Serve As The Predicate For A Claim Under Section 10(b)

Even if an incomplete MD&A were viewed as "silence" rather than as a half-truth, it would still be misleading. "Silence, *absent a duty to disclose,* is not misleading under Rule 10b-5." *Basic*, 485 U.S. at 239 n.17 (emphasis added). Where a duty to disclose exists, however, silence *can* be misleading because a reasonable investor will be aware of the duty and will reasonably infer from a regulated party's silence that no circumstance for which disclosure is required is actually present.

Petitioner contends that, even if it violated Section 13(a) by omitting required information from its MD&A, that omission could not cause its conduct to be deceptive

or misleading within the meaning of Section 10(b). Petitioner argues (Br. 15) that a "duty to disclose" exists for these purposes only if (1) disclosure of additional information is necessary to prevent an affirmative statement from being misleading, or (2) the defendant is subject to the common-law duty to disclose or abstain that arises from a fiduciary relationship of trust, *e.g.*, *Chiarella* v. *United States*, 445 U.S. 222, 228 (1980). Even assuming, *arguendo*, that the first basis for potential liability is inapplicable here (but see pp. 8-15, *supra*), petitioner offers no sound basis for disputing that the SEC disclosure mandate here creates a "duty to disclose."

1. Petitioner's argument rests on the counter-intuitive proposition that a judge-made rule drawn from the common law of trusts (the fiduciary duty discussed in *Chiarella*) imposes a "duty to disclose" that can make silence misleading, but that a disclosure requirement imposed by a federal statute or regulation does not. There is no logical basis for that distinction. If Congress required issuers to disclose any tender offer within 24 hours, a reasonable investor would understand an issuer's silence to mean that no tender offers had been made within the last day. Under petitioner's approach, however, an issuer would not commit securities fraud even if it deliberatively deceived potential investors by keeping a tender offer secret.

Disclosure requirements under federal securities laws most obviously benefit investors by inducing issuers and other regulated parties to disclose information that is relevant to investment decisions. But the existence of those requirements can benefit investors even in circumstances where no actual disclosures are made, by allowing investors to infer with confidence that the types of events for which disclosure is required have not

occurred. A reasonable investor thus will view silence differently in a legal context where various disclosures are required than it would in an unregulated environment. Yet under petitioner's approach, unscrupulous parties could exploit the very trust that disclosure requirements are intended to foster, by engaging in strategic omissions that they expect investors to misconstrue. If that approach were accepted, disclosure obligations "designed to protect investors even when there is no fraud, would afford a shelter or sanctuary for those who defraud investors." *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783, 787 (2d Cir. 1951) (Frank, J.).

2. The ordinary meaning of the term "duty" encompasses any "legal obligation that is owed or due to another and that needs to be satisfied." *Black's Law Dictionary* 615 (10th ed. 2014); see, *e.g.*, 4 *Oxford English Dictionary* 1143 (2d ed. 1989) ("Action, or an act, that is due in the way of moral or legal obligation; that which one ought or is bound to do; an obligation."). A statute or regulation that mandates disclosure thus creates a "duty" to disclose as that term is commonly understood. *E.g.*, *Stratte-McClure* v. *Morgan Stanley*, 776 F.3d 94, 101 (2d Cir. 2015) (duty to disclose may arise "when there is * * * a 'statute or regulation requiring disclosure'" (quoting *Glazer* v. *Formica Corp.*, 964 F.2d 149, 157 (2d Cir. 1992)); *Gallagher* v. *Abbott Labs.*, 269 F.3d 806, 808 (7th Cir. 2001) (when "positive law creates a duty to disclose"); *Oran* v. *Stafford*, 226 F.3d 275, 285 (3d Cir. 2000) (Alito, J.) ("when there is * * * a statute requiring disclosure"); *Shaw* v. *Digital Equip. Corp.*, 82 F.3d 1194, 1202 n.3 (1st Cir. 1996) ("when a statute or regulation requires disclosure"), abrogated in part on other grounds by 15 U.S.C. 78u-4(b)(2). There is no rea-

son to suppose that the *Basic* Court had in mind a narrower meaning, or that it intended to exclude federal statutory or regulatory disclosure requirements from the principle that silence can give rise to Section 10(b) liability if a "duty to disclose" exists. See 485 U.S. at 239 n.17.[2]

