No. 21-594

In The
Supreme Court of the United States

ALPHABET INC., ET AL.,

Petitioners,

v.

STATE OF RHODE ISLAND, OFFICE OF THE RHODE ISLAND TREASURER ON BEHALF OF THE EMPLOYEES' RETIREMENT SYSTEM OF RHODE ISLAND; LEAD PLAINTIFF, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,

Respondent.

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

BRIEF OF *AMICUS CURIAE* WASHINGTON LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES **Page(s)**

STATUTES AND REGULATIONS

LEGISLATIVE MATERIALS

OTHER AUTHORITIES

INTEREST OF *AMICUS CURIAE*

Washington Legal Foundation (WLF) is a nonprofit, public-interest law firm and policy center with supporters nationwide.[1] Founded in 1977, WLF promotes and defends free enterprise, individual rights, limited government, and the rule of law.

To that end, WLF often appears before this and other federal courts in cases raising the proper scope of the federal securities laws. *See, e.g.*, *China Agritech, Inc. v. Resh,* 138 S. Ct. 1800 (2018)*; Cal. Pub. Emps.' Ret. Sys. v. ANZ Sec., Inc.,* 137 S. Ct. 2042 (2017). And WLF's Legal Studies Division has published many articles on the proper construction of the federal securities laws and related topics. *See, e.g.,* Doug Greene, et al.*, Private Securities Litigation: Making the 1995 Reform Act's "Safe Harbor" Safer*, WLF Working Paper (Nov. 16, 2018).

WLF is concerned that the decision below will force companies to include voluminous and stale information in their forward-looking risk disclosures. This makes little sense because risk disclosures are intended to provide investors with a concise description of significant *future* harms that companies face. Requiring companies to provide a compre-hensive log of *past* events among their risk disclosures conflicts with the plain meaning of the word "risk," is inconsistent with the statutory purpose behind requiring companies to identify

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[1] No party's counsel authored any part of this brief, and no person other than WLF or its counsel contributed money to the preparation or submission of this brief. Counsel for all parties received notice of WLF's intention to file this brief at least 10 days prior to the due date, and have consented to this filing.

significant "risk factors," will result in an uptick in meritless litigation against companies for alleged failures to disclose past events, and ultimately will burden investors who must parse and evaluate reams of historical data wholly unrelated to *future* risks the companies may face.

REASONS FOR GRANTING THE PETITION

Petitioners correctly argue that a company's risk disclosures cover *future* potential threats or harms and need not disclose whether that particular risk materialized in the past.

Under the Ninth Circuit's ruling, however, any time a company discloses a "risk" that could materialize in the future, it also must state whether that risk previously has manifested—even if the incident in question was fully resolved before the company's filing and caused no harm to the company's bottom line. Because the Ninth Circuit's ruling effectively will force companies to disclose extensive, immaterial information about past incidents, it will likely confuse investors who must navigate a company's SEC filings to find information relevant to their investment decisions.

Moreover, as in this case, companies will be subject to potentially frivolous securities litigation based on forward-looking statements, which is exactly the outcome that Congress sought to avoid when it passed the Private Securities Litigation Reform Act (PSLRA). That is why courts consistently have held that risk disclosures are both forward-looking and immaterial as a matter of law.

Given the Ninth Circuit's deepening of an already-existing circuit split on this issue, this case is an appropriate vehicle for the Court to address these important issues, which have significant public-policy ramifications.

ARGUMENT

I. THE PETITION SHOULD BE GRANTED BECAUSE THE NINTH CIRCUIT'S DECISION IS WRONG.

Under the federal securities laws and corresponding SEC rules, a company is required to disclose certain past events that have occurred since the company's last securities filing. *See* 17 C.F.R. § 229.101 (Description of Business); 17 C.F.R. § 229.102 (Description of Property); 17 C.F.R. § 229.103 (Legal Proceedings). A company also is prohibited from omitting "a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading." 17 C.F.R. § 240.10b-5(b).

Beyond these disclosure requirements, a company filing a Form 10-K also must include a "risk factor section," in which the company provides a "concise" "discussion of the most significant factors that make the offering speculative or risky." 17 C.F.R. § 229.503(c) (2017).[2] These "risk factor" disclosures need only alert investors to the possibility of *future* harms. *See Bondali v. Yum! Brands, Inc.*, 620 F. App'x 483, 491 (6th Cir. 2015); *In re ChannelAdvisor Corp. Sec. Litig.*, No. 5:15-CV-

[2] The filings at issue here occurred in 2017 and 2018. A substantially similar provision is now codified at 17 C.F.R. § 229.105 ("Where appropriate, provide under the caption 'Risk Factors' a discussion of the material factors that make an investment in the registrant or offering speculative or risky.").

