Special Meeting of The Corporate Governance and Securities Litigation Committee - VIRTUAL via WebEx

Maryland State Retirement and Pension System
120 E. Baltimore Street, 16th Floor, Board Room
Baltimore, Maryland 21202

Tuesday, 12/19/2023
8:30 - 9:00 AM ET

For the purposes of receiving legal advice and consulting with staff about a pending securities litigation matter, pursuant to General Provisions Art. § 3-305(b)(7), to consult with counsel to obtain legal advice, and § 3-305(b)(8), to consult with staff, consultants, or other individuals about pending or potential litigation.

INFORMATION 1. Call Meeting to Order

ACTION ITEM 2. Motion to meet in Closed Session

Motion to meet in Closed Session for the purposes of receiving legal advice and consulting with staff about a pending securities litigation matter, pursuant to General Provisions Art. § 3-305(b)(7), to consult with counsel to obtain legal advice, and § 3-305(b)(8), to consult with staff, consultants, or other individuals about pending or potential litigation.

APPROVE…………DISAPPROVE

ACTION ITEM 3. Macquarie Infrastructure Corp. v. Moab Partners, L.P.

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APPROVE…………DISAPPROVE

ACTION ITEM 4. Motion to adjourn closed session and return to open session

APPROVE…………..DISAPPROVE

ACTION ITEM 5. Motion to adjourn the meeting

APPROVE…………..DISAPPROVE

OFFICE OF THE ATTORNEY GENERAL
MARYLAND STATE RETIREMENT AND PENSION SYSTEM
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December 13, 2023

PRIVILEGED AND CONFIDENTIAL ATTORNEY-CLIENT COMMUNICATION AND ATTORNEY WORK PRODUCT

TO: Members of the Corporate Governance and Securities Litigation Committee

FROM: Emily Spiering, Deputy Counsel and Michael Watts, Assistant Attorney General

RE: *Amicus Curiae* ("Friend of the Court") Participation in the U.S. Supreme Court's Review of *Macquarie Infrastructure Corp. v. Moab Partners, L.P.* , No. 21-2524, 2022 WL 17815767 (2d Cir. Dec. 20, 2022).

The Maryland State Retirement and Pension System ("System") has been asked to join an *amicus* brief to be filed on behalf of institutional investors on December 20, 2023, in a case before the U.S. Supreme Court from the Second Circuit, *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, No. 22-1165. The issue in the case is whether violations of disclosure obligations imposed under Securities and Exchange Commission ("SEC") regulations may form the basis of private securities litigation actions brought by investors. The Supreme Court's ultimate decision in the case could limit investor remedies for violations of required SEC reporting upon which investors rely, resulting in less than a full and fair disclosure to investors of material risks to company financial operations which are known to corporations.

Consistent with the Committee's authority under Paragraph 14 of its charter, we recommend that the Committee consider authorizing the Executive Director to sign the *amicus* brief on behalf of the Board of Trustees, if the Office of the Attorney General ("OAG") gives final approval for the System to sign on to the brief.[1] A

[1] We are currently seeking formal OAG approval and expect to have a response no later than 12/19.

copy of the draft proposed amicus brief and outside counsel's recommendation memorandum are attached.

Background:

This case concerns whether violations of "Item 303" of SEC Regulation S-K, which requires companies to disclose in their SEC filings material known trends that are reasonably likely to impact the company's financial condition, are actionable under the antifraud rights of action provided by Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5.

Section 10(b) of the Exchange Act prohibits deception in connection with the purchase or sale of securities. To that end, SEC Rule 10b-5 declares it unlawful to make an untrue statement or omit a material fact "necessary" to make an affirmative statement "not misleading." 17 C.F.R. § 240.10b-5(b). A violation of this requirement can give rise to a private claim.

Item 303 of SEC Regulation S-K, Management's Discussion and Analysis of Financial Condition and Results of Operations, is an administrative regulation that outlines which portions of the Management Discussion and Analysis ("MD&A") section are required to be disclosed in periodic reports with the SEC. Item 303 requires companies to disclose known trends or uncertainties that are "reasonably likely to have a material effect on [the registrant's] financial condition or operating performance." Any known trend which is likely to occur needs to be disclosed unless company management reasonably concludes that it will not have a material effect on the company's financials. By placing the onus on management to find there is no financial impact, the SEC allows a company some leeway to determine whether disclosure is required. A question concerning Item 303 disclosures can lead to an SEC inquiry and potentially an enforcement action if the SEC finds it warranted.

U.S. courts are split as to whether failures to disclose known trends in violation of Item 303, absent an affirmative misstatement of fact, can form the basis of an Exchange Act Section 10(b) securities fraud claim. The Ninth Circuit, in *In re NVIDIA Corp. Sec. Litig.*, 768 F.3d 1046 (9th Cir. 2014), held that an Item 303 disclosure failure cannot give rise to a fraud claim because the standard for a material omission under Item 303 is different (and less demanding) than the standard for materiality for a securities fraud claim. The Ninth Circuit has held that a duty to disclose must "be separately shown" to support private Section 10(b) liability. *NVIDIA*, 768 F.3d at 1056.

In *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94, 103 (2d Cir. 2015), the Second Circuit took the opposing stance and ruled that violations of Item 303 can form the basis of an Exchange Act Section 10(b) securities fraud claim provided the other elements— *i.e.,* materiality, scienter, and loss causation—are sufficiently alleged. The Second Circuit stated that due to the obligatory nature of the SEC regulations, a reasonable investor would interpret the absence of a 303 disclosure to imply the nonexistence of known trends or uncertainties that the company reasonable expects will have an material unfavorable financial impact. *Id.* at 102. The Second Circuit subsequently maintained its position, citing its prior decisions repeatedly.

Meanwhile, other circuits have acknowledged the circuit split, while declining to take definitive stances. *See Mun. Emps.' Ret. Sys. of Mich. v. Pier 1 Imports, Inc*., 935 F.3d 424, 436 (5th Cir. 2019) (affirming that the circuit "ha[s] never held that Item 303 creates a duty to disclose under the Securities Exchange Act"); *Carvelli v. Ocwen Fin. Corp.*, 934 F.3d 1307, 1331 (11th Cir. 2019) (holding that an Item 303 violation does not automatically give rise to 10(b) liability).

In *Macquarie Infrastructure Corp. v. Moab Partners,* the Supreme Court is poised to resolve this split. Therein, Petitioners argue that the Second Circuit erred when it held that the failure to make a material disclosure required by Item 303 can provide a basis for claims under the Exchange Act if the other elements (materiality, scienter and causation) have been sufficiently pleaded. In *Macquarie*, Respondent Moab's central allegation is that between February 2016 and February 2018, Petitioner and its management defrauded investors in part by failing to disclose that one of its largest operations relied on a residual fuel oil known as "6-Oil." Respondent alleges that the reliance on this fuel was material information to investors because a new international regulation capping the sulfur content of oil would have a material negative impact on Petitioner's overall economic performance. Petitioners contend that even if disclosure was required by Item 303, the plain language of Exchange Act § 10(b) and Rule 10b-5 do not authorize a private right of action for a pure omission and therefore Rule 10b-5 does not give private plaintiffs the right to sue to enforce SEC regulations adopted under § 13(a).

Respondents argue that if the Court finds in favor of the Petitioners, companies will be able to withhold material information known to pose a risk to a company's financial operations without significant risk of recrimination. They argue that the ability of investors to enforce material violations of Item 303 helps ensure that the market is apprised of critical information relevant to a public company's health and financial outlook.

Importantly, outside counsel has advised that the SEC will be writing an *amicus* in support of Respondents' position and the U.S. Solicitor General will argue for the SEC alongside Respondents before the Supreme Court.[2] Respondents also argue that private rights of action arising from failures to disclose under Item 303 have the added benefit of supplementing SEC enforcement of this regulation, noting that SEC staffing substantially limits the ability of the SEC to review of Item 303 forms and investigate any alleged failures to comply.

