No. 23-980

In The Supreme Court of the United States

FACEBOOK, INC., ET AL.,

Petitioners,

v.

AMALGAMATED BANK, ET AL.,

Respondents.

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

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

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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. WLF often appears as an amicus before this Court in disputes over the proper scope of the federal securities laws. *See, e.g.*, *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, 601 U.S. 257 (2024); *Goldman Sachs Grp., Inc. v. Ark. Tchr. Ret. Sys.*, 594 U.S. 113 (2021).

WLF believes that the Ninth Circuit's decision creates significant confusion around the scope of SEC-required risk disclosures under Item 105 (17 C.F.R. § 229.105). If left intact, companies will be forced to snub recent SEC guidance discouraging lengthy, unfocused risk disclosures and instead include reams of historical data wholly unrelated to risks of possible future events the companies may face, or otherwise find themselves exposed to meritless litigation for failure to disclose past instances when the risk arose. This outcome unfairly burdens investors, who must parse through lengthy disclosures included to avoid litigation, rather than focusing on the prospective risks that management believes could have a material impact on the business.

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[1] No party's counsel authored any part of this brief. No person other than Washington Legal Foundation or its counsel contributed any money to the preparation or submission of this brief.

SUMMARY OF ARGUMENT

Item 105 calls for the *prospective* disclosure of risks that could materially impact the operation of a company's business in the *future*. Although Item 105 risk disclosures are inherently forward-looking, the decision below mandates backward-looking disclosures about a stated risk through a misguided application of Rule 10b–5.

The Ninth Circuit's decision is wrong because the omission of backward-looking information does not render a forward-looking risk disclosure materially misleading. Risk disclosures "are not meant to educate investors on what harms are currently affecting the company," so "'a reasonable investor would be unlikely to infer anything'" from a risk disclosure about the past or present materialization of that risk. *In re Marriott Int'l*, 31 F.4th 898, 904 n.2 (4th Cir. 2022) (citation omitted). In other words, a reasonable investor takes a risk disclosure at face value and does not discount the prospective risk as less meaningful, "purely hypothetical," or "merely conjectural," as the Ninth Circuit concluded. Pet. App. 24a.

The decision below also failed to consider the reason "cautionary statements of potential risk have only rarely been found to be actionable by themselves." *In re Marriott Int'l, Inc., Customer Data Sec. Breach Litig.*, 543 F. Supp. 3d 96, 128 (D. Md. 2021) (citation omitted), *aff'd*, 31 F.4th 898 (4th Cir. 2022). Two important legal protections (the "bespeaks caution" doctrine and the PSLRA safe harbor) insulate forward-looking statements – including risk disclosures – from Rule 10b–5 liability. The Ninth Circuit's ruling turns these protections on their head.

Rather than treating risk disclosures as non-actionable forward-looking statements, the Ninth Circuit converted them by judicial fiat into actionable statements of current or historical fact.

Affirming would invite meritless securities litigation predicated on "fraud-by-hindsight." Caught between the SEC's risk disclosure requirement and a heightened litigation risk, companies will feel compelled to over-disclose. Instead of a concise and informative discussion of prospective risk that educates investors on potential harms, investors will be treated to retrospective risk disclosures with loads of historical data of no material relevance, designed to do nothing more than ward off litigation. This result increases compliance costs, complicates an already complex disclosure regime, and ultimately harms investors who look to SEC filings to find information relevant to their investment decisions.

The Court should reverse and allow forward-looking risk disclosures to do the job they are meant to do.

ARGUMENT

I. The Ninth Circuit's decision wrongly imposes Rule 10b–5 liability on forward-looking risk disclosures.

Many SEC disclosure regulations require that a company provide retrospective disclosure about what has occurred since the company's last securities filing. *See, e.g.*, 17 C.F.R. Part 210 (describing disclosure requirements relating to periodic financial statements). Unlike these other SEC disclosure regulations, however, Item 105 of Regulation S-K requires that a company provide in its periodic filings

a concise, prospective discussion of "material factors that make an investment in the registrant or offering speculative or risky." 17 C.F.R. § 229.105.[2] These disclosures are designed to alert investors to "what harms *may come* to their investment." *See Bondali v. Yum! Brands, Inc.*, 620 F. App'x 483, 491 (6th Cir. 2015) (emphasis in original).

