No. 22-1165

IN THE
Supreme Court of the United States

MACQUARIE INFRASTRUCTURE CORP., ET AL.,
Petitioners,

v.

MOAB PARTNERS, L.P., ET AL.,
Respondents.

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

BRIEF FOR THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION, THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, AND BUSINESS ROUNDTABLE AS AMICI CURIAE SUPPORTING PETITIONERS

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TABLE OF CONTENTS

Page:

INTEREST OF THE *AMICI CURIAE* 1

SUMMARY OF ARGUMENT 3

ARGUMENT 4

A. Item 303 provides a standard for disclosure that is too malleable and too deferential to impose an actionable duty under Rule 10b-5. . 4

B. The Second Circuit's rule contravenes this Court's warnings that Rule 10b-5 should not push companies to disclose a mountain of "essentially useless information." 11

C. The Second Circuit's approach undermines Item 303's objective of providing investors access to management's perspective. 17

D. Expanding Rule 10b-5's private right of action will encourage even more costly nuisance suits. 19

CONCLUSION 22

TABLE OF AUTHORITIES

Page(s):

Cases:

Arber v. Essex Wire Corp.,
490 F.2d 414 (6th Cir. 1974) 10

Basic Inc. v. Levinson,
485 U.S. 224 (1988) 3, 11

Blue Chip Stamps v. Manor Drug Stores,
421 U.S. 723 (1975) 19

Buckman Co. v. Plaintiffs' Legal Comm.,
531 U.S. 341 (2001) 17

Carvelli v. Ocwen Fin. Corp.,
934 F.3d 1307 (11th Cir. 2019) 6, 15

Isquith ex rel. Isquith v. Middle S. Utilities, Inc.,
847 F.2d 186 (5th Cir. 1988) 10

In re Kirchner,
Exchange Act Release No. 80947, File No. 3-18024 (SEC June 15, 2017) 16

Matrixx Initiatives, Inc. v. Siracusano,
563 U.S. 27 (2011) 11

Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit,
547 U.S. 71 (2006) 19

In re NVIDIA Corp. Secs. Litig.,
768 F.3d 1046 (9th Cir. 2014) 6, 15

Oran v. Stafford,
226 F.3d 275 (3d Cir. 2000) 6, 15

Rodman v. Grant Found.,
608 F.2d 64 (2d Cir. 1979) 10

Steckman v. Hart Brewing, Inc.,
143 F.3d 1293 (9th Cir. 1998) 9

Stoneridge Inv. Partners v. Scientific-Atlanta, Inc.,
552 U.S. 148 (2008) 19

Stratte-McClure v. Morgan Stanley,
776 F.3d 94 (2d Cir. 2015) 2

TSC Indus., Inc. v. Northway, Inc.,
426 U.S. 438 (1976) 12

Statute:

Securities Exchange Act of 1934,
15 U.S.C. § 78a *et seq.* 2

Regulations:

17 C.F.R. § 229.303 .... 2, 5

17 C.F.R. § 229.303(a) 5, 7, 18

17 C.F.R. § 229.303(b)(2)(ii) 7

17 C.F.R. § 240.10b-5 2

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Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, SEC Release No. 6835, 1989 WL 1092885 (May 18, 1989) 4, 5, 6, 8, 9, 18

Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information, 85 Fed. Reg. 12068 (Feb. 28, 2020) 14, 15

Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information, 86 Fed. Reg. 2080 (Jan. 11, 2021) 7, 8, 14, 18

Lauren M. Mastronardi, Note, *Shining the Light a Little Brighter: Should Item 303 Serve as a Basis for Liability Under Rule 10b-5?*, 85 Fordham L. Rev. 335 (2016) 10

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Mary Jo White, Chair, Secs. & Exch. Comm'n, *The Path Forward on Disclosure* (Oct. 15, 2013), https://www.sec.gov/news/speech/spch101513mjw 13

INTEREST OF THE *AMICI CURIAE*[1]

The Securities Industry and Financial Markets Association ("SIFMA") is a securities industry trade association representing the interests of hundreds of securities firms, banks, and financial asset managers across the United States. SIFMA's mission is to support a strong financial sector while promoting investor opportunity, capital formation, job creation, economic growth, and the cultivation of public trust and confidence in the financial markets.