The operative terms in Section 10(b) and Rule 10b-5 —"defraud," "fraud," and "deceit," 15 U.S.C. 78j(b); 17 C.F.R. 240.10b-5—also comfortably encompass the misconduct alleged here. *E.g.*, *Black's Law Dictionary* 491 ("deceit" means "[t]he act of intentionally leading someone to believe something that is not true; an act designed to deceive or trick"); *id.* at 775 ("fraud" means "[a] knowing misrepresentation or knowing concealment of a material fact made to induce another to act to his or her detriment"). An issuer that deliberately omits material adverse information, in a legal context where reasonable investors would infer from nondisclosure that no such adverse information exists, engages in "fraud" and "deceit" within the usual meaning of those terms. Cf. *SEC* v. *Zandford*, 535 U.S. 813, 819 (2002) (stating that Section 10(b) "should be 'construed not technically and restrictively, but flexibly to effectuate its remedial purposes'") (citation omitted). Indeed,

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[2] The Third Circuit's statement in *Oran* that a "statute requiring disclosure" may create a duty to disclose for these purposes, 226 F.3d at 285, contradicts petitioner's position that a statute cannot have that effect. The court further explained that Item 303's materiality standard is broader than the *Basic* standard, and that a violation of Item 303 "does not automatically give rise to a material omission under Rule 10b-5." *Id.* at 288. But the court did not squarely decide whether an Item 303 violation would be actionable under Rule 10b-5 if the omission were material under *Basic*, because the plaintiff had not adequately pleaded materiality. See *ibid.*

many courts adjudicating state-law tort or similar actions have recognized that a statute or regulation mandating disclosure can impose a "duty to disclose" that makes silence misleading.[3]

3. Petitioner invokes (*e.g.*, Br. 4, 18) this Court's statement that, "[e]ven with respect to information that a reasonable investor might consider material, companies can control what they have to disclose under [Section 10(b) and Rule 10b-5(b)] by controlling what they say to the market." *Matrixx Initiatives, Inc.* v. *Siracusano*, 563 U.S. 27, 45 (2011) (*Matrixx*). Petitioner's reliance on that statement is misplaced.

Matrixx did not alter the rule that a duty to disclose can make silence misleading. To the contrary, immediately before the sentence on which petitioner relies, the

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[3] *E.g.*, *Brown* v. *K & V Auto., Inc.*, 946 So. 2d 458, 466 (Ala. Civ. App. 2006) (disclosure statute imposed a "duty to disclose" for statutory fraud action); *SCC Acquisitions Inc.* v. *Central Pac. Bank*, 143 Cal. Reptr. 3d 711, 715 (Cal. Ct. App. 2012) ("statute or other prescriptive law"); *Glazer* v. *Dress Barn, Inc.*, 873 A.2d 929, 961 (Conn. 2005) ("statute or regulation"); *Abazari* v. *Rosalind Franklin Univ. of Med. & Sci.*, 40 N.E.3d 264, 275 (Ill. App. Ct. 2015) ("statutory duty to disclose"), cert. denied, 136 S. Ct. 1526 (2016); *Rivermont Inn, Inc.* v. *Bass Hotels Resorts, Inc.*, 113 S.W.3d 636, 641 (Ky. Ct. App. 2003) ("when a statute imposes such a duty"); *Binette* v. *Dyer Library Ass'n*, 688 A.2d 898, 903 (Me. 1996) ("[S]ilence rises to the level of supplying false information when such failure to disclose constitutes the breach of a statutory duty."); *Williams* v. *East Coast Sales, Inc.*, 298 S.E.2d 80, 82 (N.C. App. 1982) ("*legal duty* imposed by statute"); *France* v. *Chaprell Jeep-Eagle Dodge, Inc.*, 968 P.2d 844, 847 (Okla. Civ. App. 1998) ("This statute establishes a duty" to disclose.); *Favors* v. *Matzke*, 770 P.2d 686, 690 (Wash. Ct. App. 1989) ("statutory duty to disclose"); see also *Chroniak* v. *Golden Inv. Corp.*, 983 F.2d 1140, 1147 (1st Cir. 1993) (omission in violation of New Hampshire disclosure statute qualified as an "unfair or deceptive practice or act" under state law).