Under Rule 10b–5, the anti-fraud rule promulgated under Section 10(b) of the Securities Exchange Act of 1934, a company cannot make affirmative declarations that omit "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). A statement is misleading, however, only if it creates a false impression about the true situation in the minds of investors. *See, e.g.*, *Emps.' Ret. Sys. of R.I. v. Williams Cos., Inc.*, 889 F.3d 1153, 1164 (10th Cir. 2018) ("To be actionable … an omission … must affirmatively create an impression of a state of affairs that differs in a material way from the one that actually exists.") (citation omitted).

Rule 10b–5 does not "create an affirmative duty to disclose any and all material information." *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 44 (2011). Additional disclosure is necessary only if a statement becomes materially misleading without it. *See Macquarie*, 601 U.S. at 263 (Rule 10b–5 "prohibits omitting a material fact necessary 'to make the statements made ... not misleading.'"). And whether a

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[2] The filing at issue here occurred in 2017. The "risk factors" disclosure provision was then codified at 17 C.F.R. § 229.503(c) (2017).

statement creates a material misimpression is considered from the viewpoint of a "reasonable investor." *Matrixx*, 564 U.S. at 38 (citation omitted).

Here, the Ninth Circuit held that an Item 105 risk disclosure becomes "a materially misleading statement" under Rule 10b–5 if it fails to disclose instances when a stated risk has "'come to fruition.'" Pet. App. 25a (quoting *Berson v. Applied Signal Tech.*, 527 F.3d 982, 987 (9th Cir. 2008)). The Ninth Circuit even said that a risk disclosure that omits such information is subject to Rule 10b–5 liability, even if there is no known "ensuing harm" from materialization of the risk. *Id.*

The Ninth Circuit's decision wrongly imposes Rule 10–5 liability on prospective risk disclosures for backward-looking omissions and flouts statutory and common law protections normally afforded forward-looking cautionary statements. The Court should reverse this judicial expansion of Item 105 and Rule 10b–5 liability.

A. A forward-looking risk disclosure is not rendered materially misleading by the omission of a backward-looking disclosure of realized risks.

The determination of whether a statement is materially misleading to a reasonable investor "always depends on context." *Omnicare, Inc. v. Laborers Dist. Council Const. Indus. Pension Fund*, 575 U.S. 175, 176 (2015). A reasonable investor reads a risk disclosure in the context of what Item 105 asks a company to disclose. *See id.*

The text of Item 105 calls for disclosure of "risk factors," which are defined as "material factors that

make an investment … speculative or risky." 17 C.F.R. § 229.105. "Risk" is a forward-looking concept: one that concerns the "*possibility* of loss, injury, disadvantage, or destruction." *Bondali*, 620 F. App'x at 491 (quoting Webster's Third New International Dictionary 1961 (1986)) (emphasis in original). It would conflict with the ordinary meaning of "risk" to speak of a risk that something has occurred *in the past*. "Risk disclosures" therefore serve a singular purpose: to identify and disclose to investors issues that could affect the company *in the future*. *See id.*

Because risk disclosures "are not meant to educate investors on what harms are currently affecting the company," the law assumes "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." *Marriott*, 31 F.4th at 902 n.2 (quoting *Bondali*, 620 F. App'x at 491). For that reason, courts have held risk disclosures are not materially misleading and cannot form the basis for a securities fraud claim for failure to disclose information about the past or present, absent some other disclosure that brings the past or present into play.[3]

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[3] *See, e.g.*, *Marriott*, 31 F.4th at 902 n.2 (noting that risk disclosures generally are not actionable because they "lack materiality" with respect to an investor's understanding of the current state of the company); *Kolominsky v. Root, Inc.*, 100 F.4th 675, 689 (6th Cir. 2024) (dismissing claim that risk disclosure should have said "marketing strategy was affecting" the business rather than "it could"); *Heavy & Gen. Laborers' Local 472 & 172 Pension & Annuity Funds v. Fifth Third Bancorp*, 2022 WL 1642221, at *17 (N.D. Ill. May 24, 2022) ("No

The Ninth Circuit, however, held that a risk disclosure is materially misleading insofar as "it 'speaks entirely of as-yet-unrealized risks' when the risks have 'already come to fruition.'" Pet. App. 25a (quoting *Berson v. Applied Signal Tech.*, 527 F.3d 982, 987 (9th Cir. 2008)). But the Ninth Circuit put a heavy thumb on the scale by framing the issue in terms of risk disclosures "speak[ing] *entirely of as-yet-unrealized* risks." *Id.* (emphasis added). Nothing in Item 105 would lead a reasonable investor to conclude that a company has not previously encountered a risk unless the risk disclosure says so. Nor has the SEC ever issued guidance suggesting that companies should provide backward-looking risk disclosures. It might make sense for a reasonable investor to assume that the lack of retrospective disclosure means something did not happen where an SEC disclosure requirement specifically contemplates *both* explicit retrospective *and* prospective disclosure. *See, e.g.*, 17 C.F.R. § 229.106(b)(2) ("Describe whether any risks from cybersecurity threats, including as a result of