The Chamber of Commerce of the United States of America ("Chamber") is the world's largest business federation. It represents approximately 300,000 direct members and indirectly represents the interests of more than three million companies and professional organizations of every size, in every economic sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae* briefs in cases, like this one, that raise issues of concern to the nation's business community.

Business Roundtable represents the chief executive officers ("CEOs") of over 200 of America's leading companies. The CEO members lead U.S.-based companies that support one in four American jobs and almost a quarter of U.S. gross domestic product. Business

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[1] No counsel for a party authored any part of this brief, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amici curiae*, their members, or their counsel made a monetary contribution to the brief's preparation or submission.

Roundtable was founded on the belief that businesses should play an active and effective role in the formulation of public policy, and Business Roundtable members develop and advocate for policies to promote a thriving U.S. economy and expanded opportunity for all. Business Roundtable participates in litigation as *amicus curiae* when important business interests are at stake.

Many of *amici*'s members are subject to the Securities Exchange Act of 1934 (Exchange Act), 15 U.S.C. § 78a *et seq.*, and accordingly, Rule 10b-5, 17 C.F.R. § 240.10b–5. They are also subject to Regulation S-K and, specifically, to its Item 303, which calls for management to discuss and analyze certain "trends" and "uncertainties." 17 C.F.R. § 229.303. For decades, *amici*'s members and other issuers of publicly traded securities understood that omissions pursuant to Item 303 are not actionable under Rule 10b-5, and approached management's discussion and analysis with that understanding.

That settled approach was upended by the Second Circuit's decision in *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94 (2d Cir. 2015), and its progeny. Breaking from the longstanding precedents of other circuits, the Second Circuit held that "Item 303 imposes the type of duty to speak that can, in appropriate cases, give rise to liability under Section 10(b)" and Rule 10b-5. *Id.* at 102 & n.5. The Second Circuit's erroneous rule means that public companies must *overdisclose* or incur risk simply by omitting a disclosure in any remotely doubtful case. Such overdisclosure is hardly benign. This Court, the SEC, and scholars have all warned against bloated disclosures that bury actually useful information in a pile of verbal junk. The Second

Circuit's interpretation aggravates this problem. Moreover, if this Court were to expand Rule 10b-5's private right of action to include Item 303 violations, the already-troubling burden of costly nuisance suits would swell. Congress has tried, without success, to quash such strike suits; this Court should not open a new vista for them. *Amici* have an interest in restoring the proper boundaries of Rule 10b-5.

SUMMARY OF ARGUMENT

A failure to satisfy Item 303's disclosure obligations cannot be shoehorned into a securities fraud action under Rule 10b-5. The two provisions are essentially a mismatch. Although Item 303's forward-looking disclosure obligations may be couched in mandatory terms, the breadth and amorphousness of Item 303's reporting standards make it difficult in many instances to determine when management is obligated to make a disclosure. Such open-ended standards do not lend themselves to an actionable fraud claim under Rule 10b-5, as courts have long held. The Second Circuit erred in departing from this consensus.

The Second Circuit's approach perniciously incentivizes companies to overdisclose. No one is well-served by prophylactic, heavily-lawyered disclosures—page after page, footnote after footnote—that are more likely to confuse an investor than inform. In *Basic Inc. v. Levinson*, this Court cautioned that Rule 10b-5 should not be interpreted in a way that would merely flood the market with "essentially useless information." 485 U.S. 224, 234 (1988). That principle weighs heavily here: because Item 303's standard is so loose and so vague, corporate officers often will be unable to conclude with the necessary certainty that a particular contingency can safely be omitted. If any arguable

misapplication of the standard will result in a class action lawsuit (or many), then the inevitable choice is to put out more and more management's discussion and analysis ("MD&A") under the heading of Item 303.

The Second Circuit's rule also tends to deprive investors of the principal benefit of MD&A: the opportunity to see the company through "the eyes of management." The inevitable effect of creating a private cause of action for alleged violations of Item 303 is that MD&A disclosures morph from management's candid prediction of intangible trends in their business—the useful purpose behind adopting Item 303—into a pre-litigation document shaped largely by lawyers.

Finally, securities litigation is already far too costly and prone to meritless nuisance suits—especially in the class action context. Expanding the implied private cause of action under Rule 10b-5 to encompass omitted disclosures required under Item 303 would greatly exacerbate this harmful trend. This Court should reverse.