Court stated that "[s]ilence, *absent a duty to disclose*, is not misleading under Rule 10b-5." 563 U.S. at 45 (emphasis added) (quoting *Basic*, 485 U.S. at 239 n.17). The Court in *Matrixx* held that adverse drug reports could be material even if they were not statistically significant. *Id.* at 30-31. In explaining that conclusion, the Court observed that Section 10(b) and Rule 10b-5 *themselves* impose "an affirmative duty to disclose" only "when necessary 'to make . . . statements made, in the light of the circumstances under which they were made, not misleading.'" *Id.* at 44 (quoting 17 C.F.R. 240.10b-5(b)). But the Court did not discuss whether silence in breach of an independent statutory or regulatory disclosure requirement can mislead. And companies' general freedom to "control[] what they say to the market," *id.* at 45, does not extend to circumstances where a statute or regulation requires them to speak.

Chiarella is also inapposite. The Court in that case addressed the circumstances in which a duty to disclose may be inferred "despite the absence of statutory language * * * specifically addressing the legality of nondisclosure." 445 U.S. at 230. Here, Section 13(a) and SEC regulations specifically make nondisclosure unlawful. Petitioner also relies (Br. 25) on the Restatement (Second) of Torts and a student note. But those sources discuss disclosure obligations imposed by the common law or by Rule 10b-5 itself, and neither addresses whether breach of an independent statutory or regulatory disclosure requirement can make silence misleading. See Restatement (Second) of Torts § 551; Frank F. Coulom, Jr., Note, *Rule 10b-5 and the Duty to Disclose Market Information: It Takes a Thief*, 55 St. John's L. Rev. 93, 93-95 (1980).

4. The rationale for treating silence as misleading when a "duty to disclose" exists applies with full force here. As explained above, pp. 8-15, *supra*, a reasonable investor understands an MD&A, in light of Item 303, to represent implicitly that the issuer has disclosed all the required information. "Due to the obligatory nature of these regulations, a reasonable investor would interpret the absence of an Item 303 disclosure to imply the non-existence of" additional trends or uncertainties meeting the regulatory threshold. *Stratte-McClure*, 776 F.3d at 102. If additional trends or uncertainties actually exist for which Item 303 mandates further disclosure, the MD&A would be misleading, even if the issuer could be described as "silent."

Petitioner suggests (Br. 26) that an omission is insufficient, standing alone, to qualify as a fraudulent "device, scheme, or artifice" or "act, practice, or course of business" within the meaning of paragraphs (a) or (c) of Rule 10b-5. 17 C.F.R. 240.10b-5(a) and (c). But this case does not involve an omission, standing alone, because petitioner did not entirely fail to file a Form 10-K (or even file a Form 10-K without an MD&A). Rather, petitioner filed a Form 10-K with an MD&A disclosing known trends and uncertainties. This case thus falls squarely within paragraph (b): Petitioner made "statements" that were misleadingly incomplete "in the light of the circumstances under which they were made." 17 C.F.R. 240.10b-5(b). In any event, respondents' allegations—a deliberate scheme to prepare and file a Form 10-K with an MD&A that violated Item 303 and left undisclosed material information because of concerns about the stock price—involve far more than just an omission and, if proven, would satisfy Rule 10b-5(a) and (c) as well.