Discussion:

The principal objectives of the Board of Trustees with respect to securities litigation are to: (1) fulfill the Board's fiduciary duty by effectively managing securities claims as assets of the System; and (2) maximize recovery of System assets on claims, while minimizing fees paid to obtain recoveries. Eliminating a private right of action to allow investors to seek redress for material violations of the SEC's disclosure obligations would leave enforcement solely to the SEC and disincentivize full and complete compliance with the SEC's disclosure obligations under Item 303, while limiting investors ability to recover losses caused by a material and willful failure to disclose.

Respondents believe that an *amicus* brief signed by institutional investors will send a powerful message to the Supreme Court that investors' rights are threatened by the weakening of Item 303 enforcement that will result from a Supreme Court decision in favor of the Petitioners and also help make clear to the Court the consequences of a decision that will limit the avenues of private litigants and possibly the SEC to enforce disclosure obligations like Item 3030. which is being written by Kevin K. Russell of Goldstein, Russell & Woofter, LLC, and funded by plaintiff's firm Kessler Topaz Meltzer & Check, LLP. Mr. Russell is a former U.S. Attorney for the Appellate Section of the U.S. Department of Justice and has argued thirteen merits cases in the Supreme Court and served as counsel or co-counsel in nearly fifty others.

Our office has reviewed an initial draft *amicus* brief for institutional investors and we will review and provide comments on successive drafts as we receive them. The draft *amicus* brief defends the Second Circuit's legal reasoning and persuasively argues that institutional investors play a vital role in maintaining the integrity of the U.S. securities markets, Item 303 disclosures are highly relevant to the investment decisions of institutional investors, and regulatory enforcement of Item 303 obligations is insufficient and must be aided by private actions. The brief

[2] *Amicus* briefs were filed in support of the Petitioner by the Washington Legal Foundation, Chamber of Commerce, Securities Industry and Financial Markets Association, Atlantic Legal Foundation, and the Society for Corporate Governance.

explains that institutional investors routinely review the Item 303 disclosures before making investment decisions and find these disclosures considerably more important than boilerplate reports of events which have already occurred. The *amicus* brief also persuasively rebuts a key claim to Petitioners' textualist argument that was not addressed by Respondents' initial brief.[3]

One of the firms in the Office of the Attorney General's securities litigation counsel pool, Bernstein Litowitz Berger & Grossman, LLC ("BLBG"), represents the Respondents in this litigation. BLBG urges the System to sign the *amicus* and notes that, as in *Macquarie*, Item 303 claims can be an important part of certain cases where Defendants have disclosed certain material trends and uncertainties but have remained silent on other negative material trends that, when disclosed, cause extreme market losses. BLBG further notes that because the parties dispute the full extent of statements and conduct that would remain in the case if the Supreme Court finds in Petitioners' favor, dismissal of the Item 303 allegations could have a negative impact on the ultimate class-wide recovery.[4] In addition to an *amicus* brief from institutional investors and the SEC, BLBG also expects briefs to be filed by Law and Business Professors, former SEC Officials, and American Association for Justice/Public Justice.

As of today, we understand that Discovery Capital Management, Oklahoma Firefighters Pension & Retirement System, the Fire and Police Association of Colorado, Colorado Public Employees Retirement Association, City of Providence Employees' Retirement System, Louisiana Municipal Police Employees Retirement System, and The Michigan Association of Public Employee Retirement Systems, on behalf of Michigan Pension and Retiree Healthcare Plans, have already indicated their intention to sign on to the brief. BLBG advises that a number of other plans are actively considering whether to sign on. The brief is due on December 20, and we have been asked to provide a decision **no later than December 19**, in order for the System to participate as a signatory.

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[3] Petitioners argue that Rule 10b-5 can only be read to impose liability for "misrepresentations and half-truths" and not "pure omissions," when the rule is read in conjunction with §11, which explicitly delineates liability between "material facts required to be stated" and a "material fact necessary to make the statements not misleading." The *amicus* brief astutely characterizes this as misdirection since Petitioners' omission would have only constituted a "pure omission" if they had left out the entire MD&A discussion rather than merely certain portions of it.

[4] The System incurred an estimated losses of $399,813.88 calculated on a First-In-First-Out ("FIFO") basis and $58,235 calculated on a Last-In-First-Out ("LIFO") basis.

<u>Action by the Corporate Governance and Securities Litigation Committee:</u>

Paragraph 14 of the charter for the Corporate Governance and Securities Litigation Committee provides as follows:

> *Pursuant to a policy adopted by the committee or on a case by case basis, and consistent with the policies of the board, the committee may delegate to the Executive Director the authority to sign or issue an amicus brief, advocacy statement or letter regarding a securities litigation matter on behalf of the Board, provided that the Executive Director first consults with the Chief Investment officer and the OAG.*

Consistent with the Committee's authority under Paragraph 14 of its charter, we recommend that the Committee consider authorizing the Executive Director to sign the *amicus* brief on behalf of the Board of Trustees, if the OAG gives formal approval for the System to sign on to the brief. We have conferred with Robert Burd (in the CIO's absence) and Martin Noven, and they support the recommendation. Any action will be reported to the Board of Trustees.

We will be available during closed session at a meeting of the Committee on Tuesday, December 19, 2023, at 8:30 a.m. to discuss this matter and answer any questions.

Attachment

cc: Martin Noven, Andrew Palmer, Toni Voglino, Robert Burd, Dominique Cherry, Rachel Cohen

ADVICE OF COUNSEL – NOT AN OPINION OF THE ATTORNEY GENERAL

No. 22-1165

IN THE

Supreme Court of the United States

MACQUARIE INFRASTRUCTURE CORP., ET AL.,

Petitioners,

v.

MOAB PARTNERS, L.P., ET AL., on behalf of itself and all others similarly situated,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF INSTITUTIONAL INVESTORS AS *AMICI CURIAE* IN SUPPORT OF RESPONDENTS

OTHERS

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TABLE OF AUTHORITIES

INTEREST OF AMICI CURIAE[1]

[List of tentative signatories:

- Discovery Capital Management
- Michigan Association of Public Employee Retirement Systems, on behalf of Michigan Pension and Retiree Healthcare Plans
- Oklahoma Firefighters Pension & Retirement System
- Colorado Public Employees Retirement Association
- City of Providence Employees Retirement System
- Louisiana Municipal Police Employees Retirement System

[1] No counsel for petitioners or respondents authored any part of this brief, and no person other than amicus curiae or its counsel made any monetary contribution to the preparation or submission of this brief.

SUMMARY OF ARGUMENT

Federal securities laws were enacted to provide investors confidence in our capital markets by ensuring them access to accurate information essential to the valuation of a company's shares. Congress thus imposed on issuers a variety of disclosure obligations and instructed the Securities and Exchange Commission ("SEC") to develop additional requirements. Congress and this Court have recognized that providing a private right of action to those injured by material violations of those disclosure obligations is essential to the proper functioning of the legal regime and our financial markets.

Amici institutional investors rely heavily not only on the accuracy of the information disclosed under this regime, but also the *completeness* of those disclosures. Item 303 disclosures are particularly important. Most information provided under federal securities law is backward-looking. That information is important, but stock valuations are principally based on a prediction of *future* performance. Item 303 plays an essential role in investors' assessment of whether past performance is likely to be repeated in the future by requiring management to disclose "material events and uncertainties known to management that are reasonably likely to cause reported financial information not to be necessarily indicative of future operating results or of future financial condition." 17 C.F.R. § 229.303(a).

Incomplete Item 303 disclosures can be exceedingly misleading, indeed even more misleading that outright misstatements. When an annual report purports to comply with Item 303, investors will understand the absence of any discussion of an event or trend to indicate that management does not believe it will occur, or that its impact on the firm will be immaterial. When that is not true, investors often would be better off if the company had made no Item 303 disclosure at all. At least then they would be on notice that they would need to conduct an independent, comprehensive assessment.

Such incomplete disclosures are actionable under Section 10(b). Contrary to petitioners' framing, this is not a case about pure omissions. Petitioners were not simply silent about Item 303 or future trends and events—they included in their annual report an extensive discussion that would lead reasonable investors to believe the disclosure was comprehensive and included all that Item 303 requires. Moreover, as required by 18 U.S.C. § 1350, the Company's CEO signed a certification attesting that the report "fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934," referring to the provisions under which Item 303 was promulgated. The omissions charged in this case rendered that certification and the seemingly complete MD&A discussion misleading.