00307-F, 2016 WL 1381772, at *5 (E.D.N.C. Apr. 6, 2016), *aff'd*, *Dice v. Channeladvisor Corp.*, 671 F. App'x 111 (4th Cir. 2016) (per curiam).

The Ninth Circuit's ruling, however, goes much further by creating an affirmative obligation to disclose all materialized risks in connection with a company's discussion of future risks. *See* Pet. App. 25a (Alphabet should have disclosed among its "risk factors" that it "knew that those risks had materialized").

A. The Ninth Circuit Fails to Explain How a Risk Disclosure Alone Creates a Misleading Impression.

According to the Ninth Circuit, "[r]isk disclosures that 'speak entirely of as-yet-unrealized risks and contingencies' and do not 'alert the reader that some of these risks may already have come to fruition' *can mislead reasonable investors*." Pet. App. 24a (quoting *Berson v. Applied Signal Tech., Inc.*, 527 F.3d 982, 985–87 (9th Cir. 2008) (alterations omitted) (emphasis added)). The problem is that the Ninth Circuit never explains *how* or *why* reasonable investors would be misled. After all, a statement is misleading only if it creates a false impression about the true state of affairs in the minds of investors. *See, e.g.*, *Emps.' Ret. Sys. of Rhode Island v. Williams Cos., Inc.*, 889 F.3d 1153, 1164 (10th Cir. 2018) ("To be actionable under the securities laws, an omission must be misleading; in other words, it must affirmatively create an impression of a state of affairs that differs in a material way from the one that actually exists." (citation omitted)); *Retail Wholesale & Dep't Store Union Loc. 338 Ret. Fund v. Hewlett-Packard Co.*, 845 F.3d 1268, 1275 (9th Cir.

2017) ("[T]here was no duty to disclose because [the company's] failure[] to speak did not affirmatively create an impression of a state of affairs that differs in a material way from the one that actually exists." (internal quotation marks omitted)); *Indiana Elec. Workers' Pension Tr. Fund IBEW v. Shaw Grp., Inc.*, 537 F.3d 527, 541 (5th Cir. 2008) (an omission is misleading only if it "affirmatively create[s] an impression of a state of affairs that differs in a material way from the one that actually exists").

Thus, a risk disclosure can be misleading only if it creates a false impression. Although the Ninth Circuit never says so, the court implies that a risk disclosure is misleading if the risk has already materialized because the risk disclosure creates the false impression that no risks have yet materialized. But the Ninth Circuit does not even attempt to explain why or how a risk disclosure—which inherently concerns future events—could create *any* misimpression in the minds of reasonable investors about the present or the past, much less a misleading impression about whether certain events that *could occur* in the future have *already occurred*.

Rather than clarify how a risk disclosure "can mislead reasonable investors," the Ninth Circuit simply invokes the holdings of other Ninth Circuit cases. But none of the cases cited (least of all *Berson*, upon which the court most heavily relies) provide any support for the notion that a risk disclosure alone can mislead investors about the current or past state of affairs of the company on the matter at issue. Indeed, the *Berson* decision makes clear that risk disclosures alone are *not* misleading; rather, what can be potentially misleading is verbiage that accompanies risk disclosures—but is separate and distinct from the actual warning of a possible future adverse event. *Berson*, 527 F.3d at 986–87.

In *Berson*, the Ninth Circuit considered whether defendants who "touted the company's backlog," *i.e.*, the dollar value of the work the company had contracted to do but had not yet performed, had misled investors. *Berson*, 527 F.3d at 984–85. Although the defendants warned that the backlog figures could change, they also described the company's backlog as "anticipated revenues" and stated that the "backlog figures [we]re firm." *Id.* at 986. Defendants did not disclose, however, that the company's backlog figures included contracts subject to "stop-work orders" that were "substantially delayed and at serious risk of being cancelled altogether." *Id.*

The Ninth Circuit held that defendants' statements were actionable not because of anything inherently misleading in a company's warnings about future events, but because "once defendants chose to tout the company's backlog, they were bound to do so in a manner that wouldn't mislead investors as to what that backlog consisted of." *Id.* at 987. Contrary to the ruling below, nothing in *Berson* suggests that a risk disclosure can itself give a false impression about past or current events.[3]