ARGUMENT

A. Item 303 provides a standard for disclosure that is too malleable and too deferential to impose an actionable duty under Rule 10b-5.

By design, Item 303 is a provision requiring judgment calls about uncertain future events. It contains few bright lines, precisely because the SEC wrote the provision to be "intentionally flexible," *Management's Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures*, SEC Release No. 33-6835, 1989 WL 1092885, at *17 (May 18, 1989) ("SEC Release"). Gen-

erally, what must be included under Item 303 depends on management's subjective predictions about what is "reasonably likely" to happen.

Subjective, uncertain predictions are an inappropriate foundation for Rule 10b-5 liability. Allowing plaintiffs' lawyers to litigate Item 303's judgment calls under Rule 10b-5 creates a severe penalty for making a wrong guess about the future. This reality compels corporate officers to include more and more speculation about more and more contingent events, because of the risk that a decision *not* to include a particular uncertainty may be subject to second-guessing by a private plaintiff and, ultimately, a jury.

1. Item 303 of Regulation S-K requires disclosure of a wide range of information concerning a company's "financial condition and result of operations," 17 C.F.R. § 229.303. Unlike Rule 10b-5, which uses a rule of materiality to winnow liability, Item 303 is designed to be capacious—to encourage management to disclose enough information so that an investor has "an opportunity to look at the company through the eyes of management." SEC Release, 1989 WL 1092885, at *3; *see* 17 C.F.R. § 229.303(a) (Item 303 disclosures are designed "to better allow investors to view the registrant from management's perspective"). Those differing standards powerfully underscore why the substance of Item 303 and the procedural mechanism of the Rule 10b-5 private civil action are fundamentally a mismatch for one another. They cannot be judicially fused together into a new and uniquely plaintiff-friendly cause of action.

Indeed, both the SEC and the courts have repeatedly recognized the tension between the scope of what

management is supposed to disclose under Item 303 and the scope of the materiality standard this Court applied in *Basic*. Because the scope of the former is generally much broader, the SEC itself called the *Basic* test "inapposite" in the Item 303 context: "The probability/magnitude test for materiality approved by the Supreme Court in [*Basic*] is inapposite." SEC Release, 1989 WL 1092885, at *6 n.27. And several circuits have agreed. *See, e.g.*, *Carvelli v. Ocwen Fin. Corp.*, 934 F.3d 1307, 1331 (11th Cir. 2019) ("On its face, Item 303 imposes a more sweeping disclosure obligation than Rule 10b-5, such that a violation of the former does not *ipso facto* indicate a violation of the latter."); *In re NVIDIA Corp. Secs. Litig.*, 768 F.3d 1046, 1055 (9th Cir. 2014) ("Management's duty to disclose under Item 303 is much broader than what is required under the standard pronounced in *Basic*."); *Oran v. Stafford*, 226 F.3d 275, 288 (3d Cir. 2000) (Alito, J.) (noting that "the materiality standards for Rule 10b-5 and SK-303 differ significantly").

In essence, Item 303 considers whether a disclosure or omission *could be* material, not whether it *is* material. *See* SEC Release, 1989 WL 1092885, at *6 n.27 ("MD&A . . . specifies its own standard for disclosure—*i.e.*, reasonably likely to have a material effect."). Because "Item 303, at least in some cases, has a lower threshold for disclosure than does normal materiality, . . . disclosures required under Item 303 do not always implicate normal materiality standards." Brian Neach, Note, *Item 303's Role in Private Causes of Action Under*

the Federal Securities Laws, 76 Notre Dame L. Rev. 741, 756 (2001).[2]

2. The provision of Item 303 at issue here requires disclosure of "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." 17 C.F.R. § 229.303(b)(2)(ii).[3] The regulation makes clear that "whether a matter is 'reasonably likely' to have a material impact on future operations is based on 'management's assessment.'" 2021 Final Rule, 86 Fed. Reg. at 2093 (quoting 17 C.F.R. § 229.303(a)). This standard is consistent with Item 303's objective "to better allow investors to view the registrant *from management's perspective*." 17 C.F.R. § 229.303(a) (emphasis added).