Petitioners' policy objections are both beside the point (they should be directed to the SEC or to Congress) and unconvincing. Their complaints about the alleged ambiguity in Item 303 are doubly irrelevant. First, denying respondents a cause of action in this case will do nothing to affect petitioners' Item 303 obligations, which exist independent of any private right of enforcement. Second, the Item's more relaxed materiality requirement is entirely irrelevant to the question before the Court because private litigants must satisfy the ordinary materiality standard applied in all Section 10(b) cases.

Petitioners' rendition of issuers' traditional floodgates argument has no merit either. It ignores that Congress responded to concerns about meritless litigation with a variety of procedural protections, such as heightened pleading standards, not by carving out certain kinds of violations from the 10(b) private right of action. Nor can petitioners show any concerning flood of litigation in the Second Circuit, which has applied the rule petitioners oppose for nearly a decade without ill effect.

There is also no basis to petitioners' equally worn prediction that allowing private remedies for non-disclosure will prompt harmful over-disclosure. Petitioners ignore that the audience for these documents is not ordinary retail investors but highly sophisticated analysts and other investment professionals who routinely review significant amounts of information and are perfectly capable of ignoring irrelevant information. Moreover, balancing the benefits of disclosure against the costs of over-disclosure is best left in the expert hands of the SEC, which can tailor Item 303's requirements to reach the optimal balance. Indeed, the SEC has been attentive to this need, even modifying Item 303 after this suit was filed to "provide clarity and focus to registrants as they consider what information to discuss and analyze." Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information, Exchange Act Release No. 10890 ("2021 Guidance"), 86 Fed. Reg. 2080, 2089 (Jan. 11, 2021).

Finally, as the SEC has frequently explained to Congress and this Court, the Commission lacks the resources to adequately detect and address Item 303 violations on its own. Indeed, although the SEC endeavors to "undertake[] *some* level of review for each reporting company at least *once every three years*,"[2] even when it scrutinizes a report, the Commission's staff has no way of knowing what the MD&A has *failed* to disclose.

[2] SEC, Filing Review Process, https://www.sec.gov/divisions/corpfin/cffilingreview (emphasis added)

ARGUMENT

I. Federal Securities Law Assures Investors That They Can Rely On The Truth And Completeness Of Mandatory Disclosures.

Federal securities law arose as a response to the worst economic crisis in the Nation's history. In the run up to the stock market crash of 1929, "some 50 billions of new securities were floated in the United States." H.R. Rep. No. 73-85, at 2 (1933). "Fully half or $25,000,000,000 worth of securities floated during this period have been proved to be worthless," *ibid*., amounting to more than *half a trillion* dollars today adjusted for inflation.[3] Those losses were bad enough, but the loss of investor confidence in our capital markets was catastrophic.

Recognizing that restoration of that confidence was essential to ending the economic crisis and to the health of our free-market economy moving forward, Congress enacted the Securities Act of 1933 and the Securities Exchange Act of 1934. At the heart of both laws are mandatory disclosure obligations, the private enforceability of which is essential to their ability to provide investors confidence in the accuracy and completeness of those disclosures and, thereby, in our capital markets.

A. Federal Securities Law Were Enacted In Response To The Lack Of Reliable Investment Information.

Although Congress determined to root out fraud from securities trading, it realized that prohibitions against

[3] *See* U.S. Inflation Calculator, https://www.usinflation calculator.com (last visited December 8, 2023).

fraud would not be sufficient to restore and maintain investor confidence. Equally important was ensuring that investors had access to reliable information regarding the securities sold on national exchanges. *See, e.g.*, *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 194 (1976).

A central flaw Congress identified in securities markets leading up to the Great Depression was that investors lacked "facts essential to estimating the worth of any security." H.R. Rep. No. 73-85, at 2. To address that problem, Congress crafted new laws designed "to substitute a philosophy of full disclosure for the philosophy of *caveat emptor*." *Lorenzo v. SEC*, 139 S. Ct. 1094, 1103, (2019) (citation omitted). Thus, in drafting the Securities Exchange Act of 1934, "Congress expressly relied on the premise that securities markets are affected by information, and enacted legislation to facilitate an investor's reliance on the integrity of those markets." *Basic*, 485 U.S. 224, 245-46 (1988). It did so by imposing a variety of disclosure obligations on companies participating on national security exchanges and creating the Security Exchange Commission ("SEC") with a mandate to elaborate on those obligations by regulation. *See, e.g.*, 15 U.S.C. §§ 77e, 77g, 78m.

B. Private Remedies For Violations Of Federal Disclosure Obligations Is Critical To Market Confidence In The Disclosure Regime.

1. Congress recognized that investor confidence was unlikely to be restored if federal disclosure obligations were merely precatory. Left to their own devices, many companies would disclose only positive information and neglect the negative. Moreover, disclosures are only as helpful as they are accurate. After all, there was no shortage of disclosures in the lead-up to the Great Depression; the problem was that many were false or incomplete.

Congress also recognized that leaving enforcement solely to the SEC would be grossly insufficient. *See infra* XX. It enacted a series of private enforcement provisions that allowed those injured by violations of the Act's disclosure rules to recover, subject to a variety of requirements and limitations to protect defendants from meritless litigation. *See, e.g.*, 15 U.S.C. §§ 77k, 77*l*, 78r.

Whether Section 10(b) was one of those provisions was once a subject of debate, but no more. Congress has "ratified the implied right of action" under that provision, recognizing it as a "prominent feature of federal securities regulation." *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 164 (2008). In the Private Securities Litigation Reform Act of 1995 (PSLRA), Pub. L. No. 104-67, 109 Stat. 737, Congress rejected calls to eliminate the private 10(b) right of action, recognizing that the "success of the U.S. securities markets is largely the result of a high level of investor confidence in the integrity and efficiency of our markets"[4] and that retaining the private Section 10(b) right of action was necessary to "protect investors and to maintain confidence in the securities markets."[5] "[P]rivate rights of action are not only fundamental to the success of our securities markets," the Senate Report explained, "they are an essential complement to the SEC's own enforcement program." S. Rep. No. 104- 98, at 8 (quoting SEC Chairman Arthur Levitt).

This Court, too, has long recognized that "'private securities litigation [is] an indispensable tool with which defrauded investors can recover their losses'—a matter

[4] S. Rep. No. 104-98, at 8 (1995).

[5] H.R. Rep. No. 104-369, at 31 (1995) ("Conf. Rep.").

crucial to the integrity of domestic capital markets." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 320 n.4 (2007) (quoting *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, 547 U.S. 71, 81 (2006) (citation omitted)). It is the "SEC enforcement program *and* the availability of private rights of action *together* [that] provide a means for defrauded investors to recover damages and a powerful deterrent against violations of the securities laws." *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 174 n.10 (2008) (quoting S. Rep. No. 104-98, at 8 (June 19, 1995)). Accordingly, this Court has taken care not to construe the securities laws in a way that could "seriously impair the deterrent value of private rights of action" by diminishing "the incentives for [securities market actors] to comply with the federal securities laws." *Randall v. Loftsgaarden*, 478 U.S. 647, 664 (1986).

2. The availability of a private remedy is particularly important to institutional investors, who are entrusted with managing trillions of dollars in assets by some of the nation's most important institutions. In enacting the PSLRA, Congress noted that "[i]nstitutional investors are America's largest shareholders, with about $9.5 trillion in assets, accounting for 51% of the equity market." S. Rep. 104-98, at 11. By 2017, institutional investors held more than $21 trillion in equity, and nearly 80% of the shares, in the nation's largest companies.[6] Much of that is held on behalf of pension funds covering tens of millions of retired Americans, often on behalf of public employers like States, local government, and public universities. Each year,

[6] *See* Pensions & Investments, *80% of equity market cap held by institutions* (Apr. 25, 2017), https://www.pionline.com/article/20170425/INTERACTIVE/170429926/80-of-equity-market-cap-held-by-institutions.

institutional investors invest billions of additional dollars in the U.S. capital markets on behalf of their clients and beneficiaries.