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reasonable investor would conclude that, in making this disclosure, Fifth Third promised that no employee misconduct had ever occurred."); *Chapman v. Mueller Water Prods., Inc.*, 466 F. Supp. 3d 382, 405 (S.D.N.Y. 2020) (risk disclosure that "new products may have quality or other defects" could not "be understood as a guarantee" that previously shipped products did not have defects); *In re ChannelAdvisor Corp. Sec. Litig.*, 2016 WL 1381772, at *6 (E.D.N.C. Apr. 6, 2016) (finding risk disclosures were not misleading because "it is unlikely that a reasonable investor would, from that cautionary language, infer anything about [defendant's] current contracts"), *aff'd*, 671 F. App'x 111 (4th Cir. 2016); *In re Noah Educ. Holdings, Ltd. Sec. Litig.*, 2010 WL 1372709, at *7 (S.D.N.Y. Mar. 31, 2010) (risk factors could not be read "to imply that … cost of raw materials had not increased … in the current quarter").

any previous cybersecurity incidents, have materially affected or are reasonably likely to materially affect the registrant."). But that is not true of Item 105. The Ninth Circuit provided no basis for the notion that a reasonable investor understands an Item 105 risk disclosure to "speak[] entirely of as-yet unrealized risk" unless it includes specific language to that effect.

As a further rationale for imposition of Rule 10b–5 liability, the Ninth Circuit asserted that unless a risk disclosure refers to any realized risk, the disclosure necessarily represents the risk "as purely hypothetical," and an investor would treat it as "merely conjectural." Pet. App. 25a. But the Ninth Circuit offered no justification for these *ipse dixits*, which incorrectly assume that a reasonable investor construes a risk disclosure – even though it concerns only the possible *future* occurrence of an event – as conveying that the event had never occurred in the past.

Item 105 does not differentiate between or assign different weight to risks that have previously transpired and those that have not. And a risk disclosure should be assumed to mean what it says: the stated risk is real and makes an investment in the company risky in the future. Any other assumption would defeat the very purpose of a risk disclosure. Unless a company comments specifically on the likelihood of a risk – something neither Item 105 requires nor that is normal practice[4] – a reasonable

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[4] *See* Donald C. Langevoort, *Disasters and Disclosures: Securities Fraud Liability in the Shadow of Corporate Catastrophe*, 107 Geo. L.J. 967, 991 (2019) ("First, and most importantly, [Item 105] requires identification but not

investor should not be assumed to believe that any risk disclosure is less meaningful or less likely than any other. Quite the contrary, because a risk disclosure "is not a sham warning," the law assumes that "a reasonable investor would understand as much." *Root*, 100 F.4th at 689; *see also Sundaram v. Freshworks Inc.*, 2023 WL 6390622, at *8 (N.D. Cal. Sept. 28, 2023) ("[W]here a company's filings contain abundant and specific disclosures regarding the risks facing the company, … the investing public is on notice of these risks and cannot be heard to complain that the risks were masked as mere contingencies.") (citation omitted).

B. Risk disclosures are subject to the legal protections afforded to forward-looking statements and generally are non-actionable as a matter of law.

Risk disclosures are indisputably "forward-looking statements" under the federal securities laws. *Bondali,* 620 F. App'x at 491 (risk disclosures are "inherently *prospective* in nature") (emphasis in original); *see also Ehlert v. Singer*, 245 F.3d 1313, 1318 (11th Cir. 2001) ("The section of the prospectus at issue ... discuss[ing] [a company's] 'future success' and risk-factors that might affect that success ... is a forward-looking statement."). Forward-looking statements enjoy special status with unique legal safeguards against Rule 10b–5 liability. This has been true ever since the judicially-created "bespeaks

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assessment—that is, it requires describing kinds of risk but does not explicitly require discussion of either the probability that the risks described will come to pass or the impact on the company if they do.").

caution" doctrine emerged to "shield[] companies … from liability when they make statements that are forward-looking and accompanied by meaningful cautionary language." *Root*, 100 F.4th at 688; *see also* Hugh C. Beck, *The Substantive Limits of Liability for Inaccurate Predictions*, 44 Am. Bus. L.J. 161, 175–81 (2007) (discussing the early history and development of the "bespeaks caution" doctrine). In other words, "[c]ertain alleged misrepresentations ... are immaterial as a matter of law because it cannot be said that any reasonable investor could consider them important in light of adequate cautionary language." *Halperin v. eBanker USA.COM, Inc.*, 295 F.3d 352, 357 (2d Cir. 2002).