C. The SEC's Longstanding Position Supports The Potential Imposition Of Section 10(b) Liability For Misleading Omissions Like The One Alleged In This Case

The SEC's longstanding and consistent position is that a violation of Item 303 or other SEC disclosure obligation can be the predicate for a Rule 10b-5 claim. That view is entitled to deference. See *Zandford*, 535 U.S. at 819-820; *Basic*, 485 U.S. at 239 n.16.

The SEC has instituted administrative proceedings and imposed sanctions under Rule 10b-5 based on omissions from an MD&A in violation of Item 303. For example, in *In re Fitzpatrick*, Exchange Act Release No. 34,865, 57 SEC Docket 2178 (Oct. 20, 1994), the SEC concluded that two executives had violated Rule 10b-5 by filing an MD&A that omitted material information in breach of Item 303. *Id.* at 2182-2183 ("[T]he information omitted from First Capital Holdings' 1990 Form 10-K was clearly material," and the defendants "knew or were reckless in not knowing of the disclosure failures."). See, *e.g.*, *In re Cypress Bioscience Inc.*, Exchange Act Release No. 37,701, 62 SEC Docket 2286, 2292 (Sept. 19, 1996) (finding Rule 10b-5 violation based on issuer's Form 10-Q that included false financial statements and "failed to disclose" information "in the MD&A section" in violation of Item 303); *In re Valley Sys., Inc.*, Exchange Act Release No. 36,227, 60 SEC Docket 541, 544 (Sept. 14, 1995) (similar); *In re Westwood One, Inc.*, Exchange Act Release No. 33,489, 55 SEC Docket 2350, 2359 (Jan. 19, 1994) (similar). The SEC has taken the same position in administrative actions involving other disclosure obligations. For example, the SEC has found that a company violated Rule 10b-5 by filing Forms 10-K that "failed to disclose that [the company's president

and chief executive officer] had filed for personal bankruptcy in October 1987, as required by Item 401(f) of Regulation S-K." *Ciro*, 57 SEC Docket at 1896; see p. 11, *supra*.

The SEC has long taken the same position in federal court. For example, in *Basic*, the SEC argued that a duty to disclose exists for these purposes "where regulations promulgated by the Commission require disclosure." SEC Amicus Br. at 7, *Basic*, *supra* (No. 86-279). The SEC gave as an example another provision (Item 504) of Regulation S-K. *Id.* at 7 n.3 (citing 17 C.F.R. 229.504 (1987)). And in *SEC* v. *Conaway*, 698 F. Supp. 2d 771 (E.D. Mich. 2010), the SEC argued that a company violated Rule 10b-5 by "fail[ing] to disclose in the MD & A that [it] had experienced a material liquidity event in the third quarter." *Id.* at 822. The SEC further argued that "Item 303 can be the basis for a Rule 10b-5 action" because it "provide[s] a duty to disclose, such that liability may apply to omitted material information if scienter exists." D. Ct. Doc. 127, at 5, *Conaway*, *supra* (No. 05-cv-40263), 2009 WL 1719312; see, also *e.g.*, D. Ct. Doc. 1, at 5-6, 10-11, *SEC* v. *CVS Caremark Corp.*, No. 14-cv-177 (D.R.I. Apr. 8, 2014) (omission of information required to be disclosed in prospectus supplements).[4]

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[4] Petitioner states (Br. 43) that it is unaware of any "standalone" Rule 10b-5 claim brought by the SEC "based solely on information allegedly omitted from the MD&A," and that instead the SEC's allegations have always "included a fraudulent scheme—not a pure omission." It is unclear what petitioner means by a "standalone" "pure omission" claim. The SEC's enforcement actions typically involve egregious conduct with multiple violations. In the actions described above, the SEC imposed penalties based on the position that Regulation S-K creates a duty to disclose for purposes of Rule 10b-5.