The integrity and success of these funds is thus a matter imbued with the public interest. When violations of securities laws lead to investment losses for institutional investors, much of the cost is borne either by their beneficiaries (*i.e.*, individual workers saving for retirement or existing retirees) or public institutions and taxpayers (because in many cases, state and local governments are constitutionally obligated to guarantee defined-benefit retirement plans). Thus, institutional investors are vitally concerned that investors not be harmed by illegal conduct in the securities markets. At the same time, institutional investors have a long-term investment outlook and an interest in deterring meritless securities litigation.

Congress balanced the need to ensure a private remedy for such important institutions against concerns about meritless private securities litigation through provisions of the PSLRA intended to "increase the likelihood that institutional investors . . . would serve as lead plaintiffs." *Tellabs*, 551 U.S. at 321 (2007).[7] Congress understood that because institutional investors are injured both by securities violations *and* by meritless litigation (their income depending on the vitality of the companies they invest in), they are "parties more likely to balance the interests of the class with the long-term interests of the company." *Ibid*. Thus, Congress believed that "increasing the role of institutional investors" in securities litigation

[7] Specifically, the PSLRA created a rebuttable presumption that the plaintiff with "the largest financial interest in the relief sought by the class" should be appointed as lead plaintiff. 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I)(bb).

would "ultimately benefit shareholders and assist courts." Conf. Rep. at 34.

II. Complete and Accurate Item 303 Disclosures Are Vital to Institutional Investors.

Institutional investors and their investment advisors rely heavily on the insights provided by Item 303 disclosures, which are among the most important required by federal securities law. These disclosures are not mere boilerplate, but rather are a key component of analyzing a potential investment, by explaining the principal risks and challenges that a company faces, as known to its management.

A. Item 303 Provides Unique Insight About A Company's *Future* Performance

Investors are predominantly concerned about what the *future* holds for a company. *See, e.g.*, Michael J. Mauboussin and Dan Callahan, *Market-Expected Return on Investment: Bridging Accounting and Valuation* (April 14, 2021) ("A company's stock price reflects the expectation for future cash flows based on past, present, and prospective investments.").[8] Institutional investors (or their investment advisors) therefore undertake extensive research and analysis before investing in a particular company to try and determine the company's future performance. The scope of this undertaking necessarily varies by particular institutional investor or advisor, but invariably includes reviewing *all* of a company's SEC and other public disclosures.

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[8] https://www.morganstanley.com/im/publication/insights/articles/article_marketexpectedreturnoninvestment_en.pdf.

As petitioner acknowledges, most other mandatory disclosures relate to "historical financial information." Petr. Br. 9. Historical financial and other information can provide insight on a company's future performance. But past performance can be misleading when there is reason to think that the conditions giving rise to it are likely to change. For example, an annual report's extensive discussion of a company's presently robust liquidity may mislead investors about the company's future prospects when management expects that "customer demand is reasonably likely to fluctuate in response to rapid technological changes" or if the firm expects "a debt rating downgrade." Commission Statement About Management's Discussion and Analysis of Financial Condition and Results of Operations, Exchange Act Release No. 8056, 67 Fed. Reg. 3746, 3748 (Jan. 25, 2002).

That is where Item 303 comes in. It requires annual reports to include a "management discussion and analysis" ("MD&A") that, in narrative form, apprises investors of "material events and uncertainties known to management that are reasonably likely to cause reported financial information not to be necessarily indicative of future operating results or of future financial condition." 17 C.F.R. § 229.303(a) (emphasis added). This includes "any known trends or uncertainties that have had or that are reasonably likely to have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations." *Id.* § 229.303(b)(ii).

Thus, unlike most backward-looking disclosure requirements, Item 303 "call[s] for companies to provide investors" with information about their "prospects for the future." Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operation ("2003 Guidance"), Exchange Act Release No. 48960, 68 Fed. Reg. 75,056, 75,059 (Dec. 19, 2003). As the

Second Circuit observed, "Item 303 disclosures 'give investors an opportunity to look at the registrant through the eyes of management by providing a historical and prospective analysis of the registrant's financial condition and results of operations.'" *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94, 102 (2d Cir. 2015) (quoting Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures ("1989 Guidance"), Exchange Act Release No. 6835, 54 Fed. Reg. 22,427, 22,428 (May 24, 1989)).

Item 303 thus provides "[o]ne of the most important elements necessary to an understanding of a company's performance, and the extent to which reported financial information is indicative of future results." SEC Item 303 Guidance, at 75061. While information about past performance often may be reliably obtained elsewhere and likely is already reflected in the price of the stock, management is uniquely situated to identify firm-specific obstacles to future performance or to understand how generally known trends will affect a particular firm.

This case provides an excellent example of Item 303's unique value. All else equal, investors would reasonably assume that recent robust demand for Macquarie's storage services foretold similar demand for its services in the near- to mid-term. It would be highly material to investors, however, if management was aware that the regulations of an obscure international maritime regulator could dramatically affect demand for a particular kind of fuel oil that was responsible for a significant share of the company's present revenues. *See* Resp. Br. XX. Item 303 ensures that investors have access to that important insight so they can assess the company's value accurately.

B. Incomplete Item 303 Disclosures Are Particularly Misleading.

When a company files an incomplete Item 303 disclosure, the risk of misleading investors is no less than filing a disclosure that contains material falsehoods. Indeed, incomplete disclosures are particularly prone to misleading investors and can be more harmful than affirmative misstatements.

A hypothetical illustrates the point. If, for example, a regulation required a company to disclose all material debt obligations, investors would reasonably assume that any debt not listed does not exist or is not material. The incompleteness of the disclosure would be highly misleading. Indeed, a company's failure to disclose a $100 million debt would be far more misleading than disclosing the debt while misstating its amount by $10 million.

Institutional investors thus reasonably rely not only on the accuracy of required disclosures, but also their *completeness*. Generally, institutional investors conduct their own independent diligence, such as by questioning management, engaging industry consultants, or speaking with competitors. But if a company does not disclose a material known trend or uncertainty in its Item 303 disclosure, an institutional investor will reasonably assume that the trend or uncertainty does not exist (or is not material). They will not question management about that topic. And even if the investor could conduct an investigation to determine whether other material trends or uncertainties exist, they are unlikely to do so—analysts and investors have limited resources and understandably direct their research to other relevant matters.

Thus, non-disclosure under Item 303 is akin to Sir Arthur Conan Doyle's dog that did not bark in the night[9]—the absence of disclosure conveys the crucial message to institutional investors, *i.e.*, that the company is not aware of any other material trends or uncertainties with which investors should be concerned. *Cf. Leopold*, 987 F.3d at 167 ("The absence of particular evidence may sometimes provide clues as important as the presence of such evidence."); *Johnson v. Wells Fargo Bank, N.A.*, 744 F.3d 539, 543 (8th Cir. 2014) ("a list of what is missing is also evidence of what is not missing"). Institutional investors rely on this absence, *and its implications*—the dog not barking—in constructing the mosaic of information that they gather in deciding whether to invest in a company. As courts have observed in the national security context, "[w]hat may seem trivial to the uninformed, may appear of great moment to one who has a broad view of the scene and may put the questioned item of information in its proper context." *CIA v. Sims*, 471 U.S. 159, 178 (1985).

Indeed, when companies violate their obligation to make the complete disclosures required by law, investors may be worse off than if there had been no disclosure requirement at all. If they had no expectation that the company would make a full disclosure of its material debts, for example, investors would be on notice that they had to make their own judgments about this critical financial question. They might ask the company about its debts or conduct their own independent investigation. But they are

[9] *See, e.g.*, *Chisom v. Roemer*, 501 U.S. 380, 396 n.23 (1991) ("Congress' silence in this regard can be likened to the dog that did not bark.") (citing A. Doyle, Silver Blaze, in The Complete Sherlock Holmes 335 (1927)); *Church of Scientology of Cal. v. IRS*, 484 U.S. 9, 17-18 (1987); *Leopold v. CIA*, 987 F.3d 163, 167 & n.3 (D.C. Cir. 2021).

unlikely to do any of those things when they believe that already have that information because the company was required to provide a complete list of its material debts by law and has said nothing to indicate that it is not complying with that obligation.