Recognizing the wisdom behind the "bespeaks caution" doctrine and the public policy goals it supported, Congress enacted a "safe harbor" in the Private Securities Litigation Reform Act of 1995 (PSLRA) that was intended to perform a nearly identical function (though without supplanting the doctrine). *See* Beck, 44 Am. Bus. L.J. at 162 & n.5. A company can invoke the statutory safe harbor's protection (among other ways) by providing "meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement." 15 U.S.C. § 78u–5(c)(1)(i). Congress enacted the safe harbor to incentivize companies to disclose information about a company's prospects that investors find valuable, while offering protection from meritless lawsuits for failure to accurately predict the future. *See* H.R. Rep. No. 104-369, at 32, 43 (1995), *reprinted in* 1995 U.S.C.C.A.N. 730, 731, 741 (explaining that the statutory safe harbor was designed to "enhance market efficiency by

encouraging companies to disclose forward-looking information" by reducing "[t]he muzzling effect of abusive securities litigation").

As courts have held, the cautionary language need not be separate from the forward-looking statement to invoke the protections of the bespeaks caution doctrine or the PSLRA safe harbor. If the statement itself is "couched in" cautionary language, then it is protected. *Shaw v. Digital Equip. Corp.*, 82 F.3d 1194, 1213 (1st Cir. 1996) (applying bespeaks caution doctrine). In other words, risk disclosures are "self-executing" under the bespeaks caution doctrine and the PSLRA safe harbor because they are both forward-looking and a cautionary disclaimer alerting investors that the described event might materialize.

For example, in *Root*, the plaintiff challenged the following risk disclosure under Rule 10b–5: "As we grow, we *may* struggle to maintain cost-effective marketing strategies, and our customer acquisition costs *could* rise substantially." 100 F.4th at 682 (emphasis in original). According to the plaintiff, the company already experienced an increase in customer acquisition costs, which made the risk disclosure misleading. *Id.* The Sixth Circuit observed that a statement "labeled a risk factor" is "a cautionary statement" and "forward looking." *Id.* at 689. Thus, the Sixth Circuit held that a risk disclosure "falls squarely within the Bespeaks Caution doctrine's protection" because a "reasonable investor" would understand the disclosure as a legitimate warning of potential harm. *Id.* Accordingly, the plaintiff's argument that the company "should have said its marketing strategy was affecting [its] CAC, instead of

saying that it *could*, fail[ed].” *Id.* (emphasis in original) (citing *Bondali*, 620 F. App’x at 491).

Because of protections like the bespeaks caution doctrine and PSLRA safe harbor, risk disclosures “[t]hough ubiquitous in securities filings … have only rarely been found to be actionable by themselves.” *Marriott*, 543 F. Supp. 3d at 128 (citation omitted). The Ninth Circuit’s ruling turns these protections on their head. Rather than treating risk disclosures as non-actionable forward-looking statements, the Ninth Circuit converted them by judicial fiat into actionable statements of current or historical fact. Simply put, the Court also should reverse the Ninth Circuit because the legal protections for forward-looking statements must continue to apply with equal force to forward-looking risk disclosures.

II. The Ninth Circuit’s decision undermines important public policy goals.

The Court should clarify that only risks involving possible future events need to be disclosed as part of a company’s Item 105 risk disclosures and that such a risk disclosure is not rendered misleading by omission of backwards-looking information, unless it includes an express representation about the past or present. Such a ruling would have several important public policy benefits far beyond this case.

A. The Ninth Circuit's decision conflicts with recent amendments and guidance intended to shorten Item 105 risk disclosures and rid them of immaterial and unhelpful information.

As part of its recent amendments to Item 105, the SEC noted that "prescriptive requirements result in disclosure that is not material to an investment decision and is costly to provide." Modernization of Regulation S-K Items 101, 103, and 105, 85 Fed. Reg. 63,726, 63,746 (Oct. 8, 2020). The amendments were meant to "discourage … the disclosure of information that is not material," *id.*, and "to improve disclosures for investors and to simplify compliance efforts for registrants" with a "thoughtful mix of prescriptive and principles-based requirements that should result in improved disclosures and the elimination of unnecessary costs and burdens." Press Release, *SEC Proposes to Modernize Disclosures of Business, Legal Proceedings and Risk Factors under Regulation S-K* (Aug. 18, 2019), https://tinyurl.com/y5phuhrt. The SEC believed the amendments would "reduce disclosure costs and burdens," in part because companies "would have the flexibility to determine whether certain information is material under the principles-based approach." 85 Fed. Reg. at 63,746.