The SEC has also promulgated regulations premised on the view that regulatory disclosure requirements impose a duty to disclose for purposes of Rule 10b-5. For example, Regulation FD mandates that an issuer's disclosure of material nonpublic information must be made to all investors simultaneously. See 17 C.F.R. 243.100. When the SEC imposed that obligation, it also created a safe harbor providing that "[n]o failure to make a public disclosure required solely by §243.100 shall be deemed to be a violation of Rule 10b-5." 17 C.F.R. 243.102. That regulation presupposes that, without a safe harbor, Regulation FD's disclosure requirement would create a duty to disclose. The SEC explained that it was responding to concerns about "the prospect of private liability for violations of Regulation FD," and that it intended to distinguish "other reporting requirements under Section 13(a) or 15(d) *which do create a duty to disclose for purposes of Rule 10b-5*." 65 Fed. Reg. 51,726 & n.86 (Aug. 24, 2000) (emphasis added). See 17 C.F.R. 240.13a-11(c) (similar safe harbor for certain disclosure requirements on Form 8-K).

II. Petitioner's Arguments Lack Merit

A. The Court Of Appeals Did Not Create A Private Right Of Action To Enforce Regulation S-K Or Item 303

Contrary to petitioner's contention (*e.g.*, Br. 36-38), the court of appeals' decision does not have the legal or practical effect of authorizing private suits to enforce Regulation S-K or Item 303. An issuer's mere failure to disclose all of the information Item 303 requires does not violate Section 10(b) or Rule 10b-5. To establish li-

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And *Fitzpatrick* found a violation of Rule 10b-5 based solely on material omissions from an MD&A. See 57 SEC Docket at 2182-2183.

ability under those provisions, both the SEC and private plaintiffs must also plead and prove a connection with the purchase or sale of a security, materiality as defined in *Basic*, and scienter. Private plaintiffs must further plead and prove reliance, loss, and loss causation. See *Dura Pharm., Inc.* v. *Broudo*, 544 U.S. 336, 341-342 (2005).

Materiality and scienter are particularly significant requirements. A plaintiff cannot establish materiality under *Basic* simply by identifying a violation of Item 303 because Item 303's mandate "extend[s] considerably beyond th[at] required by Rule 10b-5." *Oran*, 226 F.3d at 288. Item 303 requires disclosure of known trends and uncertainties that are reasonably expected to have a material effect on the issuer's liquidity, capital resources, or operations. See 17 C.F.R. 229.303(a)(1) and (3)(ii). By contrast, *Basic* requires "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." 485 U.S. at 231-232 (citation omitted).

Information that Item 303 requires to be disclosed therefore is not "inevitably" or "automatically" material under *Basic*. *Oran*, 226 F.3d at 288; see 54 Fed. Reg. at 22,430 n.27 (*Basic* is "inapposite to Item 303 disclosure"). But the difference between the two standards does not justify a categorical rule that an issuer can never violate Section 10(b) by or through violating Item 303. To proceed on a Section 10(b) claim, plaintiffs must prove both that disclosure was required by Item 303 and that the omitted information was material under *Basic*. While many omissions will be material under Item 303 but not the stricter Section 10(b) standard,

some omissions will be material under *both* Item 303 *and* Section 10(b). See Langevoort & Gulati at 1651.

A plaintiff also cannot establish scienter simply by identifying a violation of Item 303. As discussed above, see pp. 12-13, *supra*, Item 303 does not require disclosure of every known trend or uncertainty, and determining whether Item 303 requires disclosure sometimes requires judgment calls. It can be correspondingly difficult for a plaintiff to show that an issuer violated Item 303, let alone that it did so with scienter. The Private Securities Litigation Reform Act of 1995 (PSLRA), Pub. L. No. 104-67, 109 Stat. 737, provides additional protection in private suits by requiring plaintiffs to plead "with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. 78u-4(b)(2)(A).

