CLEARY GOTTLIEB

ALERT MEMORANDUM

April 3, 2015 clearygottlieb.com

In *Omnicare*, Supreme Court Clarifies the Scope of Liability for Statements of Opinion Under Section 11 of the Securities Act of 1933

On March 24, 2015, the U.S. Supreme Court issued *Omnicare, Inc. v. Laborers District Council Construction Industry Pension Fund*, in which it clarified the scope of liability for statements of opinion under Section 11 of the Securities Act of 1933. In particular, the Court held that statements of opinion can be actionable as *misstatements* under Section 11 only if the plaintiff pleads and proves that the speaker did not actually hold the stated belief or if the statement of opinion contains explicit, supporting facts that are untrue. The Court further held that statements of opinion can be actionable as *omissions* under Section 11 if the speaker does not disclose the factual basis for the opinion, and if those facts conflict with what a reasonable investor would take from the statement itself. Importantly, the Court also rejected the position that a statement of opinion can be actionable if it simply turns out to be wrong. Taken together, these holdings are likely to shift litigation concerning statements of opinion under Section 11 towards issues concerning the basis for disclosed opinions, and may place increasing importance on other potential defenses to liability for those opinions (such as the bespeaks caution doctrine and the PSLRA's safe harbor for forward-looking statements).

Background

Section 11 of the Securities Act of 1933 creates liability if "any part of [a] registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading."

Prior to the Supreme Court's *Omnicare* decision, several Circuit Courts issued conflicting decisions concerning when a statement of opinion could constitute "an untrue statement of a material fact" for purposes of Section 11. Some courts (including the Second and Ninth Circuits) held that the only statement of fact conveyed in a statement of opinion is that the speaker actually holds the disclosed opinion. As such, these courts concluded that a statement of opinion could only be actionable as "an untrue statement of a material fact" under Section 11 if the plaintiff pled and proved that the speaker did not truly hold its opinion when made. Other courts (including the First and Third Circuits) issued similar rulings, while also leaving open the possibility that statements of opinion could be actionable under Section 11 if they lacked a reasonable basis. More recently, the Tenth Circuit issued a decision raising the further possibility that statements of opinion may never be "the stuff of section 11 liability" because the text of Section 11 only mentions statements of fact and "many common law authorities took a dim view of opinion liability."

© Cleary Gottlieb Steen & Hamilton LLP, 2015. All rights reserved.

This memorandum was prepared as a service to clients and other friends of Cleary Gottlieb to report on recent developments that may be of interest to them. The information in it is therefore general, and should not be considered or relied on as legal advice. Throughout this memorandum, "Cleary Gottlieb" and the "firm" refer to Cleary Gottlieb Steen & Hamilton LLP and its affiliated entities in certain jurisdictions, and the term "offices" includes offices of those affiliated entities.

In *Omnicare*, however, the Sixth Circuit took a markedly different approach to the issue of liability for statements of opinion under Section 11. *Omnicare* involved a pharmacy services company, which the government alleged had received illegal kickbacks from drug manufacturers. After the revelation of this information, investors filed claims under Section 11 challenging the company's earlier disclosures that it "believe[d]" its contracts were "legally and economically valid" and "in compliance with applicable" law. The Sixth Circuit recognized that these statements reflected the company's opinion and beliefs, but nonetheless held that the plaintiffs were not required to plead that the company did not believe its disclosed opinion because Section 11 is "a strict liability claim" that does not require a showing of fraudulent intent. Instead, the Sixth Circuit only required the plaintiffs to plead that the statement of opinion was objectively false (i.e., turned out to be incorrect) to state a claim under Section 11.

The Supreme Court's Decision

Justice Kagan's opinion for the Court rejected the approach adopted by the Sixth Circuit as "wrongly conflat[ing] facts and opinions." Based on dictionary definitions and "our everyday ways of speaking," she (writing on behalf of seven justices) concluded that facts differ from opinions in that a statement of fact "expresses certainty about a thing, whereas a statement of opinion does not." The Court therefore concluded that a statement of opinion is not rendered false simply because the opinion turns out to be erroneous, because "the words 'I believe' themselves admitted that possibility." To hold otherwise, would "allow investors to second-guess inherently subjective and uncertain assessments" (or to "Monday morning quarterback an issuer's opinions"), which the Court stated would be inconsistent with the limitation of Section 11's misstatement clause to factual statements. Nonetheless, the Court modified the analysis applied by the other Circuit Courts to consider the issue, in order to reflect the possibility that statements of opinion could be actionable as *omissions* under certain circumstances. In doing so, the Court identified three separate situations where a statement of opinion could be actionable under Section 11 as either a misstatement or an omission.

First, as several Circuit Courts had previously held, the Court concluded that statements of opinion can be considered "untrue statement[s] of fact" if the speaker did not actually believe its disclosed opinion because every statement of opinion "explicitly affirms one fact: that the speaker actually holds the stated belief." However, the Court held that the plaintiffs in *Omnicare* had not established liability under this theory because they "d[id] not contest that Omnicare's opinion was honestly held," and instead "explicitly 'exclude[d] and disclaim[ed]' any allegation sounding in fraud or deception."

Second, the Court held that a statement of opinion could be actionable as an "untrue statement of fact" under Section 11 if it contains additional, "embedded statements of fact" that are untrue. For example, the Court observed that the statement "I believe our TVs have the highest resolution available because we use a patented

technology" could be false if the company at issue did not actually use a patented technology. Here, the portion of the statement giving rise to potential liability is not one of opinion, but of fact: "we use a patented technology."