The amendments to Item 105 were lauded as good news for investors and companies alike. As one commentator put it, "[i]nvestors will not need to wade through as much material to find key points," and "companies are no longer required to list everything but the proverbial kitchen sink when describing their businesses, their liability exposures, and their risks."

See Alexandra R. Lajoux, *SEC's New Reg S-K is Good News for Investors and Directors Alike*, Nat'l Assoc. of Corporate Directors (Aug. 31, 2020), https://tinyurl.com/3uz8jpy5.

But the decision below will undo any positive gain from this rule change and set the stage for an unworkable disclosure regime, one that forces companies to lard their risk disclosures with extraneous details of past incidents rather than focusing on the most important risks of possible future events facing the company. Contrary to the SEC's stated goals, affirming would increase the complexity of risk disclosures and corresponding costs borne by companies trying to comply with the court's new standard for Item 105.

"[E]ven if more concise and firm-specific risk factors provide greater clarity to investors," companies may believe "lengthier and more boilerplate risk factor disclosures provide benefits to the firm by reducing the likelihood that those disclosures are flagged as inadequate under judicial and regulatory review." Richard A. Cazier et al., *Are Lengthy and Boilerplate Risk Factor Disclosures Inadequate? An Examination of Judicial and Regulatory Assessments of Risk Factor Language*, 96 The Accounting Rev. 131, 132 (July 2021). This would continue a troubling trend of court decisions unwittingly incentivizing "lengthy, non-specific, and standardized risk factor disclosures" that are "associated with more favorable judicial and regulatory assessments," but contravene SEC guidance and that are of less use to investors. *Id.* (empirical study shows that lengthy and boilerplate

risk disclosures receive more favorable assessments from courts).

Moreover, the SEC—and courts—have noted that in areas like cybersecurity companies should not "make detailed disclosures [of cybersecurity events] that could compromise [their] cybersecurity efforts—for example, by providing a 'roadmap' for those who seek to penetrate a company's security protections." SEC Statement and Guidance on Public Company Cybersecurity Disclosures, 83 Fed. Reg. 8,166, 8,169 (Feb. 26, 2018); *see also Marriott*, 31 F.4th at 905. In other words, the excess disclosure of the materialization of cybersecurity risks itself presents a cybersecurity risk. The same dynamic would certainly apply in many other corporate areas. The Ninth Circuit's decision contradicts SEC guidance like this on the proper scope of risk disclosures.

B. Affirming would harm investors because companies will over-disclose immaterial and unhelpful information in response to litigation risk.

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)). Empirical data also has shown that investors and analysts following a stock are better able to evaluate and accurately predict share price movements through more specific risk

disclosures unburdened by boilerplate and vague language about immaterial issues. *See* Ole Kristian Hope et al., *The Benefits of Specific Risk-Factor Disclosures*, 21 Rev. of Accounting Studies 1005, 1032 (2016) ("Our empirical findings … suggest that the level of specificity in risk disclosures does affect investors' and analysts' evaluations.").

Reversal would not prejudice investors. They can still sue if a company has made statements of *current or historical fact* that are rendered misleading by 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 of the materialization of risks calling the financial performance into question. *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."). Even without the Ninth Circuit's improper ruling, investors will continue to have avenues to seek redress when a company fails to disclose the materialization of a risk if it renders other statements specifically about the past or present misleading.

C. Affirming would result in meritless lawsuits premised on forward-looking risk disclosures.

Risk disclosures are "ubiquitous" because they are required by Item 105 and facilitate forward-looking disclosures and projections under the PSLRA "safe harbor" that companies might otherwise not

provide. For good reason, risk disclosures have "rarely" served as the basis for securities class actions.

Affirming would change the status quo, materially expand the scope of Rule 10b–5 liability, and usher in a new wave of lawsuits based on a company's failure to disclose past incidents alongside risk disclosures. This outcome would run contrary to Congress's stated desire to limit the proliferation of meritless securities litigation.

As this Court has noted, 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). The Court once again must 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. … '[W]e deal with a judicial oak which has grown from little more than a legislative acorn.'") (citation omitted).

CONCLUSION

This Court should reverse.

Respectfully submitted,

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