The district court dismissed most of respondents' Item 303-related claims because of inadequate pleading of Section 10(b)'s additional elements. Pet. App. 73a-74a. And, as petitioner observes (Br. 49 n.6), "significant hurdles" remain "to pleading and proving a private [Section 10(b)] claim based on an alleged omission of Item 303 information." There is consequently no danger that petitioner will be held liable for a mere violation of Item 303. But if respondents can establish all the traditional elements of a private Section 10(b) cause of action—that is, if respondents can prove that petitioner defrauded them by omitting material information with scienter, and that they sustained losses as a result—it would make no sense to absolve petitioner of liability simply because its conduct *also* violated *another* SEC rule for which no private right of action exists. Cf. *Blockburger* v. *United States*, 284 U.S. 299, 304 (1932) (in the criminal context, "the same act or transaction

[may] constitute[] a violation of two distinct statutory provisions").

B. The Court Of Appeals' Decision Is Consistent With The PSLRA And With Section 11

1. Petitioner contends (Br. 32) that the decision below subverts Congress's determination, in enacting the PSLRA, to "accept[] the § 10(b) private cause of action as then defined" but "to extend it no further.'" *Ibid.* (quoting *Stoneridge Inv. Partners, LLC* v. *Scientific-Atlanta, Inc.*, 552 U.S. 148, 166 (2008) (*Stoneridge*)). Although the question presented in the certiorari petition (Pet. i) did not refer specifically to private suits, petitioner has reformulated it (Br. i) to ask whether a "privately enforceable" duty to disclose exists. Unlike in *Stoneridge*, however, petitioner's theory cannot be confined to private suits. The rule petitioner invokes—that "[s]ilence, absent a duty to disclose, is not misleading under Rule 10b-5," Br. 4 (quoting *Basic*, 485 U.S. at 239 n.17)—applies equally in SEC enforcement actions.

Contrary to petitioner's argument, moreover, respondents' theory of liability is hardly new. Misleading half-truths were treated as actionable misrepresentations even before the SEC promulgated Rule 10b-5(b) in 1942. See 7 Fed. Reg. 3804 (May 22, 1942); *Universal Health Services*, 136 S. Ct. at 2000 (citing a 1931 decision of the New York Court of Appeals as a "classic example" of that principle); pp. 13-14, *supra*. When Congress enacted the PSLRA, it was already settled that Rule 10b-5 reached fraud committed by silence in breach of a duty to disclose, *Basic*, 485 U.S. at 239 n.17, and the SEC had already imposed penalties on the ground that Regulation S-K (including Item 303) imposed such a duty, see pp. 22-23, *supra* (collecting cases).

In *Stoneridge*, this Court declined to extend the private right of action to reach a new category of defendants (aiders and abettors). 552 U.S. at 158. It did not suggest that a primary actor (here, the issuer) could escape liability for securities fraud simply by establishing that the precise fact pattern involved had not arisen in pre-PSLRA cases. That rigid approach would undermine Rule 10b-5's purpose of "encompass[ing] the infinite variety of devices that are alien to the 'climate of fair dealing' that Congress sought to create and maintain." *Herpich* v. *Wallace*, 430 F.2d 792, 802 (5th Cir. 1970) (quoting *SEC* v. *Capital Gains Research Bureau*, 375 U.S. 180, 201 (1963)).

Petitioner briefly suggests (Br. 17, 50-53) that the decision below is wrong because the provision of Regulation S-K specifically requiring disclosure of certain legal proceedings, 17 C.F.R. 229.103 (Item 103), did not mandate disclosure of the CityTime fraud. But that is a factbound challenge to the adequacy of the allegations that petitioner violated Item 303, and it is not fairly encompassed within the question presented. In any event, even if Item 103 were inapplicable, that would not mean that Item 303's broader requirements were inapplicable as well. See 53 Fed. Reg. 29,227 (Aug. 3, 1988) (explaining that disclosure of a pending investigation can be required by Item 103, Item 303, or both).

