

[Securities Regulation Daily Wrap Up, FRAUD AND MANIPULATION—U.S.: High Court takes on question of whether an Item 303 omission is actionable under 10\(b\), \(Sept. 29, 2023\)](#)

Securities Regulation Daily Wrap Up

[Click to open document in a browser](#)

By [Rodney F. Tonkovic, J.D.](#)

In the absence of an otherwise-misleading statement, can the failure to make an Item 303 disclosure support a private 10(b) claim?

A few days before the start of its new term, the Supreme Court granted certiorari for a petition asking if violations of Regulation S-K give rise to a Section 10(b) fraud claim. A Second Circuit panel held that petitioner Macquarie Infrastructure's failure to make a material disclosure required by Item 303 of Regulation S-K can serve as the basis for a fraud claim. The petition argued that the case involves a pure omission, that is, there was no affirmative statement rendered misleading by omission. The Second Circuit's holding places it in opposition to the Third, Ninth, and Eleventh Circuits, the petition says, and its expansion of liability under Section 10(b) conflicts with Court precedent (*Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, [cert. granted](#) September 29, 2023).

Macquarie. Petitioner Macquarie Infrastructure owned and operated a portfolio of infrastructure businesses. One of these businesses was International-Matex Tank Terminals (IMTT), a bulk liquid storage service. IMTT has stored a high-sulfur fuel oil known as "No. 6 oil" since the 1970s. Over the years, environmental regulations have caused the demand for No. 6 oil to decline, and in 2016 a regulation (IMO 2020) was issued to cap the sulfur content of fuel oil by 2020. In late 2017 and early 2018, the demand for storage at IMTT's facilities declined as customers failed to renew their contracts for storing No. 6 oil. In early 2018, Macquarie announced that it was reducing its 2018 dividend guidance; the company's stock price dropped after this news.

A lawsuit followed, and the lead plaintiff, respondent Moab Partners, L.P., brought a number of claims. Centrally, the complaint alleged that Macquarie failed to anticipate and disclose that IMO 2020 would have a negative impact on its financial performance. As relevant here, the [district court](#) rejected the argument that Macquarie violated a disclosure obligation under Item 303 of Regulation S-K because Moab failed to point to an uncertainty that should have been disclosed and also failed to plead in which SEC filings it should have been disclosed it. The court went on to dismiss the complaint in its entirety after finding no primary violations of the securities laws.

The Second Circuit. The Second Circuit [disagreed](#) in a summary order holding that Moab adequately alleged a "known trend or uncertainty" giving rise to a duty to disclose under Item 303. This also sufficed to establish an actionable omission and scienter under Section 10(b). The heightened pleading standard of the PSLRA was satisfied because the defendants were in the position of knowing that it was likely that IMO 2020 would reduce revenue, yet did not make corresponding disclosures, the Second Circuit concluded. The panel vacated the dismissal as to all claims and remanded the case to the district court.

The petition. Filed in May 2023, the petition asks whether the Second Circuit erred in holding that failing to make a disclosure required under Item 303 can support a private claim under Section 10(b), even in the absence of an otherwise-misleading statement. The case presents a square circuit split, Macquarie says, with the Third, Eleventh, and Ninth Circuits all holding that a failure to disclose under Item 303 is not enough on its own to support a private cause of action; the Fifth Circuit has said in dicta that it has never held that Item 303 creates a duty to disclose. In addition, the petition argues that the Supreme Court has repeatedly stated that the private right of action in the Exchange Act should not extend beyond its boundaries. The Second Circuit's expansion of Section 10(b) liability, then, conflicts with the Court's precedents.

Furthermore, Item 303 is not a suitable vehicle for an implied private right of action. The Item's disclosure obligations are meant to be flexible and general, and its disclosures comprise the type of "soft information" that is not objectively verifiable. Opening the door to private actions for violations of Item 303 amounts to allowing plaintiffs to plead "fraud by hindsight," which stands in tension with established precedent, the petition says.

Briefs. In its [brief in opposition](#), Moab argued that the petition concerns an issue of "diminishing importance." Macquarie stressed that the Court had granted certiorari in 2017 for a case out of the Second Circuit raising the same issue, [Leidos, Inc. v. Indiana Public Retirement System](#). The petition in *Leidos* centered around a conflict between the Second and Ninth Circuits, the Ninth being the first circuit to hold that an Item 303 violation cannot support a 10(b) claim. That petition, however, went unheard because the case settled. Moab's brief points out that the Solicitor General, as amicus in *Leidos*, sided with the Second Circuit. Plus, no other circuit has adopted the Ninth Circuit's reasoning, and there have been no other petitions raising the question since then. The circuit split is "superficial," and could disappear in time. The brief says that the Item 303 issue rarely arises and usually makes no difference to the outcome of the case because the claims are sustained only when investors can meet 10(b)'s other elements (which the Second Circuit held Moab had done).

Macquarie countered in its [reply](#) that the "split is anything but 'superficial.'" Three circuits fundamentally disagree with the Second about whether an issuer can be sued for an omission simply by failing to speak under Item 303. Moab is overlooking the distinction between a pure omission—which would not be actionable—and a half-truth, where a duty to disclose would arise because the speaker's affirmative statements would otherwise be misleading.

The brief goes on to note that plaintiffs have unsurprisingly included more Item 303 claims in securities cases in the Second Circuit than in the Ninth. Instead of being "rare," Macquarie suggests that Item 303 "remains fertile ground for litigation, and, successful or not, companies must aggressively, and expensively, defend themselves. Since the three circuits seeing the most securities cases have already weighed in, the court should resolve the split now, the brief contends.

The petition is [No. 22-1165](#).

Attorneys: Linda T. Coberly (Winston & Strawn LLP) for Macquarie Infrastructure Corp.; David C. Frederick (Kellogg, Hansen, Todd, Figel & Frederick, P.L.L.C.) for Moab Partners, L.P.

Companies: Macquarie Infrastructure Corp.; Moab Partners, L.P.

LitigationEnforcement: FraudManipulation InvestorEducation PublicCompanyReportingDisclosure
SupremeCtNews