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[3] The ruling below also incorrectly cites *Siracusano v. Matrixx Initiatives, Inc.*, 585 F.3d 1167 (9th Cir. 2009). In *Matrixx*, the court discussed a forward-looking litigation-risk disclosure that omitted the existence of a pending lawsuit that had only commenced shortly before the risk disclosure was issued—but for which the company would be actively defending against, incurring litigation expense, and having exposure to a

Moreover, according to the Ninth Circuit, "[r]isk disclosures that 'speak entirely of *as-yet-unrealized* risks and contingencies' and do not 'alert the reader that some of these risks may already have come to fruition' can mislead reasonable investors." Pet. App. 24a (alterations omitted) (emphasis added). Yet the Ninth Circuit was putting its thumb on the scales by framing the issue as whether disclosures "speak *entirely* of *as-yet-unrealized* risks." *Id.* (alterations omitted) (emphasis added). The court's framing invites this Court to clarify whether a risk disclosure reasonably can be construed as informing investors that the disclosed "risks" are "as-yet unrealized." As *Berson* highlights, when a disclosure appears to communicate that a risk is "as-yet unrealized," it is not the disclosure of the risk itself that creates that impression. Instead, the impression is created, if at all, by surrounding language.

The Ninth Circuit simply does not and cannot meaningfully articulate why and how, in the absence of such potentially misleading, accompanying verbiage, a risk disclosure creates a false impression in the minds of reasonable investors about past or current events.

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potential judgment *well into the future*. *Id.* at 1181. Given the inherently future-oriented nature of the litigation, *Matrixx* had no need to explain how forward-looking statements about future risks could give investors a false impression about a company's past or current state of affairs (apart from the ongoing litigation). *Id.* at 1180–83.

B. The Ninth Circuit's Ruling Ignores the Plain Meaning of "Risk Disclosures."

The plain meaning of "risk" belies the notion that a forward-looking risk disclosure could mislead investors about the past or present. Risk is commonly understood as a forward-looking concept—one that concerns the "*possibility* of loss, injury, disadvantage, or destruction." *Bondali*, 620 F. App'x at 491 (quoting *Risk*, Webster's Third New International Dictionary 1961 (1986) (emphasis in *Bondali*)). "Risk disclosures" therefore serve a singular purpose: to identify and disclose to investors issues that could affect the company in the future. *Id.* Because a risk disclosure concerns *prospective* harms, it cannot mislead a reasonable investor into thinking the matter at issue has already manifested itself.

C. The Ninth Circuit's Ruling Is Particularly Flawed Because the Past Incidents at Issue Were Fully Remediated and Caused No Harm.

Here, the Ninth Circuit's holding—that a company has an affirmative obligation to disclose materialized risks in connection with its discussion of future risks—is particularly unsound. The issue that Alphabet omitted from its forward-looking risk disclosures had been remediated by the time of its securities filing. *See* Pet. App. 25a ("Google had already remediated the software glitch in Google+ before it made the 10-Q statements"). As the district court rightly held, "[t]here is no support for the position that a remediated technological problem which is no longer extant must be disclosed in the company's future-looking disclosures." Pet. App. 44a.

Moreover, the Ninth Circuit's ruling suggests (in stark contrast to this Court's precedent) that companies cannot rely on a traditional materiality analysis in assessing whether a past event must be disclosed. Here, the Ninth Circuit held that, because Alphabet's "business model is based on trust," even fully remediated software bugs that never harmed consumers would still need to be disclosed to investors. *See* Pet. App. 26a. As petitioners note, the implication for technology companies resolving tens or hundreds of thousands of software bugs on a regular basis is that they must either disclose demonstrably immaterial past events or risk exposure under federal securities law.

II. THE PETITION SHOULD BE GRANTED TO RESOLVE THE CIRCUIT SPLIT AMONG SIX COURTS OF APPEALS.

This Court's review also would bring clarity to muddled jurisprudence about "risk disclosures." With the Ninth Circuit's ruling, there is now a well-defined circuit split, with lower courts lacking guidance as to whether forward-looking risk disclosures are actionable. Intervention by this Court is needed.

Whether a company must disclose past events among its risk disclosures should not depend on where the company is located or in which court a securities litigation case is brought. Yet this is precisely the current situation.