2. Section 11 of the Securities Act of 1933, 15 U.S.C. 77k(a), imposes liability on various persons who are associated with a registration statement that "contained an untrue statement of a material fact *or omitted to state a material fact required to be stated therein* or necessary to make the statements therein not misleading." *Ibid.* (emphasis added). Petitioner suggests (Br. 29-31) that Congress's failure to include the italicized

(or similar) language in Section 10(b) casts doubt on the theory of liability that the court of appeals accepted here. That argument lacks merit.

Section 10(b) broadly reaches "any manipulative or deceptive device or contrivance in contravention of" SEC rules. 15 U.S.C. 78j(b). Rule 10b-5(b) reaches any failure "to state a material fact necessary in order to make * * * statements made, in the light of the circumstances under which they were made, not misleading." 17 C.F.R. 240.10b-5(b). As explained above, see pp. 8-21, *supra*, an MD&A that discloses some but not all required information may fall within that prohibition whether the MD&A is viewed as a misleading half-truth or as silence where a duty to disclose exists. The fact that Section 11 uses somewhat different language in the specific context of registration statements provides no reason to decline to give Section 10(b) and Rule 10b-5 their natural reading. Cf. *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 382-383 (1983) ("Since § 11 and § 10(b) address different types of wrongdoing, we see no reason to carve out an exception to § 10(b) for fraud occurring in a registration statement just because the same conduct may also be actionable under § 11.").

C. Petitioner's Policy Arguments Provide No Sound Basis For Exempting This Form of Securities Fraud From Section 10(b)

Petitioner offers various policy arguments (Br. 41-54) against imposing Section 10(b) liability in cases involving material omissions from an MD&A. Even if those arguments accurately predicted the practical effects of the court of appeals' holding, they would not justify reversing the judgment below. See *Omnicare*, 135 S. Ct. at 1331; *Halliburton Co.* v. *Erica P. John Fund, Inc.*,

134 S. Ct. 2398, 2413 (2014); *Basic*, 485 U.S. at 239 n.17. They are also unpersuasive on their own terms.

1. Petitioner's policy arguments "overstate[] * * * the breadth of liability," and the resulting deluge of immaterial information, the court of appeals' decision can be expected to produce. *Omnicare*, 135 S. Ct. at 1332. Petitioner asserts (*e.g.*, Br. 41, 47) that various problems would arise from "private enforcement" of Item 303. But the court of appeals did not authorize private enforcement of Item 303; a plaintiff must plead and prove all of the elements of Section 10(b), not merely that an MD&A was incomplete. See pp. 24-27, *supra*.

Petitioner contends (Br. 47) that "nearly two dozen" Section 10(b) cases have been filed within the Second Circuit since it decided *Stratte-McClure*, compared with a "handful" in the Ninth Circuit. Even if petitioner's tally were accurate, it would shed little light on the question here. By the time of *Stratte-McClure*, the Ninth Circuit had already held (erroneously) that Item 303 violations can *never* be the predicate for a Section 10(b) claim. See *In re NVIDIA Corp. Sec. Litig.*, 768 F.3d 1046, 1056 (9th Cir. 2014), cert. denied, 135 S. Ct. 2349 (2015). Moreover, petitioner's figures would not show that *Stratte-McClure* caused any uptick or that the recent suits lack merit. It has long been understood that a duty to disclose can make silence misleading; the SEC has asserted that view for decades, including in cases where Item 303 imposed the duty; and the Second Circuit indicated that such cases were viable in 2001, see *In re Scholastic Corp. Sec. Litig.*, 252 F.3d 63, 70-74 (2d Cir.), cert. denied, 534 U.S. 1071 (2001), long before the cases petitioner identifies.