IV. Incomplete Item 303 Disclosures Give Rise To Section 10b-5 Liability.

Petitioners nonetheless claim that Congress has provided no remedy for such deceit. For the reasons given by respondents, they are wrong. Amici emphasize two important points below.

1. This is not a case about pure omissions. *Contra* Petr. Br. 20-25; Washington Legal Foundation Br. 11-13, 15, 23; Atlantic Legal Foundation Br. 21; Society for Corporate Governance Br. 2. Petitioners did not simply omit, for example, the entire MD&A discussion from their annual reports. Had they done so, investors would have been on notice that they would be left to their own devices to figure out whether there were regulatory or other events on the horizon that could substantially disrupt demand for the Company's services. *See, e.g.*, Donald C. Langevoort & G. Mitu Gulati, *The Muddled Duty to Disclose Under Rule 10b-5*, 57 Vand. L. Rev. 1639, 1681 (2004) ("[I]f an issuer's response to a[n SEC] line-item were something along the lines of 'we cannot provide the information requested' or a simple failure to file completely, this would operate as a breach of the line-item requirement but not be a fraud. The investor is on notice of the noncompliance and would not be misled."). Instead, as in every Item 303 case, petitioners included a lengthy section in their report labeled "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations." *See, e.g.*, [Macquarie 2015 10-k at 56.]

In that context, institutional investors—who keenly focus on issuer's MD&A disclosures—would understand petitioners to be conveying that the report includes all the information required for an MD&A discussion under federal law, not simply part of it. As the Second Circuit reasoned, "[d]ue to the obligatory nature of these regulations, a reasonable investor would interpret the absence of an Item 303 disclosure to imply the nonexistence of 'known trends or uncertainties . . . that the registrant reasonably expects will have a material . . . unfavorable impact on . . . revenues or income from continuing operations.'" *Stratte-McClure*, 776 F.3d at 102 (quoting 17 C.F.R. § 229.303(a)(3)(ii)); *see also* Langevoort & Gulati, *supra*, at 1680 ("[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.").

Leaving out required information in this context is no less misleading than when an applicant for a mortgage fills out a form calling for a disclosure of all credit card debt, but leaves some of her cards off the list. In both cases, the incomplete disclosures "fall squarely within the rule that half-truths—representations that state the truth only so far as it goes, while omitting critical qualifying information—can be actionable misrepresentations." *Universal Health Svcs., Inc. v. United States*, 579 U.S. 176, 188 (2016). The "classic example of an actionable half-truth" arises when a property seller "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." *Ibid*. This case is even worse than the classic example, because the implication that the disclosure is complete is much stronger here—by using language that invokes the Item 303 obligation, petitioners unambiguously convey to the reader that they *knew* they had a *legal obligation* to completely disclose all of the information required by the regulation and were undertaking to fulfill it.

If that were not enough, Macquarie included a certification from its CEO, as required by 18 U.S.C. 1350, stating that the report "fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended" [Macquarie 2017 10-k, Exhibit 32.1]. Section 13(a) requires issuers to "file with the Commission . . . such information and documents (and such copies thereof) as the Commission shall require," including "such annual reports . . . as the Commission may prescribe." 15 U.S.C. § 78m(a)(1)-(2). And Item 303 describes part of the information the Commission requires be included in annual reports (*i.e.*, the MD&A section of the report). *See* 17 C.F.R. §§ 229.10(a)(2), 229.303. Macquarie's CEO thus expressly certified that the reports complied with all reporting requirements, including Item 303.

As required by 18 U.S.C. § 7241(a)(1), the annual reports further included certifications that, to officials' knowledge, the report did "not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading." *See, e.g.*, [Macquarie 2105 10-k at Ex. 31.1]. This language, of course, directly tracks the words of Section 10b-5.

In signing the legislation that imposed both certification requirements, President Bush explained that "[t]his law says to shareholders that the financial information you receive from a company will be true and reliable" and that under the statute, "CEOs and chief financial officers must personally vouch for the truth and fairness of their companies' disclosures." Remarks By the President at Signing of H.R. 3763, 2002 WL 1751366.

Petitioners note that Section 1350 "does not itself carry a private right of action," Br. 35 n.8, but false certifications can be the basis of fraud actions without the need for an express right of action to enforce the certification requirement. In *Universal Health Services*, for example, this Court did not doubt that a federal contractor would commit actionable fraud in seeking payment of an invoice by falsely certifying compliance with applicable contract requirements, even if there were no separate right of action to enforce the various contract rules. *See* 579 U.S. at 188.

2. Petitioners thus are wrong to frame this case as asking whether Section 10(b) provides a private right of action for violations of Item 303. The regulation simply provides a part of the background against which the company's affirmative statements are reasonably understood by investors.

Indeed, a defendant would actionably mislead investors by falsely implying compliance with a standard even if that standard were not legal and compliance was purely voluntary. For example, an annual report that invoked voluntary accounting standards of a private standard-setting body would be misleading if, in fact, it did not comply with those standards.

For purposes of the law of fraud (and, by implication, for claims under Section 10(b)) it makes no difference *why* a company has conveyed that it is disclosing everything required by a particular standard; it matters only *that* the company has conveyed that it is being comprehensive. So long as that representation is conveyed, investors will be misled by material deviations from the disclosure standard the defendant has invoked.

V. Petitioners' Policy Objections Are Irrelevant And Unfounded.

Petitioners and their amici raise a number of policy objections, complaining that Item 303's materiality standard is too lax and speculating that allowing a cause of action to investors injured by misleadingly incomplete MD&A disclosures will prompt a flood of meritless litigation and harmful over-disclosure. *See* Petr. Br. 41-45; SIFMA Br. 15-17, 19-21; Atlantic Legal Foundation Br. 14-18; Society for Corporate Governance Br. 11, 18-27; Washington Legal Foundation Br. 24-27. Those arguments are misdirected and unconvincing.

They are misdirected because this Court "does not presume that any result consistent with one party's account of the statute's overarching goal must be the law." *Slack Techs., LLC v. Pirani*, 598 U.S. 759, 769 (2023) (cleaned up). Petitioners' policy arguments simply rehash arguments Congress and the SEC have already considered and rejected. Congress responded to complaints that private lawsuits "chill corporate disclosure" in the PSLRA not by paring back coverage of the Section 10(b) private right-of-action, but by enacting a variety of protections against meritless litigation. S. Rep. 104-98 at 4-5; *see, e.g.*, *ibid*.; *Tellabs,* 551 U.S. at 320; *infra* XX. The SEC has likewise responded to calls to reduce unwarranted disclosure burdens, including with respect to Item 303 in particular.[10] For example, in 2021, the SEC amended Item 303 "to eliminate duplicative disclosures and modernize and

[10] *See, e.g.*, 2018 Guidance; Disclosure Update and Simplification, Exchange Act Release No. 10532, 83 Fed. Reg. 50,148 (October 4, 2018); Business and Financial Disclosure Required by Regulation S-K, Exchange Act Release No. SEC Release No. 10064, 81 Fed. Reg. 23,916 (April 22, 2016); 2002 Guidance.

enhance MD&A disclosures for the benefit of investors, while simplifying compliance efforts for registrants." 2021 Guidance, at 2080. Those modifications were supported by many issuers and their trade associations, including some of petitioners' amici.[11]

Petitioners may think the SEC has not done enough. But how much is too much disclosure is ultimately a matter of judgment, as is weighing the potential costs of over-disclosure against the benefits of private enforcement (including deterrence and compensation for injured investors). The SEC is the entity within the federal government charged with tailoring disclosure rules to strike what it deems to be the best balance of those competing interests.

All that said, even if this Court thought it appropriate to consider petitioner's policy argument itself, none has any merit.