Four Courts of Appeals (as well as the Southern District of New York) now hold that a company must disclose events that have previously occurred alongside its "risk disclosures" or face substantial exposure from securities lawsuits. *See Karth v. Keryx Biopharmaceuticals, Inc.*, 6 F.4th 123, 138 (1st Cir. 2021) ("[a] company must also disclose a relevant risk if that risk had already begun to materialize"); *Williams v. Globus Med., Inc.*, 869 F.3d 235, 242 (3d Cir. 2017) ("a company may be liable under Section 10b for misleading investors when it describes as hypothetical a risk that has already come to fruition"); *In re Harman Int'l Indus., Inc. Sec. Litig.*, 791 F.3d 90, 104 (D.C. Cir. 2015) (company's risk disclosure failed to "warn of actual obsolescence that had already manifested itself"); *In re Facebook, Inc. IPO Sec. & Derivative Litig.*, 986 F. Supp. 2d 487, 516 (S.D.N.Y. 2013) ("a company's purported risk disclosures are misleading where the company warns only that a risk may impact its business when that risk has already materialized").

Meanwhile, the Fourth and Sixth Circuits (as well as a district court in the Tenth Circuit) correctly recognize that a company need not recount past events in its forward-looking risk disclosures. *See Bondali*, 620 F. App'x at 491; *Dice*, 671 F. App'x at 112; *Indiana Pub. Ret. Sys. v. Pluralsight, Inc.,* No. 119CV00128JNPDBP, 2021 WL 1222290, at *14 (D. Utah Mar. 31, 2021) ("several courts have found that risk disclosures are not independently actionable under Section 10(b) and Rule 10b-5") (collecting cases). As the Sixth Circuit has explained, "cautionary statements are 'not actionable to the extent plaintiffs contend defendants should have disclosed risk factors 'are' affecting financial results rather than 'may' affect financial results.'" *Bondali*, 620 F. App'x at 491 (citation omitted). This is because the purpose of risk disclosures is to "warn an investor of what harms may come to their investment. They are not meant to educate investors on what harms are currently affecting the company." *Id.*

Indeed, the Fourth and Sixth Circuits offer an additional reason why forward-looking risk disclosures are not actionable under the federal securities laws: statements about future risks are immaterial as a matter of law. *See Bondali*, 620 F. App'x at 491; *ChannelAdvisor*, 2016 WL 1381772, at *5.

In *Bondali*, the Sixth Circuit explained that "a reasonable investor would be unlikely to infer *anything* regarding the current state of a corporation's compliance, safety, or other operations from a statement intended to educate the investor on future harms." *Bondali*, 620 F. App'x at 491. In *ChannelAdvisor*, the same logic prevailed and the district court held that it was "unlikely that a reasonable investor would, from th[e] cautionary language [contained in a risk disclosure], infer anything about" a company's current state of affairs. *ChannelAdvisor*, 2016 WL 1381772, at *6. The Fourth Circuit agreed, affirming the district court. *Dice*, 671 F. App'x at 112.

Other courts, however, have either explicitly or implicitly held that risk disclosure statements can be material. *See* Pet. App. 23a (discussing "the materiality of the misleading omission" in a risk disclosure); *Howard v. Arconic Inc.*, No. 2:17-CV-1057, 2021 WL 2561895, at *6 (W.D. Pa. June 23, 2021) ("the risk disclosures were materially false or misleading").

The wide array of approaches demonstrates that courts require additional guidance as to whether risk disclosures are actionable under the federal securities laws and, if so, why that is the case.

III. THE PETITION SHOULD BE GRANTED BECAUSE CLARIFICATION OF RISK DISCLOSURE REQUIREMENTS WILL HAVE IMPORTANT PUBLIC POLICY BENEFITS.

Granting review and clarifying that only *future* risks need to be disclosed as part of a company's "risk disclosures" will have important public policy benefits far beyond this case.

A. The Ninth Circuit's Ruling Will Have a Negative Impact on Public Companies and Investors.

If left uncorrected, the Ninth Circuit's rule will become the de facto standard nationwide for lawsuits based on a company's risk disclosures. Companies will face substantial liability from securities lawsuits if they fail to disclose past events in their forward-looking risk disclosures, and will be forced to disclose massive amounts of information about past incidents that would otherwise be immaterial to investors. For technology companies like Alphabet, this means disclosing every software bug or data privacy breach they have encountered.

Yet the decision's scope is even greater than that. For example, manufacturers across all industries likely would need to disclose every quality control or supply chain challenge faced (no matter how trivial or how easily remediated). Disclosures for publicly traded companies would be onerous, as they would have to make radical changes to the way they prepare their public statements.