Petitioner contends (Br. 44) that the court of appeals' rule would "undermine the flexibility inherent in the

Commission's disclosure regime" and "incentivize registrants to flood the market with immaterial and premature disclosures." But the fact that the SEC has long pressed Rule 10b-5 claims predicated on Item 303 violations (and is defending that position here) indicates that the agency views the benefit to securities-fraud enforcement in this context as justifying any possible adverse impact on the quality of disclosure. Plaintiffs must prove, *inter alia*, that the omitted information was material under *Basic*. This Court has been "careful not to set too low a standard of materiality," out of "concern[] that a minimal standard might bring an overabundance of information within its reach." *Basic*, 485 U.S. at 231. The materiality requirement can perform that same function in the context of Section 10(b) suits premised on Item 303 violations.

Contrary to petitioner's contention (see Br. 42-43), Section 10(b) enforcement complements rather than subverts the SEC's comment-letter process. The SEC's Division of Corporate Finance periodically reviews registrants' public filings for compliance with SEC disclosure obligations. See Div. of Corp. Fin., SEC, *Filing Review Process* (Jan. 19, 2017).[5] When a company "can improve its disclosure or enhance its compliance," the Division "provides the company with comments," initiating a "dialogue with a company about its disclosure" in which a "company generally responds" and, if appropriate, amends its filings. *Ibid.* With respect to the MD&A, SEC staff members encourage issuers to "emphasize material information that is required or promotes understanding [of the company's financial condition, liquidity and capital resources, changes in financial

[5] https://www.sec.gov/divisions/corpfin/cffilingreview.htm.

condition and results of operations,] and de-emphasize (or, if appropriate, delete) immaterial information that is not required and does not promote [that] understanding." 68 Fed. Reg. at 75,059; see 81 Fed. Reg. at 23,919.

The comment-letter process and Section 10(b) enforcement thus both aim to improve the quality of information available to the market, without flooding investors with immaterial information. If MD&A quality declines or the comment-letter process becomes less effective, the SEC has targeted tools at its disposal. For example, it could revise Item 303, modify the comment-letter process, or adopt a tailored safe harbor from Rule 10b-5 liability, as it has done before. See p. 24, *supra*; cf. *Halliburton*, 134 S. Ct. at 2413 ("These [policy] concerns are more appropriately addressed to Congress.").

2. Acceptance of petitioner's position would harm investors and the securities markets by exempting from Section 10(b) liability conduct that is clearly fraudulent. Under petitioner's approach, an issuer could deliberately violate Item 303 and omit a material disclosure precisely to dupe investors into believing that the security was less risky than it actually was. Petitioner's legal theory would logically extend, moreover, to similar schemes that exploit investors' trust in the efficacy of other statutory or regulatory disclosure requirements.

Petitioner's approach would prevent defrauded investors from obtaining compensation for their losses, and would prevent the SEC from obtaining various sanctions that are available under Section 10(b) but not under Section 13(a). *E.g.*, 15 U.S.C. 78u(d)(2) (person who violates Section 10(b) may be barred from serving as an officer or director); 17 C.F.R. 230.405 (an issuer found liable under Rule 10b-5 loses regulatory benefits of being a "well-known seasoned issuer"); see also 17

C.F.R. 230.262(a)(5) and 230.506(d)(1)(iv) (cease-and-desist order entered because of a Section 10(b) violation disqualifies issuer from certain securities offerings).

Petitioner's approach also would lead to disparate treatment of materially equivalent conduct. Under petitioner's theory, the MD&A in this case would have been actionable if it had opened with the statement, "This section contains all the information required by Item 303." But because the SEC already requires every MD&A to "[f]urnish the information required by Item 303," see SEC *Form 10-K*, Item 7, a reasonable investor would understand the filing of an MD&A as an implicit representation to the same effect. For purposes of Section 10(b) liability, there is no sound reason to distinguish between the two situations.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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