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[2] This is not a circumstance in which one (broader) standard subsumes the other (narrower) standard; here they are qualitatively different. Indeed, in some circumstances, the materiality test under Rule 10b-5 may require more disclosure than Item 303's standard—a fact that the SEC recently cited to further underscore why the *Basic* standard is inapposite for Item 303. *See* Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information, 86 Fed. Reg. 2080, 2094 (Jan. 11, 2021) ("2021 Final Rule") ("[T]he probability/magnitude test could result in disclosure of issues that are large in potential magnitude but low in probability.").

[3] This is the current version of the provision, following the 2021 amendments to Item 303. Although this case is governed by the previous version of Item 303, the amendments do not alter the analysis here. *See* Pet. 5 n.1; *see also* 2021 Final Rule, 86 Fed. Reg. at 2093 (SEC explaining its view that the 2021 "amendments reflect a standard that is consistent with longstanding Commission guidance"). This brief cites Item 303's current language unless otherwise noted.

Determining whether disclosure is necessary under this aspect of Item 303 requires multiple steps. SEC Release, 1989 WL 1092885, at *6. First, a company's management "should consider whether a known trend, demand, commitment, event, or uncertainty is *likely* to come to fruition." 2021 Final Rule, 86 Fed. Reg. at 2093; *see also* SEC Release, 1989 WL 1092885, at *6. Next, management must assess whether "such known trend, demand, commitment, event or uncertainty would reasonably be likely to have a material effect on the registrant's future results or financial condition." 2021 Final Rule, 86 Fed. Reg. at 2093. Where management cannot determine whether the "trend, demand, commitment, event, or uncertainty" is likely to come to fruition but it would have a material impact were it to come to fruition, management must assess whether "a reasonable investor would consider omission of the information as significantly altering the mix of information made available in the registrant's disclosures." *Id.* at 2093-2094.

The SEC has introduced a further complication. As the SEC stated in a 1989 guidance document on compliance with Item 303, there is a

> distinction between prospective information that is required to be discussed and voluntary forward-looking disclosure. . . . The distinction between the two rests with the nature of the prediction required. Required disclosure [under Item 303] is based on *currently known trends, events, and uncertainties that are reasonably expected to have material effects*, such as: A reduction in the registrant's product prices; erosion in the registrant's

> market share; changes in insurance coverage; or the likely non-renewal of a material contract. In contrast, optional forward-looking disclosure involves *anticipating a future trend or event or anticipating a less predictable impact of a known event, trend or uncertainty*.

SEC Release, 1989 WL 1092885, at *4.

3. Thus, Item 303 asks management to make a series of difficult judgments: to assess (for example) whether there is an "uncertainty"; to assess how likely the uncertain contingency is to come about; and to assess whether, *if* it comes about sometime in the future, it is "reasonably likely" to have a material effect at that future time. If so, the "uncertainty" must be written up under Item 303. But if the impact would instead be "less predictable," *id.*, then assessing it is optional, not required. *Id.*[4]

It is difficult to discern when forward-looking information is sufficiently certain that it crosses the line from optional to mandatory. *See* Suzanne J. Romajas, Note, *The Duty to Disclose Forward-Looking Information: A Look at the Future of MD&A*, 61 Fordham L. Rev. S245, S286 (1993) ("[T]he distinction that the SEC has drawn between required and optional disclosures is so subtle that corporations and courts alike find Item 303 of Regulation S-K difficult to apply."). Despite decades of regulatory guidance, what Item 303 requires

[4] *Cf. Steckman v. Hart Brewing, Inc.*, 143 F.3d 1293, 1297-98 (9th Cir. 1998) (noting that "forward-looking statements" are "not required" under Item 303 and holding that prediction failure based on the known event of a slowdown was not actionable under section 12).

is still unclear. *See* Mark S. Croft, *MD&A: The Tightrope of Disclosure*, 45 S.C. L. Rev. 477, 478 (1994) ("Under Item 303 . . . the MD & A disclosure requirements are open-ended and exceedingly complex."); Lauren M. Mastronardi, Note, *Shining the Light a Little Brighter: Should Item 303 Serve as a Basis for Liability Under Rule 10b-5?*, 85 Fordham L. Rev. 335, 349 (2016) ("Despite this guidance from the SEC, the requirements under this section are flexible and complicated, leaving the company with a difficult task.").