Third, the Court held that statements of opinion may be actionable under Section 11's "omissions provision" under certain, limited circumstances. In particular, the Court stated that "a reasonable investor may, depending on the circumstances, understand an opinion statement to convey facts about how the speaker has formed the opinion." Therefore, "if the real facts are otherwise, but not provided, the opinion statement will mislead its audience" and can be actionable as an omission. However, the Court identified several important limitations to this basis of liability, including that:

- an opinion statement "is not necessarily misleading when an issuer knows, but fails to disclose, some fact cutting the other way" because "[r]easonable investors understand that opinions sometimes rest on a weighing of competing facts";

- "whether an omission makes an expression of opinion misleading always depends on context" and an opinion must therefore be read "in light of all its surrounding text, including hedges, disclaimers, and apparently conflicting information," as well as "the customs and practices of the relevant industry"; and

- an "investor cannot just say that the issuer failed to reveal its basis" but must instead "identify particular (and material) facts . . . whose omission makes the opinion statement at issue misleading to a reasonable person reading the statement fairly and in context," which the Court characterized as "no small task for an investor."

Moreover, the Court explicitly stated that, "to avoid exposure for omissions under § 11, an issuer need only divulge an opinion's basis, or else make clear the real tentativeness of its belief."

Implications of the Court's Decision

With respect to Section 11's "untrue statement of material fact" clause, the *Omnicare* decision adopts the earlier majority rule that pure statements of opinion can only be actionable if they are not truly held, which the Court indicated would require an allegation of "fraud or deception." Thus, under *Omnicare*, claims asserting that pure statements of opinion are affirmatively misleading must be dismissed unless the complaint contains factual allegations, sufficient to satisfy the heightened pleading requirements of Rule 9(b), that the speaker in fact did not believe the expressed opinion.

With respect to Section 11's "omissions provision," however, there may be increased litigation concerning the basis for a company's disclosed opinions. But to reiterate what the Court cautioned in this regard, an "investor cannot just say that the issuer failed to reveal its basis" but must instead "identify particular (and material) facts . . . whose omission makes the opinion statement at issue misleading to a reasonable person reading the statement fairly and in context," which the Court characterized as "no small task for an investor." Further, to the extent that plaintiffs challenge statements of opinion concerning an issuer's anticipated future performance (as they often do), defendants should bear in mind that such statements of opinion also may be protected under the bespeaks caution doctrine or the PSLRA's safe harbor for forward-looking statements, which were not addressed by the Court in *Omnicare*.

If you have any questions, please feel free to contact any of your regular contacts at the firm. You may also contact our partners and counsel listed under "Litigation and Arbitration" or "Capital Markets" located in the "Practices" section of our website at http://www.clearygottlieb.com.

Office Locations

NEW YORK
One Liberty Plaza
New York, NY 10006-1470
T: +1 212 225 2000
F: +1 212 225 3999

WASHINGTON
2000 Pennsylvania Avenue, NW
Washington, DC 20006-1801
T: +1 202 974 1500
F: +1 202 974 1999

PARIS
12, rue de Tilsitt
75008 Paris, France
T: +33 1 40 74 68 00
F: +33 1 40 74 68 88

BRUSSELS
Rue de la Loi 57
1040 Brussels, Belgium
T: +32 2 287 2000
F: +32 2 231 1661

LONDON
City Place House
55 Basinghall Street
London EC2V 5EH, England
T: +44 20 7614 2200
F: +44 20 7600 1698

MOSCOW
Cleary Gottlieb Steen & Hamilton LLC
Paveletskaya Square 2/3
Moscow, Russia 115054
T: +7 495 660 8500
F: +7 495 660 8505

FRANKFURT
Main Tower
Neue Mainzer Strasse 52
60311 Frankfurt am Main, Germany
T: +49 69 97103 0
F: +49 69 97103 199

COLOGNE
Theodor-Heuss-Ring 9
50668 Cologne, Germany
T: +49 221 80040 0
F: +49 221 80040 199

ROME
Piazza di Spagna 15
00187 Rome, Italy
T: +39 06 69 52 21
F: +39 06 69 20 06 65

MILAN
Via San Paolo 7
20121 Milan, Italy
T: +39 02 72 60 81
F: +39 02 86 98 44 40

HONG KONG
Cleary Gottlieb Steen & Hamilton (Hong Kong)
Hysan Place, 37th Floor
500 Hennessy Road, Causeway Bay
Hong Kong
T: +852 2521 4122
F: +852 2845 9026

BEIJING
Cleary Gottlieb Steen & Hamilton LLP
45th Floor, Fortune Financial Center
5 Dong San Huan Zhong Lu
Chaoyang District
Beijing 100020, China
T: +86 10 5920 1000
F: +86 10 5879 3902

BUENOS AIRES
CGSH International Legal Services, LLP-
Sucursal Argentina
Avda. Quintana 529, 4to piso
1129 Ciudad Autonoma de Buenos Aires
Argentina
T: +54 11 5556 8900
F: +54 11 5556 8999

SÃO PAULO
Cleary Gottlieb Steen & Hamilton
Consultores em Direito Estrangeiro
Rua Funchal, 418, 13 Andar
São Paulo, SP Brazil 04551-060
T: +55 11 2196 7200
F: +55 11 2196 7299

ABU DHABI
Al Sila Tower, 27th Floor
Abu Dhabi Global Market Square
Al Maryah Island, PO Box 29920
Abu Dhabi, United Arab Emirates
T: +971 2 412 1700
F: +971 2 412 1899

SEOUL
Cleary Gottlieb Steen & Hamilton LLP
Foreign Legal Consultant Office
19F, Ferrum Tower
19, Eulji-ro 5-gil, Jung-gu
Seoul 100-210, Korea
T:+82 2 6353 8000
F:+82 2 6353 8099