A. Petitioners' Complaints About Item 303's Requirements Provide No Basis For Comprehensively Eliminating Private Omissions Claims.

Petitioners and their amici complain at length that figuring out what must be disclosed under Item 303 is complicated and uncertain. *See, e.g.*, Petr. Br. 41-45; SIFMA Br. 7-10; Atlantic Legal Foundation Br. 9-14; Society for Corporate Governance Br. 7-14, 27-31; Washington Legal

[11] *See, e.g.,* Letter to SEC from U.S Chamber of Commerc's Center for Capital Markets Competitiveness (May 4, 2020, *available at https://www.sec.gov/comments/s7-01-20/s70120-7149390-216380.pdf*; Letter to SEC from Securities Industry and Financial Markets Association (Apr. 28, 2020), *available at https://www.sec.gov/comments/s7-01-20/s70120-7130286-216134.pdf*.

Foundation Br. 22-24. They ignore, however, the significant steps the SEC has taken—some after this case was brought—to provide clarity. *See, e.g.*, 2021 Guidance, at 2089 (explaining revisions to regulation were intended to "provide clarity and focus to registrants as they consider what information to discuss and analyze"); 1989 Guidance (interpretative release providing guidance on Item 303 requirements); *id*. at 22,427 & n.5 (collecting prior guidance).

More importantly, however, nothing in petitioners' legal arguments turns on the alleged ambiguity in Item 303's requirements—their reasoning would preclude private claims relating to even the clearest disclosure obligation (*e.g.*, a rule requiring disclosure of every person owning more than 10% of the company's stock). And their proposed solution is a poor fit for the alleged problem—as petitioners emphasize, compliance with Item 303 is still required, subject to enforcement action and civil penalties by the SEC. Petr. Br. 29, 41-45.

Indeed, petitioners' and amici's principal objection—that Item 303's materiality requirement is less demanding than what is usually required to state a claim for fraud—applies *only* to cases brought by the Commission. In a private suit, plaintiffs must satisfy the same standard that would apply if instead of omitting a known trend that threatened its business, the company had acknowledged the trend but lied about its expected impact on the firm. *See, e.g.*, *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94, 100 (2d Cir. 2015).[12]

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[12] Some amici argue that even the *Basic* standard materiality requirement is insufficient protection for defendants. *See, e.g.,* Washington Legal Foundation Br. 25 n.14. But this Court has repeatedly reaffirmed the standard and Congress has declined to

B. Allowing A Private Remedy In This Context Will Not Open The Floodgates To Meritless Litigation.

Nor is there any merit to the petitioners' rendition of the classic objection that ruling against the issuer in this case will open the floodgates of meritless securities litigation.

1. This Court has heard and rejected such predictions before, noting the multiple protections against meritless suits Congress included in the original legislation and enhanced in the PSLRA. *See, e.g.*, *Tellabs,* 551 U.S. at 320. For example, as just noted, private litigants must satisfy the same materiality element required in every Section 10(b) case, precluding suits over a defendants' failure to include information in the MD&A that does not alter the "'total mix' of information made available" in the market. *Basic*, 485 U.S. at 232 (citation omitted). Among other things, this allows issuers to defend against Item 303 claims by showing that the information it allegedly failed to disclose was already known to the market. *See, e.g.*, *Ganino v. Citizens Utils. Co*., 228 F.3d 154, 167 (2d Cir. 2000).

To the extent issuers complain that the SEC has not provided sufficient guidance regarding what must be included the MD&A discussion, Congress offered substantial protection against good faith mistakes by by requiring proof of scienter. *See United States ex rel. Schuette v. SuperValu Inc.*, 598 U.S. 739, 750-53 (2023) (discussing common law scienter requirement's application to good-faith mistakes of law). The PSLRA's heightened pleading requirements for scienter provide

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disturb it. *See, e.g.*, *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 39-40 & n.4 (2011).

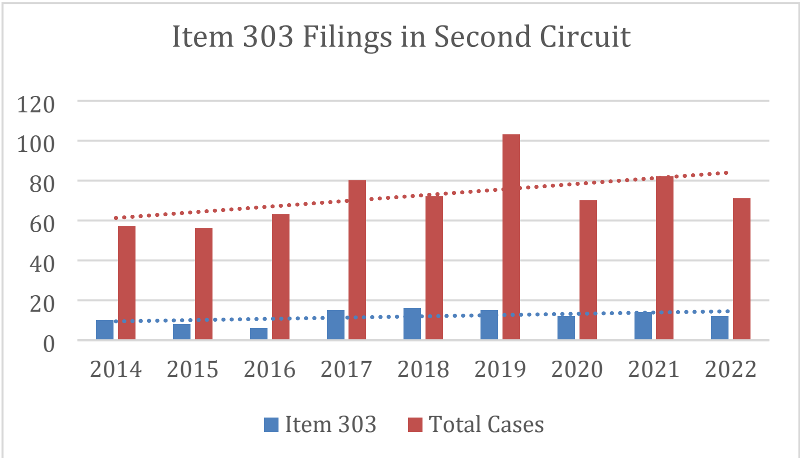
additional protection, requiring early dismissal of cases in which plaintiffs cannot plead facts giving rise to "strong inference of scienter." 15 U.S.C. § 78u-4(b)(2). At the same time, other elements of the claim must be pleaded with particularity under Federal Rule of Civil Procedure 9, and the PSLRA stays discovery until the Complaint has been tested against those pleading standards through a motion to dismiss. 15 U.S.C. § 78u-4(b)(3)(B).

In addition, as the SEC has emphasized, "[a]ny forward-looking information supplied" in an MD&A "is expressly covered by the safe-harbor rule for projections" in the PSLRA. 17 C.F.R. § 229.303(b) (citing 17 CFR 230.175, 240.3b–6); *see also* 15 U.S.C. § 78u-5(c). And recoveries are subject to important PSLRA limitations. 15 U.S.C. § 78u-4(a)(4), (a)(6), (b)(4).

2. The experience of the Second Circuit—which has recognized claims based on misleading Item 303 omissions since 2015—does not bear out petitioners' dire predictions.

To start, only a fraction of securities cases filed in the Second Circuit include Item 303 claims and that number has remained relatively steady, even as the overall number of securities class actions has increased.[13]

[13] This chart is drawn from the list of Item 303 cases in Appendix E to the petition for certiorari and data on total securities filings by circuit. *See* Janeen McIntosh *et al*, *Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review* 5 (Jan. 24, 2023) (data on securities class action filings by circuit for 2018-2022); Stefan Boettrich and Svetlana Starykh, *Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review* 1 (Jan. 29, 2019) (same for 2014-2018).



Moreover, precluding claims based on Item 303 omissions would not eliminate any material number of lawsuits, given that such suits invariably include other claims and theories of liability as well. *See* Doug Green, Securities Claims Based on Item 303 of Regulation S-K: It Just Doesn't Matter (Sep. 30, 2015) (opining that "very rarely, if ever, would there be an omitted fact that gives rise to an Item 303 claim without also rendering false or misleading one or more challenged statements").[14] This case is a good example: the Item 303 allegations are but one of many claims in the case, which petitioners acknowledge will continue regardless of how this Court resolves the Question Presented. *See* BIO 9-10; Pet. 12 n.3.

Petitioners' own list of Item 303 cases from the Second Circuit also illustrates the robustness of the multitude of protections defendants enjoy against meritless suits. *See* Pet. App. E. For example, of the cases filed in 2020, more than 40% were disposed of by successful motions to

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[14] Https://www.dandodiscourse.com/2015/09/30/securities-claims-based-on-item-303-of-regulation-s-k-it-just-doesnt-matter/.

dismiss, with the Item 303 claims generally failing for inability to satisfy the Second Circuit's test for such omissions, for lack of materiality, and/or failure to adequately plead scienter.[15] That is consistent with the rate of dismissal for securities complaints across the board.[16]

C. Amici's Over-Disclosure Objections Are Meritless.

Some of petitioners' amici speculate that allowing a private right of action for misleading Item 303 disclosures will lead to burdensome over disclosure. *See, e.g.*, Chamber Br. 11-16; Society for Corporate Governance Br. 19-26. That prediction has no merit either.