4. The relevant history confirms that Item 303 was written to give flexibility to address difficult-to-foresee contingencies—not to create a litigation trip wire. Indeed, before the SEC adopted the regulation, courts had held that failure to disclose speculation—however likely the speculated-about outcome may be—was not actionable under the securities laws. *See, e.g.*, *Rodman v. Grant Found.*, 608 F.2d 64, 72 (2d Cir. 1979) ("Full factual disclosure need not be embellished with speculative financial predictions."); *Arber v. Essex Wire Corp.*, 490 F.2d 414, 421 (6th Cir. 1974) ("[T]he law mandates disclosure of only existing material facts. It does not require an insider to volunteer any economic forecast."). The SEC relaxed its position in 1978, "encouraging, although not requiring, disclosures of management projections both in filings with the SEC and in general." *Isquith ex rel. Isquith v. Middle S. Utilities, Inc.*, 847 F.2d 186, 205 (5th Cir. 1988) (quoting *Guides for Disclosure of Projections for Future Economic Performance*, SEC Release No. 5992 (Nov. 7, 1978)). That position eventually evolved into the current rule, which mandates disclosure of *some* predictions while leaving the disclosure of others optional. But nothing

in that history supports the notion that Item 303 could be weaponized by plaintiffs invoking Rule 10b-5.

B. The Second Circuit's rule contravenes this Court's warnings that Rule 10b-5 should not push companies to disclose a mountain of "essentially useless information."

By transforming Item 303 disclosures and omissions into a basis for Rule 10b-5 liability, the Second Circuit's rule encourages what Rule 10b-5 seeks to avoid: too much disclosure of "essentially useless information that a reasonable investor would not consider significant, even as part of a larger 'mix' of factors to consider in making his investment decision." *Basic*, 485 U.S. at 234. That directly undermines this Court's decision in *Basic*, which made clear that Rule 10b-5 is not intended to be used in that fashion.

1. Rule 10b-5 provides a private cause of action for representations or omissions that are "material" and "misleading." *E.g.*, *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 38 (2011); *Basic*, 485 U.S. at 238. Omissions are actionable only where they implicate "the ever-present duty not to mislead." *Basic*, 485 U.S. at 240 n.18; *see Matrixx*, 563 U.S. at 44. Materiality also serves as a barrier to suit—information is material only when there is a "substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of the information made available." *Basic*, 485 U.S. at 231-32 (citation omitted).

The materiality rule is intended to "filter out essentially useless information that a reasonable investor would not consider significant, even as a part of a larger 'mix' of factors to consider in making his investment

decision." *Id.* at 234 (citation omitted). Dumping too much information on investors can create inefficiencies; the excessive information can impede reasoned decisionmaking. *See TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 448-49 (1976). Thus, "if the standard of materiality [for disclosure purposes] is unnecessarily low, not only may the corporation and its management be subjected to liability for insignificant omissions or misstatements, but also management's fear of exposing itself to substantial liability may cause it simply to bury the shareholders in an avalanche of trivial information." *Id.*

This Court's warnings have proved prescient. For decades now, given the low materiality standard, companies' MD&A disclosures have grown "unnecessarily lengthy, difficult to understand and confusing." Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations, 68 Fed. Reg. 75056, 75058-59 (Dec. 29, 2003) ("2003 Guidance"). In one study of 25 large, well-known companies, the number of pages devoted to MD&A disclosures increased 300% between 1972 and 1992—the period during which Item 303 took shape. Ernst & Young, *To the Point: Now Is the Time to Address Disclosure Overload*, at 1 (June 21, 2012).[5] MD&A disclosures went from an average of three pages in 1972 (before Item 303 was promulgated), to seven pages in 1982 (during Item 303's infancy), to 12 pages in 1992, and to 48 pages in 2011. *Id.* at 2. The study predicted that MD&A disclosures would reach an average of 214 pages by 2032 (on top of *320 pages of footnotes*). *Id.*

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[5] *Available at* https://perma.cc/VHM4-FQ5J.

