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To read the decision in *Omnicare, Inc. v. Laborers District Council Construction Industry Pension Fund*, please click here.

Report from Washington

Supreme Court Clarifies Pleading Requirements for Claims Premised on Statements of Opinion under Section 11 of the Securities Act of 1933

March 26, 2015

The Supreme Court issued an opinion yesterday in *Omnicare, Inc. v. Laborers District Council Construction Industry Pension Fund*, which clarified the pleading requirements for claims based on statements of opinion under § 11 of the Securities Act of 1933. The Court held that an opinion can be "an untrue statement of a material fact" under the first clause of § 11 only if subjectively disbelieved at the time it is made. However, the Court also held that an opinion can form the basis for omissions liability under the second clause of § 11 if a plaintiff can plead particular material facts underlying the opinion, the omission of which made the opinion misleading "to a reasonable person reading the statement fairly and in context." While clarifying that sincerely held statements of opinion cannot be challenged as untrue statements of fact under the first clause of § 11, the Court's decision exposes defendants to potential liability under the second clause of § 11 with respect to omissions claims for certain statements of opinion.

Background

Omnicare concerned the pleading requirements under § 11, which provides a private right of action for any investor who purchases a security pursuant to a registration statement which "contained an untrue statement of a material fact or omitted to state a material fact . . . necessary to make the statements therein not misleading." 15 U.S.C. § 77k. The issue presented to the Court was whether a plaintiff must plead subjective falsity or only objective falsity of a statement of opinion to plead a cause of action under § 11.

Petitioners are Omnicare, Inc., the country's largest provider of pharmacy-related services for the elderly and other residents of long-term care facilities, and individuals who were officers or directors of Omnicare at the relevant time. Respondents are pension funds which

purchased shares of Omnicare stock in Omnicare's December 2005 public stock offering. The pension funds originally brought suit in 2006, alleging that statements in the registration statement were materially false or misleading at the time they were made, entitling respondents to relief under § 11.

Specifically, Omnicare's registration statement included statements of opinion as to legal compliance, such as "[w]e believe our contract arrangements with other healthcare providers, our pharmaceutical suppliers and our pharmacy practices are in compliance with applicable federal and state laws." The pension funds alleged that because some of Omnicare's contractual arrangements amounted to illegal kick-backs, this statement and others like it were materially false or misleading in violation of § 11. In order to avoid the heightened pleading burden triggered by an allegation of intent, respondents specifically disclaimed any allegation of fraud or intentional wrongdoing.

The district court dismissed the complaint for failure to state a claim, following the lead of the Second, Third, and Ninth Circuits in holding that a pleading of subjective falsity is required to make out a § 11 claim based on a statement of opinion. The Sixth Circuit reversed, holding that it was inappropriate for the district court to require the pension fund respondents to plead subjective knowledge to make out a claim because § 11 is a strict liability statute that does not require any allegation of scienter. In so doing, the court recognized its disagreement with its fellow circuits. The Supreme Court granted certiorari and heard oral argument in November 2014.

Summary of the Decision

"[T]he provision is not . . . an invitation to Monday morning quarterback an issuer's opinions."

- Justice Kagan

Justice Kagan wrote the majority opinion, which was joined in full by Chief Justice Roberts and Justices Alito, Breyer, Ginsburg, Kennedy, and Sotomayor. The Court first explained that while the lower courts had addressed the issue of false and misleading statements of opinion as one question, § 11 is properly read as two separate clauses—the first clause prohibits any "untrue statement of a material fact," and the second prohibits the omission of "a material fact . . . necessary to make the statements . . . not misleading." In addressing the first clause of § 11, the Court held that "every such statement [of opinion] explicitly affirms one fact: that the speaker actually holds the stated belief." Because the first clause of § 11 only prohibits untrue statements of material ***fact***, Justice Kagan reasoned that a statement of opinion can generally be the basis for liability under this clause only if the speaker subjectively disbelieved the opinion at the time the statement was made. Justice Kagan flatly rejected the view of both the Sixth Circuit and the respondents that Omnicare could be held liable under § 11 merely because its opinion ultimately proved to be wrong, holding that "a

sincere statement of pure opinion is not an 'untrue statement of material fact,' regardless whether an investor can ultimately prove the belief wrong."

Thus, to plead a violation of the first clause of § 11, plaintiffs must plead that the defendant subjectively disbelieved the opinion at the time it was made. The Court also recognized that opinion statements may give rise to liability under the first clause of § 11 where they contain "embedded statements of [untrue] fact."