To start, the Court should reject the premise that the mere prospect that private enforcement could encourage some degree of unnecessary disclosure is a reason to abandon the substantial countervailing benefits private enforcement brings. As discussed, the information required by Item 303 is of vital importance to investors. If petitioners' amici are right that the level of MD&A disclosures is driven by the availability of a private right of action, then eliminating that action will predictably lead to significantly less of these important insights reaching markets. And while analysts and investors can easily ignore excess information, they are particularly ill-equipped to discover Item 303 information on their own when it is omitted.

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[15] Based on a review of PACER entries for cases listed in Pet. App. E.

[16] *See* Cornerstone Research, Securities Class Action Filings: 2022 Year in Review 22 ("Cornerstone 2022") ("From 1997 to 2022, 46% of core federal filings were settled, 43% were dismissed, 0.5% were remanded, and 10% are continuing.")

At the same time, while amici agree that over disclosure is harmful to some extent, petitioners' amici overstate its costs. The principal audience for Item 303 disclosures is not the casual citizen investor; it is market analysts and sophisticated investors like amici who have the training, time, and resources to process inevitably dense financial reports. Such readers are not easily diverted by the inclusion of perhaps unnecessary information and frequently spend significant time reviewing other kinds of documents from a variety of sources that are far less rich in relevant information.

In any event, no one has produced any evidence that Item 303's MD&A requirement—much less private litigation regarding misleading MD&A disclosures—has inundated investors with useless information in the Second Circuit. Instead, petitioners' amici simply reprise the same generic objections defendants raise in every case involving a disclosure obligation. Most of their complaints, and nearly all of their purported evidence, relates not to Item 303 but to issuers' general sense at times that their *overall* disclosure obligations under *all* of federal securities law was too burdensome. *See, e.g.*, Chamber Br. 13-16. Much of that evidence is badly dated, going back a decade or more and predating the Commission's 2016-2021 revisions to streamline the federal disclosure regime and Item 303 in particular. *See, e.g.*, Chamber Br. 13-14, 16 & n.9 (citing reports and speeches from 2007, 2011, 2012, 2013). Little of it relates to Item 303 in particular, instead taking issue with being burdened by "boilerplate, redundant, immaterial, irrelevant, and overly fact-packed" disclosures. *Id*. at 14 (quoting Arthur J. Radin, *Have We Created Financial Disclosure Overload?*, CPA J., Nov. 2007, at 6 (2007)). But as discussed, Item 303 provides uniquely relevant and important information unavailable from other sources.

Even if the Court were persuaded that issuers presently make excessive disclosures, there is no reason to think that allowing private claims based on misleading MD&A omissions will make matters materially worse. Again, precluding a private action does not change what Item 303 requires to be disclosed. Petitioners suggest issuers will take an excessively liberal view of those requirements to avoid private litigation. But that argument ignores that private litigation will continue to be governed by traditional materiality standards. Accordingly, it is no surprise that petitioners are unable to show, for example, that the MD&A's of companies potentially subject to suit in the Second Circuit are meaningfully different from those of other firms.

D. SEC Enforcement Is Insufficient.

Petitioners assure the Court that the SEC can step in to fill the void if the Court eliminates private suits for deceptive MD&A omissions. Petr. Br. 45-46. But that is clearly wrong.

Given the size of U.S. capital markets, it is simply impossible for any government agency to meaningfully scrutinize every regulated statement and disclosure made to investors. The Commission recently reported to Congress that the "SEC is charged with overseeing approximately $100 trillion in annual securities trading on U.S. equity markets and the activities of more than 28,000 registered entities," in addition to "24 national securities exchanges, nine credit rating agencies, and seven active registered clearing agencies" and a variety of other governmental and quasi-governmental entities.[17] Part of

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[17] SEC, Fiscal Year 2022 Congressional Budget Justification, Annual Performance Plan 2 ("SEC FY 2022 Report"), *available at*

that oversight includes "reviewing the disclosures and financial statements of more than 7,400 reporting companies." *Ibid*.

"As our capital markets have grown, though, the SEC has not." *Id*. at 4. Today, the SEC performs its work with about 10% of the staff of Goldman Sachs, just one of the thousands of companies it regulates.[18] Around 400 employees are charged with overseeing tens of thousands of annual and quarterly reports filed with the SEC, along with other duties.[19]

Petitioners argue that the SEC's "informal comment-letter process" provides adequate investor protection. Petr. Br. 45. Not so. Although the Commission screens filings and occasionally comments on MD&A disclosures, it cannot and does not review every report filed with the Commission for compliance with mandatory disclosure rules. *Contra* Petr. Br. 45. Instead, it "undertakes *some* level of review of each reporting company at least *once every three years*."[20] Moreover, the SEC is in no position to detect when a company has *omitted* material trends or uncertainties from its reports. It has no way of knowing, for example, whether new regulations from the International Maritime Organization will reduce the

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https://www.sec.gov/files/fy-2022-congressional-budget-justification-annual-performance-plan_final.pdf.

[18] *Compare id*. at 4 (in 2022, SEC had fewer than 4,400 staff); Goldman Sachs, About US (reporting nearly 40,000 employees), https://www.goldmansachs.com/about-us/.

[19] SEC FY2022 Report at 26-27.

[20] SEC, Filing Review Process, https://www.sec.gov/divisions/corpfin/cffilingreview (emphasis added).

demand for No. 6 oil, or whether that will significantly decrease demand for Macquarie's services.

It is understandable, then, that the SEC brings only a handful of actions each year for violations of disclosure rules.[21] It appears that only one or two include alleged violations of Item 303.[22] The infrequency of enforcement actions reflects the Commission's lack of resources and inherent inability to know when a company has omitted important Item 303 information, not that it believes compliance is adequate. *Contra* Petr. Br. 45-46.

Even setting aside the SEC's inability to adequately prevent and deter Item 303 violations, Petitioners' argument ignores the remedial purpose of the Section 10(b) private right of action. Congress has recognized investor confidence in our markets depends not only on a belief that violations will be relatively infrequent, but also on the assurance that when violations do occur and inflict substantial losses, investors will have a realistic means for being made whole. SEC enforcement cannot come close to fulfilling that role. In FY2022, for example, the SEC recovered approximately $194 million in disgorgement

[21] Cornerstone Research, SEC Enforcement Activity: Public Companies and Subsidiaries 2-3 ("Cornerstone FY2022 Report") (38% of the 67 enforcement actions brought in FY2022 involved reporting and disclosure violations), https://www.law.nyu.edu/sites/default/files/SEC-Enforcement-Activity-FY2022-Update.pdf.

[22] See Br. Petr. 43, *Leidos, Inc. v. Indiana Pub. Retir. Sys.*, 2017 WL 2729693 (2017).

remedies for injured investors.[23] In comparison, private litigation secured $4 billion in settlements.[24]

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be affirmed.

Respectfully submitted,

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December 20, 2023

[23] *See* Cornerstone FY2022 Report at 9.

[24] NERA, Recent Trends in Securities Class Action Litigation: 2022 Full-Year Review 13, 20 (Jan. 24, 2023).

Amicus Support for Pending Supreme Court Appeal in *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*

We are writing to ask whether you would consider joining other prominent institutional investors in an amicus brief to be submitted in a case of critical importance that will be heard by the Supreme Court early next year. The amicus brief is being written by a prominent appellate advocate, Kevin Russell of Goldstein, Russell & Woofter LLC, and will impose no costs on you.