2. Backing up this Court's admonitions, empirical research has shown that investors suffer when they must dig through heaps of trivial information for a valuable nugget here or there. Studies have demonstrated that increasing "regulation-induced disclosures" has "adverse consequences" on the forecasts of professional analysts interpreting these disclosures—specifically, the increased disclosures are "associated with a longer delay, lower accuracy, and higher dispersion" among forecasts. Joost Impink et al., *Regulation-induced Disclosures: Evidence of Information Overload?*, 58 ABACUS 432, 450 (2022).[6] Moreover, the evidence shows that analysts are subject to "information overload"—*i.e.*, a certain level of disclosure is helpful, "but at some point, the information becomes too much resulting in worse decisions." *Id.*; *see* Mary Jo White, Chair, Secs. & Exch. Comm'n, *The Path Forward on Disclosure* (Oct. 15, 2013) (describing "information overload" as "a phenomenon in which ever-increasing amounts of disclosure make it difficult for an investor to wade through the volume of information she receives to ferret out information that is most relevant").[7]

It is a well-known "fallacy" to "think[] that if some information is good, more is better." Frank H. Easterbrook & Daniel R. Fischel, *Mandatory Disclosure and the Protection of Investors*, 70 Va. L. Rev. 669, 696 (1984). "Not surprisingly, investors often voice their disapproval with the current SEC disclosure regime as they encounter needlessly voluminous and complicated SEC filings." U.S. Chamber of Commerce, Center for Capital Markets Competitiveness, *Essential Infor-*

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[6] *Available at* https://doi.org/10.1111/abac.12246.

[7] *Available at* https://www.sec.gov/news/speech/spch101513mjw.

mation: Modernizing Our Corporate Disclosure System 14 (2017);[8] *see* Arthur J. Radin, *Have We Created Financial Statement Disclosure Overload?*, CPA J., Nov. 2007, at 6 (2007) ("[A]s an investor looking at the number of pages that are boilerplate, redundant, immaterial, irrelevant, or overly fact-packed, I immediately suffer from MEGO—my eyes glaze over.").

For precisely this reason, the SEC has repeatedly stressed that Item 303, properly implemented, should not lead to "investors [being] overwhelmed by voluminous disclosure of insignificant and possibly unnecessarily speculative information." 2021 Final Rule, 86 Fed. Reg. at 2094 n.162 (quoting SEC Release No. 33-8182, 2003 WL 175446, at *6 (Jan. 28, 2003)). To combat this trend, the SEC launched its ongoing "Disclosure Effectiveness Initiative"—which includes an attempt at simplifying the disclosures required by Item 303. Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information, 85 Fed. Reg. 12068, 12069 (Feb. 28, 2020).

Even highly sophisticated investors may be misled or thrown off the trail by cluttered company narratives.[9] When the SEC rolled out its Plain English regulation in 1998,[10] for example, Warren Buffett observed:

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[8] *Available at* bit.ly/46jiu4L.

[9] *See, e.g.*, Reuven Lehavy et al., *The Effect of Annual Report Readability on Analyst Following and the Properties of Their Earnings Forecasts*, 86 The Accounting Review 1087, 1112 (2011) ("find[ing] that analyst reports of firms with less readable 10-K reports are more informative to investors, but that the earnings forecasts of such firms have greater analyst dispersion or disagreement, are less accurate, and are associated with greater levels of uncertainty").

[10] *Plain English Disclosure*, 83 Fed. Reg. 6370 (Feb. 6, 1998).

"I've studied the documents that public companies file. Too often, I've been unable to decipher just what is being said or, worse yet, had to conclude that nothing was being said." SEC, A Plain English Handbook 1 (Aug. 1998).[11] But the effect is more dramatic for less sophisticated investors. As then-SEC Chair Levitt explained, "many investors are neither lawyers, accountants, nor investment bankers." *Id.* at 3. Thus, the SEC recently noted that "eliminating information that is not material should benefit all investors" but "retail investors could benefit more as they are less likely to have the time and resources to devote to reviewing and evaluating disclosure." 85 Fed. Reg. at 12098.

3. Opening up Rule 10b-5 liability for failures to disclose under Item 303 encourages just the regime of overdisclosure that this Court disavowed in *Basic*. Materiality is supposed to be a check on the incentive to overdisclose, but Item 303 contains a relatively weak concept of materiality. *See Oran*, 226 F.3d at 288 (explaining that "[b]ecause the materiality standards for Rule 10b-5 and SK-303 differ significantly, the demonstration of a violation of the disclosure requirements of Item 303 does not lead inevitably to the conclusion that such disclosure would be required under Rule 10b-5. *Such a duty to disclose must be separately shown.*" (emphasis added, citation and internal quotation marks omitted)); *accord Carvelli*, 934 F.3d at 1331; *In re NVIDIA Corp. Secs. Litig.*, 768 F.3d at 1055. Allowing alleged violations of Item 303 to be litigated by private plaintiffs, wielding the threat of classwide liability, strongly skews managers' behavior toward the overly cautious, self-preserving end of the spectrum.