The greater portion of the Court's opinion, however, is devoted to parsing the application of the omissions clause of § 11 to statements of opinion. The Court rejected Omnicare's contention that "no reasonable person, in any context, can understand a pure statement of opinion to convey anything more than the speaker's own mindset," holding instead that a reasonable investor may understand a statement of opinion to convey more than that, depending on the context. Specifically, a reasonable investor could understand a statement of opinion to convey "facts about how the speaker has formed the opinion" or "about the speaker's basis for holding that view." The Court went on to explain that "if a registration statement omits material facts about the issuer's inquiry into or knowledge concerning a statement of opinion, and if those facts conflict with what a reasonable investor would take from the statement itself, then § 11's omissions clause creates liability." The Court cautioned that the facts which can be inferred are inherently contextual, and the reasonable inferences that can be made are dependent on the type of opinion being given, the specificity of the statement, and the context of the opinion in the registration statement as a whole.

"To the extent our decision today chills misleading opinions, that is all to the good: In enacting § 11, Congress worked to ensure better, not just more, information."

– Justice Kagan

Justice Kagan looked to the common law for guidance on how a reasonable person understands statements of opinion. The common law tort of misrepresentation provided for liability for the omission of facts known to the speaker where those facts rebut the recipient's predictable inference based on a statement of opinion. Justice Kagan further expounded that the common law provided for greater liability for those who were understood "as having special knowledge of the matter which is not available" to the listener, which, in the case of the securities laws, applies to issuers, which are understood to have special knowledge about the information in their registration statements. Moreover, Justice Kagan found support for imposing liability for misleading opinions under § 11's second clause in the Congressional purpose in enacting the statute, which was meant to ensure that issuers tell the whole truth to investors: "An issuer must as well desist from misleading investors by saying one thing and holding back another" in addition to achieving literal accuracy in registration statements.

Finally, the Court rejected concerns about unpredictable standards for issuers, maintaining that such policy arguments are properly addressed to Congress and would be mitigated by

the heightened pleading standard under *Iqbal v. Ashcroft*. Indeed, Justice Kagan cast doubt on the sufficiency of the instant complaint, describing respondents' "recitation of the statutory language" as "not sufficient" and "conclusory," and asserting that respondents "cannot proceed without identifying one or more facts left out of Omnicare's registration statement." The Court also rejected Omnicare's policy arguments about chilling the flow of information to investors, indicating that "market-based forces push back against any inclination to under disclose" and that "Congress worked to ensure better, not just more, information." The Court vacated the decision below and remanded the case for application of this new standard to the facts of the matter.

Justice Scalia concurred in part and in the judgment, agreeing with the majority's analysis of the first clause of § 11 but disagreeing with its analysis of the second clause. Justice Scalia disputed the majority's account of the common law, arguing that the "effect of the Court's rule is to adopt a presumption of expertise on all topics volunteered within a registration statement," which Justice Scalia argued was appropriate only for those disclosures specifically required by law to be set forth in the statement. Justice Scalia further opined that even if that presumption was appropriate, the common law standard would focus not on the expectations of the listener but rather on the adequacy of the basis of the statement from the expert speaker's point of view, because a person receiving an expert opinion does not assess the adequacy of the basis of that opinion, but rather relies on the expertise of the speaker.

Justice Thomas concurred only in the judgment, agreeing only that the statements of opinion at issue in the case do not constitute an untrue statement of material fact. Unlike the majority, however, Justice Thomas opined that the issue of whether the statements constitute an actionable omission was not properly before the Court, having not been squarely addressed by the courts below.

Implications

While the Court's opinion clarifies that sincerely held statements of opinion cannot be challenged as untrue statements of fact under the first clause of § 11, this decision nevertheless exposes defendants to potential liability under the second clause of § 11 with respect to omissions claims for certain statements of opinion. While this risk is mitigated by the Court's requirement that any alleged omissions be pled with specificity, issuers should be aware that phrasing a statement as one of opinion rather than of fact does not immunize the statement from potential § 11 liability. Such statements of opinion should be included only when there is underlying support both for making the statement and concluding that the

opinion is not misleading to investors. The *Omnicare* decision creates a context and fact-specific test that, depending on the application by lower courts, could make it more difficult to obtain dismissal of § 11 claims at the pleading stage in certain cases.

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