Litigation Alert: The Supreme Court's *Omnicare* Decision Clarifies When an Opinion Stated in a Registration Statement Can Give Rise to Section 11 Liability

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Overview

On March 24, 2015, the Supreme Court issued its opinion in *Omnicare, Inc. v. Laborers District Council Construction Industry Pension Fund,* a highly anticipated case concerning the circumstances under which allegedly false or misleading statements of opinion can give rise to liability under Section 11 of the Securities Act of 1933, 15 U.S.C. § 77k ("Section 11"). Generally, Section 11 prohibits issuers from making false or misleading statements or omissions of material fact in a registration statement in connection with a public securities offering. The Court's *Omnicare* decision clarifies that an issuer's statements of opinion cannot form the basis for Section 11 liability solely by virtue of the fact that they later prove to be incorrect. Such statements of opinion may only give rise to Section 11 liability if: (1) the issuer did not actually hold the opinion in question at the time of the registration statement, or (2) the statement of opinion was rendered misleading by a failure to disclose material facts about the basis for that opinion.

Background

The *Omnicare* case arose out of a December 2005 public stock offering by pharmaceutical services provider Omnicare, Inc. The registration statement for the offering included two statements of opinion concerning the company's compliance with applicable law:

- *"We believe our contract arrangements with other healthcare providers, our pharmaceutical suppliers and our pharmacy practices are in compliance with applicable federal and state laws"; and*
- *"We believe that our contracts with pharmaceutical manufacturers are legally and economically valid arrangements that bring value to the healthcare system and the patients that we serve."*

The plaintiffs purchased Omnicare stock in the December 2005 offering and later filed suit under Section 11 against the company and several individual defendants in the U.S. District Court for the Eastern District of Kentucky. The plaintiffs alleged, among other things, that the aforementioned statements of opinion were false and misleading because the company's contract arrangements did not, in fact, comply with applicable law, citing various lawsuits that were later filed by the federal government assailing the validity of the company's agreements with drug manufacturers.

The district court granted the defendants' motion to dismiss the plaintiffs' Section 11 claim. The district court ruled that a statement of opinion may be actionable under Section 11 only if the speaker believes that the statement is untrue at the time it is made. The court found therefore that plaintiffs' complaint failed to state a claim because it did not allege that defendants believed that the company's contractual arrangements did not comply with applicable law at the time of the registration statement.

On appeal, the U.S. Court of Appeals for the Sixth Circuit reversed. Contrary to the district court, the Sixth Circuit held that a statement of opinion may be actionable under Section 11 if the plaintiff sufficiently pleads that it is "objectively false," and that, because Section 11 is a strict liability statute, plaintiffs are not required to plead or prove that the defendant knew or believed the statement was false in order to establish liability.

Omnicare and the other defendants then sought review in the Supreme Court, and the Court granted *certiorari*.

The Court's Opinion

In an opinion that provides a detailed roadmap governing the application of Section 11 to statements of opinion, the Supreme Court reversed the Sixth Circuit decision and remanded the case for further proceedings.

Writing for seven justices (Justice Scalia and Justice Thomas each issued a separate concurring opinion), Justice Kagan first emphasized that Section 11 contains two relevant potential bases for liability — it creates liability for both the making of "an untrue statement of material fact," as well as the omission of "a material fact … necessary to make the statements therein not misleading" — and that each those bases applies differently to statements of opinion. With respect to the first — liability for false statements — the Court noted that Section 11's "untrue statements" clause reaches only statements of "material fact." The Court explained that while some statements of opinion may contain embedded statements of fact, for statements of "pure opinion" like Omnicare's opinions concerning its compliance with applicable law, the only factual assertion implicit in such statements is the speaker's assertion that he or she actually holds the stated opinion. Accordingly, the Court found, such statements of pure opinion can be actionable under Section 11 as "untrue statements of material fact" only if the speaker did not honestly hold the belief in question. "In other words," the Court stated, Section 11's "untrue statements" clause "is not … an invitation to Monday morning quarterback an issuer's opinions."

The Court next considered the "omissions" clause of Section 11 and the more complex question of "when, if ever, the omission of a fact can make a statement of opinion like Omnicare's, even if literally accurate, misleading to an ordinary investor." The Court first noted that the mere fact that a statement of opinion proves to be incorrect cannot itself render the statement "misleading" to a reasonable investor for purposes of Section 11. The Court went on to conclude, however, that even honestly-held statements of opinion are not entirely immune from liability under Section 11's "omissions" clause, because a reasonable investor might understand such statements to implicitly convey factual information "about the speaker's basis for holding that view" that, if untrue, could render the opinion misleading. Accordingly, the Court explained, "if a registration statement omits material facts about the issuer's inquiry into or knowledge concerning a statement of opinion, and if those facts conflict with what a reasonable investor would take from the statement itself, then [Section] 11's omissions clause creates liability."

Because the lower courts had not considered the plaintiffs' Section 11 claim in light of the correct legal standards, the Court remanded the case for further proceedings without stating a view as to the sufficiency of the plaintiffs' complaint.

Implications of the Court's Decision for Section 11 Actions

There are a variety of important implications that the *Omnicare* decision will have for issuers and their counsel in drafting registration statements and in litigating any Section 11 actions arising from them. Most notably:

- The Court's ruling forecloses the possibility that sincere statements of opinion made in a registration statement can be rendered actionable solely because they turn out to be mistaken with the benefit of hindsight. The Court recognized that reasonable investors should understand and appreciate the distinction between statements couched as opinion or belief, and those made as statements of fact, and that Section 11's requirements should not dissuade issuers from providing opinions or beliefs in registration statements that could prove useful to potential investors.
- The Court took pains to emphasize, however, that this does not give issuers "*carte blanche* to assert opinions in registration statements free from worry about [Section] 11." To the extent that there are material facts relevant to how the issuer developed the stated opinion, the issuer should strongly consider disclosing those facts. In short, "to avoid exposure for omissions under [Section] 11, an issuer need only divulge an opinion's basis, or else make clear the real tentativeness of its belief."
- The Court also addressed what facts plaintiffs must plead when they base their Section 11 claims on allegations that statements of opinion omitted material facts: "The investor must identify particular (and material) facts going to the basis for the issuer's opinion — facts about the inquiry the issuer did or did not conduct or the knowledge

it did or did not have — whose omission makes the statement at issue misleading to a reasonable person reading the statement fairly and in context. … That is no small task for an investor." Notably, Section 11 cases are typically subject to a stay of discovery during the pendency of a motion to dismiss under the Private Securities Litigation Reform Act of 1995 (PSLRA), and thus plaintiffs will likely have to plead such facts without the benefit of any discovery.

- It bears noting, however, that plaintiffs are increasingly filing their Section 11 cases in state court — as there is a split among district courts as to whether Section 11 cases are removable to federal court — and in so doing are arguing that the PSLRA stay of discovery does not apply. The Omnicare decision may create further incentive for plaintiffs to file in state court to attempt to obtain discovery in order to properly plead a Section 11 claim under the Omnicare standard.
- The Court also affirmed the longstanding disclosure principle that statements made in a registration statement — whether opinion or fact — must be viewed in context, *i.e.,* "in light of all its surrounding text, including hedges, disclaimers, and apparently conflicting information." This further reinforces the importance of ensuring that a registration statement include fulsome disclosures and carefully considered and comprehensive risk factors to guard against Section 11 liability.

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