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[11] *Available at* https://www.sec.gov/pdf/handbook.pdf.

It comes as no surprise that the risk of litigation is a significant factor driving ballooning disclosures. As former SEC Chair White observed, one important cause of "lengthy and complex disclosure" is "the risk of litigation" which forces companies "to take a defensive posture and disclose more information rather than less." White, *supra.* In fact, a survey of over two hundred companies revealed that "73 percent say their company's disclosures are influenced by concerns over potential future litigation." KPMG, *Disclosure overload and complexity: hidden in plain sight*, at 16, 22 (2011).[12]

4. Nor is there any need for a new *private* cause of action to enforce Item 303. In appropriate cases, the SEC can and does enforce violations of Item 303 as ordinary deficiencies in a company's reporting obligations, without resort to a fraud theory under Rule 10b-5. *See, e.g.*, *In re Kirchner*, Exchange Act Release No. 80947, File No. 3-18024, ¶ 36 (SEC June 15, 2017) ("The MD&A's failure to comply with [Item 303 of] Regulation S-K constitutes a violation under Section 13(a) of the Exchange Act.").[13] But companies know that, in the highly specific context of Item 303 guidance and enforcement, the SEC is attuned to the problem of overdisclosure and is less likely to pursue doubtful violations of Item 303. Private plaintiffs, though, have much different motivations. *Cf. Buckman Co. v. Plaintiffs' Legal Comm.*, 531 U.S. 341, 349-351 (2001) (noting that government agencies can take a "measured re-

[12] *Available at* bit.ly/3Ju5q2K.

[13] *Available at:* https://www.sec.gov/files/litigation/admin/2017/34-80947.pdf.

sponse" to avoid overdisclosure, whereas private litigants lack the incentive to do so).

Moreover, the market already corrects for failures to disclose material and adverse forward-looking information (either because management decided incorrectly or because it deliberately withheld the information); upon discovering such news, "the market will penalize the company later by devaluing its securities (to account for the risk that the company might be holding out on additional bad news not yet known to the public)." Mitu Gulati, *When Corporate Managers Fear a Good Thing Is Coming to an End: The Case of Interim Non-disclosure*, 46 UCLA L. Rev. 675, 690 (1999). Compelling maximum disclosure under Item 303 is not only unnecessary, but harmful to the market's self-regulation. *Id.* ("Because the market itself disciplines firms, through the imposition of nonlegal sanctions such as reputational costs, the creation of legal sanctions is largely unnecessary to force appropriate disclosures and, in fact, is positively detrimental to a well-functioning market . . . .").

C. The Second Circuit's approach undermines Item 303's objective of providing investors access to management's perspective.

The unnecessary overdisclosure produced by the threat of liability does more than just make SEC filings longer. In the case of Item 303 in particular, exacerbating the problem of overdisclosure would run contrary to the provision's purpose: to present management's perspective in candid and clear narrative form.

With Item 303, the SEC "intended to give the investor an opportunity to look at the company *through the eyes of management* by providing both a short and long-

term analysis of the business of the company." 1989 Guidance, 1989 WL 1092885, at *3 (emphasis added). The current text of the regulation makes this explicit: the MD&A "is expected to better allow investors to view the registrant from management's perspective." 17 C.F.R. § 229.303(a); *see id.* ("The discussion and analysis must focus specifically on . . . matters that are reasonably likely *based on management's assessment* to have a material impact on future operations." (emphasis added)). This objective is thwarted if the MD&A is molded into lawyerly, litigation-avoiding work product.