On September 29, 2023, the Supreme Court agreed to hear Defendants' partial appeal of the Second Circuit's recent opinion in *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, No. 21-2524 ("*Macquarie*") during its next term. Bernstein Litowitz Berger & Grossmann LLP serves as Lead Counsel on behalf of Lead Plaintiff Moab Partners, L.P. ("Moab") in the case. The case concerns "Item 303"—a Securities and Exchange Commission ("SEC") regulation that requires public companies to disclose in their SEC filings material known trends that are reasonably likely to impact the company's financial condition. For over a decade, the Second Circuit Court of Appeals has affirmatively held that violations of the disclosure obligations set forth in Item 303 may form the basis not only of SEC enforcement actions, but also of private actions brought under Section 10(b) of the Securities and Exchange Act ("Exchange Act"), so long as Section 10(b)'s other stringent pleading elements (materiality, scienter and causation) are satisfied. The Ninth Circuit has taken an opposite view, holding that Item 303 disclosure violations cannot be the basis of a claim under the Exchange Act. This Circuit split has been percolating for several years, and now seems poised to be decided by the Supreme Court.

Investors' ability to enforce material violations of Item 303 helps ensure that the market is apprised of critical information relevant to a public company's financial health and outlook. Accordingly, the SEC will be writing an amicus in support of the Plaintiffs' position and will argue alongside Plaintiffs before the Court. In addition, other interested groups—including former SEC officials as well as law and business professors—will also be submitting amicus briefs in support of the investor position. However, it would be truly impactful to express the views of those most directly injured by corporate wrongdoers' violation of Item 303: prominent and influential institutional investors like you.

I. Item 303 And The Circuit Split

Item 303 of Regulation S-K, Management's Discussion and Analysis of Financial Condition and Results of Operations, outlines the required portions of the MD&A section required to be included in periodic reports with the SEC. According to the SEC, the overriding requirement of Item 303 is to "provide readers information 'necessary to an understanding of [a company's] financial condition, changes in financial condition and results of operations.'" The SEC provides that disclosure is mandatory where there is a known trend or uncertainty that is "reasonably likely to have a material effect on [the registrant's] financial condition or operating performance." The SEC's two-part test for a duty to report under Item 303 for a known trend is:

> (1) Is the known trend . . . likely to come to fruition? If management determines that it is not reasonably likely to occur, no disclosure is required.
>
> (2) If management cannot make that determination, it must evaluate objectively the consequences of the known trend . . . on the assumption that it will come to fruition. Disclosure is then required unless management determines

> that a material effect on the registrant's financial condition or results of operations is not reasonably likely to occur.

The SEC's two-part test highlights that any known trend which is likely to occur needs to be disclosed unless management reasonably concludes that it will not have a material effect on the company's financials. By placing the onus on management to find there is no financial impact, the SEC promotes the disclosure of known trends to the company's investors.

In *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94, 103 (2d Cir. 2015), the Second Circuit ruled that violations of Item 303 can form the basis of an Exchange Act Section 10(b) securities fraud claim provided the other elements—i.e. materiality, scienter, and loss causation—are sufficiently alleged. This ruling created a circuit split from the Ninth Circuit's ruling in *In re NVIDIA Corp. Sec. Litig.*, 768 F.3d 1046 (9th Cir. 2014), which held that an Item 303 disclosure failure cannot give rise to a fraud claim because, in the Ninth Circuit's view, the standard for a material omission under Item 303 is different (and less demanding) than the standard for materiality for a securities fraud claim. The Supreme Court was poised to resolve the circuit split in 2018 in an appeal of a Second Circuit opinion that applied *Stratte-McClure*. That case, *Leidos, Inc. v. Indiana Public Retirement System*, settled after the parties and several amici briefed the issues but before the Supreme Court held oral argument.

II. The Supreme Court Will Resolve the Circuit Split And Determine Item 303's Reach

Macquarie involves securities claims asserted by court-appointed Lead Plaintiff Moab for alleged violations of Section 10(b) of the Exchange Act, as well as Section 11 of the Securities Act of 1933, on behalf of investors in Macquarie Infrastructure Corp. ("Macquarie"). Moab alleges misstatements, "half-truths" and omissions of mandated Item 303 disclosures concerning the financial reliance of IMTT, a bulk-liquid storage provider and one of Macquarie's largest operations, on a highly toxic residual fuel oil known as "6-Oil," which is used primarily to power large shipping vessels. IMTT's reliance on 6-Oil was material information to investors because an international regulation ("IMO 2020") was poised to largely eliminate the market for 6-Oil and directly threatened Macquarie's future revenues and operations.

The Second Circuit sustained Moab's claims that Defendants made false statements and "half-truths" that rendered otherwise truthful statements misleading under the Exchange Act. *See Moab Partners, L.P. v. Macquarie Infrastructure Corp.*, No. 21-2524, 2022 WL 17815767, at *3 (2d Cir. Dec. 20, 2022). Those holdings are not before the Supreme Court. The sole issue before the Supreme Court is Moab's claim that Defendants violated Section 10(b) by failing to disclose IMTT's (and by extension Macquarie's) material reliance on 6-oil and the likely expected impact of IMO 2020 on Macquarie's financial performance, in violation of Regulation S-K, Item 303. *See Macquarie*, 2022 WL 17815767, at *3.

On September 29, 2023, the U.S. Supreme Court granted Macquarie's petition for certification of the following question: "Whether the Second Circuit erred in holding. . . that a failure 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." On November 13, 2023, Macquarie filed its opening brief, and on November 2020, 2023, several amicus briefs were filed in support of Macquarie's appeal, including by the Washington Legal Foundation, Chamber of Commerce, Securities Industry and Financial Markets Association, Atlantic Legal Foundation, and the Society for Corporate Governance. Moab's opposition brief is due on December 13, 2023, and amicus briefs in support of Moab's position are due by December 20, 2023. As noted above, the amicus brief on behalf of institutional investors is being written by a prominent appellate advocate, Kevin Russell of Goldstein, Russell & Woofter LLC.

III. If The Supreme Court Sides With Defendants, Companies May Withhold Material Information Known To Pose A Risk To Their Financial Operations Without Risk of Recrimination

The Item 303 issue again before the Supreme Court is a straightforward one with direct consequences to investors' rights to full and fair disclosure: is an omission of a material known trend that is reasonably likely to have a material effect on a company's financial condition or operating performance (i.e., a violation of Item 303's affirmative disclosure duty) actionable under the antifraud rights of action provided by the Exchange Act's Section 10(b) and Rule 10b-5?

A small group of institutional investors jointly filed an amicus brief in *Leidos* arguing, among other points, that institutional investors play a vital role in maintaining the integrity of the U.S. securities markets, Item 303 disclosures are highly relevant to their investment decisions, and regulatory enforcement of Item 303 obligations is insufficient and must be aided by private actions. With respect to the importance of Item 303, the institutional investors' brief in Leidos explained that they "routinely review the [Item 303] disclosures before making investment decisions" and find these disclosures "considerably more important than boilerplate reports of things that have already happened." In other words, the brief argued, the ability to bring Section 10(b) claims premised on a public company's failure to comply with Item 303—even where there is no affirmative misrepresentation—is an important mechanism to ensure that investors have access to all material information when making investment decisions. Given the U.S. Supreme Court's continuing interest in this question, we strongly encourage like-minded institutional investors to again seek to present these views in *Macquarie*. We believe that an amicus brief signed by a diverse and even larger array of influential institutional investors will send a powerful message to the Court that investors' rights are threatened by the requested weakening of Item 303 enforcement.

An institutional investor amicus brief also will help make clear to the Court the consequences of a decision that limits the avenues available for private litigants and possibly the SEC to enforce disclosure obligations like Item 303.

Moreover, certain of the various amicus briefs submitted in support of Macquarie argue that Item 303 disclosures are 'essentially useless information' and even that fulsome Item 303 disclosure (and enforcement of the same) will somehow harm investors. An institutional investor amicus brief will help make very clear that these fears are unfounded and further emphasize the importance of accurate Item 303 disclosures for investors.

* * *

As in *Leidos* and other Supreme Court cases in which corporate defendants have sought to restrict the private right of action under the federal securities laws, the views of institutional investors acting as amicus curiae are vital. We fully expect the Chamber of Commerce and other interested amici to submit briefs in support of Macquarie's position minimizing the importance of the corporate disclosures that are governed by Item 303. Without private enforcement of this important disclosure obligation under Section 10(b), issuers will be incentivized to soften and dilute these disclosures in their annual and quarterly reports with the SEC. For these reasons, we seek your assistance in this important judicial cause.