The Ninth Circuit's risk-disclosure rule also would harm investors. To fend off securities litigation, companies will err on the side of providing "an overabundance of information," which this Court has expressly rejected as inimical to the investing public. *See Basic Inc. v. Levinson*, 485 U.S. 224, 231 (1988). Indeed, as this Court has made plain, "bury[ing] the shareholders in an avalanche of trivial information" is "a result that is hardly conducive to informed decisionmaking." *Id.* (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 448–49 (1976)).

In contrast, the approach adopted by the Fourth and Sixth Circuits does not pose any appreciable burden on investors, who maintain the ability under the federal securities laws to sue if a company has made statements of *current or historical fact* that are rendered misleading by the failure to disclose that a risk has already come to fruition. For example, investors often file securities lawsuits based on statements about a company's *current or historical* financial performance, where there are allegations that those statements were made when the company was aware that risks calling this financial performance into question had materialized. *See, e.g.*, *In re Vivendi, S.A. Sec. Litig.*, 838 F.3d 223, 251 (2d Cir. 2016) ("[A] reasonable investor could find [the company's] statements about high EBITDA growth misleading for [not disclosing the company's] liquidity risk."); *In re Cognizant Tech. Sols. Corp. Sec. Litig.*, No. 216CV06509WHWCLW, 2018 WL 3772675, at *20 (D.N.J. Aug. 8, 2018) ("At the time [the company] was making statements highlighting its anticorruption training, it was allegedly engaged in a bribery scheme involving members of senior management. These statements are misleading for this reason alone."); *In re Petrobras Sec. Litig.,* 116 F. Supp. 3d 368, 380–81 (S.D.N.Y. 2015) ("[A]t the time the Company's management was professing its opinion that the company's internal controls were effective, that same management was well aware of the extensive corruption in the Company's procurement activities"). In other words, investors will continue to have avenues to seek redress when a company fails to disclose the fruition of a material risk that renders statements of current or historical fact misleading.

B. The Ninth Circuit's Ruling Threatens to Reopen the Floodgates That the PSLRA Closed.

The Ninth Circuit's decision also threatens to usher in a new wave of lawsuits based on companies' failure to disclose past incidents alongside risk disclosures—an outcome that would run contrary to Congress's efforts to limit the proliferation of meritless securities litigation.

One of the PSLRA's primary goals was "to curb frivolous, lawyer-driven litigation." *Tellabs, Inc. v. Makor Issues & Rts., Ltd.*, 551 U.S. 308, 322 (2007). Before the enactment of the PSLRA, companies risked "open ended liability" and "baseless and extortionate securities lawsuits" when they disseminated relevant information to the market. H.R. Conf. Rep. 104-369, 32, 1995 U.S.C.C.A.N. 730, 731. Recognizing that forward-looking statements often will turn out to be wrong, Congress included a "safe harbor" in the PSLRA barring claims based on these statements to achieve its goal of limiting abusive securities filings. Specifically, the safe harbor incentivized companies to disclose potentially valuable information about a company's future prospects, while offering the companies protection from meritless lawsuits. *See* H.R. Conf. Rep. 104-369, 43, 1995 U.S.C.C.A.N. 730, 742 (explaining that the statutory safe harbor was designed to reduce "[t]he muzzling effect of abusive securities litigation"). The PSLRA required that a company seeking to invoke the safe harbor provide "meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement." *See* 15 U.S.C. § 78u–5. In other words, Congress offered companies a new layer of protection from frivolous securities lawsuits if they included "meaningful cautionary" risk disclosures in their securities filings.

The Ninth Circuit, however, has turned this regulatory regime on its head: the very risk disclosures that were originally intended to protect companies from meritless litigation have now become a way for the plaintiffs' bar to pry open the floodgates that the PSLRA was designed to shut. Unless this Court intervenes, plaintiffs' firms will continue to bring securities suits based on risk disclosures even if the defendant has not actually made any statement of historic or current fact on the topic at issue. That is not what Congress intended in the PSLRA when it encouraged companies to provide meaningful cautionary statements and the Court once again should step in to prune the ever-growing judicial oak of federal securities fraud liability. *See*

Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 276 (2010) (Section 10(b) "area of law is replete with judge-made rules, which give concrete meaning to Congress' general commands . . . we deal with a judicial oak which has grown from little more than a legislative acorn.") (quotation omitted).

Left unaddressed, the decision below will set the stage for an unworkable disclosure regime, one that forces the companies to lard their risk disclosures with extraneous details of past incidents rather than focusing on the most important future risks facing the company.

CONCLUSION

This Court should grant the petition, resolve the circuit split, and clarify whether a company must disclose all past incidents alongside the risk disclosures in their SEC filings.

Respectfully submitted,

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