Part of what makes the MD&A useful is that it provides the company's own take on itself, its competitors, and its industry, in a narrative form that is distinct from the quantitative data found in an audited financial statement. *See, e.g.*, 2021 Final Rule, 86 Fed. Reg. at 2106 (MD&A provides "a narrative explanation of the financial statements that enables investors to see a registrant 'through the eyes of management'"). For instance, the introduction should address the risks posed by uncertainties "with which *management* is concerned primarily," 2003 Guidance, 68 Fed. Reg. 75060 (emphasis added), a task that becomes more difficult if the threat of liability leaves management feeling compelled to clutter its narrative with prophylactic discussions of every conceivable uncertainty in the business universe. The MD&A can be useful because it sheds light not just on (*e.g.*) a business uncertainty, but on management's assessment of it and response to it. The latter will get lost in the stack if the disclosure must address every conceivable risk or uncertainty, for fear of liability if one is omitted. That result benefits neither the market nor individual investors.

D. Expanding Rule 10b-5's private right of action will encourage even more costly nuisance suits.

As this Court has frequently observed, "litigation under Rule 10b–5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general." *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 80 (2006) (quoting *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 739 (1975)). In Rule 10b-5 suits, "extensive discovery and the potential for uncertainty and disruption . . . allow plaintiffs with weak claims to extort settlements from innocent companies." *Stoneridge Inv. Partners v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 163 (2008). Leading up to the Private Securities Litigation Reform Act of 1995 (PSLRA), "nuisance filings, targeting of deep-pocket defendants, vexatious discovery requests, and 'manipulation by class action lawyers of the clients whom they purportedly represent' had become rampant." *Merrill Lynch*, 547 U.S. at 81 (quoting H.R. Conf. Rep. No. 104-369, at 31 (1995)).

Congress enacted the PLSRA to disrupt this incentive structure. But "various studies have shown that nuisance settlements still appear to be pervasive in this area." Emily Strauss, *Is Everything Securities Fraud?*, 12 U.C. Irvine L. Rev. 1331, 1350-51 (2022); *see also Stephen J. Choi, Karen K. Nelson & A. C. Pritchard, The Screening Effect of the Private Securities Litigation Reform Act*, 6 J. Empirical Legal Stud. 35, 37 (2009) ("We do not find statistically significant evidence that nuisance suits have been discouraged."). The scope of liability in securities class actions poses a special problem in this regard. "[S]ecurities class actions are not ordinary cases; they are the litigation

equivalent of aircraft carriers." U.S. Chamber Inst. for Legal Reform, *A Rising Threat: The New Class Action Racket That Harms Investors and the Economy* 5 (Oct. 2018).[14] "Claimed damages in securities class actions are often massive" and "the burden of expensive discovery falls overwhelmingly on defendants"— factors that routinely induce many companies to settle even when "the likelihood of success may be low for plaintiffs." Strauss, *supra*, at 1351.

In 2022, federal securities class action settlements totaled $4 billion—at an average of $38 million per case settled—with plaintiffs' attorneys' fees and costs exceeding $1 billion. NERA, *Recent Trends in Securities Class Action Litigation: 2022 Full-Year Review* 13, 20 (Jan. 24, 2023).[15] The cost of securities litigation exacts a toll on the Nation's economic competitiveness. As a bipartisan commission noted in 2007, "U.S. class action litigation is tremendously more costly and voluminous" than in European countries and "[t]he class action vehicle is the primary contributor to the high U.S. D&O insurance costs, which are six times greater when compared to the same costs in Europe." Commission on the Regulation of U.S. Capital Markets in the 21st Century, at 29 (Mar. 2007).[16]

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[14] *Available at*: https://instituteforlegalreform.com/wp-content/uploads/2020/10/A_Rising_Threat_Research_Paper-web_1.pdf.

[15] *Available at*: https://www.nera.com/content/dam/nera/publications/2023/PUB_2022_Full_Year_Trends.pdf.

[16] *Available at*: https://www.centerforcapitalmarkets.com/wp-content/uploads/2014/06/Commission-on-the-regulation-of-us-cap-markets-report-and-recommendations.pdf.

Securities litigation is already too burdensome, and expanding the private right of action under Rule 10b-5 to include omissions of disclosures required by Item 303 would further ratchet up the costs. Such a rule would invite plaintiffs' lawyers to try their luck at manufacturing a fraud claim, perhaps in a forum they perceive to be friendly, leaving corporations sitting ducks for strike suits. Congress has recognized the threat of abuse these lawsuits pose. This Court should not give them more oxygen than they already enjoy.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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