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The Circuits Split on Securities Act Pleading Standards

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Last week, the United States Court of Appeals for the Sixth Circuit held that a claim alleging a false statement of opinion or belief in a registration statement may proceed under Section 11 of the Securities Act notwithstanding the absence of allegations showing that the defendants did not actually hold the opinion or believe the statement. Indiana State District Council of Laborers & Hod Carriers Pension & Welfare Fund v. Omnicare, Inc., (6th Cir. May 23, 2013). The Sixth Circuit's decision conflicts with decisions of the Second and Ninth Circuits holding that liability under Section 11 for a statement of belief or opinion would exist only if the statement was both objectively and subjectively false or misleading. *See Fait* v. *Regions Financial Corp*., 655 F.3d 105 (2d Cir. 2011); *Rubke* v. *Capital Bancorp Ltd*., 551 F.3d 1156 (9th Cir. 2009). Under that standard, a Section 11 complaint that fails to plausibly allege that a defendant did not actually believe the false statement or hold the opinion would be dismissed.

The Sixth Circuit reasoned that Section 11 provides for strict liability for misrepresentations or omissions of material facts in a registration statement and hence "a defendant's knowledge is not relevant." The Court distinguished claims under Section 10(b) and Rule 10b-5, which require proof of scienter, and declined to follow *Virginia Bankshares, Inc.* v. *Sandberg*, 501 U.S. 1083 (1991), which first articulated the "objective and subjective" falsity standard. The Supreme Court's decision in *Virginia Bankshares* involved a misleading proxy claim under Section 14(a) of the Exchange Act. The Sixth Circuit read the Supreme Court's opinion to have assumed that the jury in that case had found that defendants made their statements with knowledge of their falsity; accordingly, in the Sixth Circuit's view, the Supreme Court had "effectively treated [Section 14(a)] as a statute that required scienter." The Second and Ninth Circuits, by contrast, have relied on *Virginia Bankshares* and, in particular, on Justice Scalia's concurring opinion in that case, to articulate a general rule for pleading falsity in cases involving statements of opinion or belief.

The issue that divides the Circuits is very significant in Securities Act litigation. Claims under the Securities Act are generally subject to liberal pleading rules and, unlike plaintiffs asserting claims under Rule 10b-5, Securities Act plaintiffs need not plead facts sufficient to raise a strong inference of scienter. Accordingly, the "objective and subjective" falsity standard has often provided defendants with a potent argument for dismissing Securities Act claims, including claims alleging GAAP violations, at the pleading stage where such claims involve assertions of opinion or belief as opposed to statements of concrete historical facts. The issue seems ripe for review by the Supreme Court, which will then have the opportunity to clarify liability standards with respect to both registration statements and proxy materials. We believe that the Second and Ninth Circuit holdings are faithful to *Virginia Bankshares*, which recognized that a statement of opinion or belief involves a factual assertion about the state of mind of the speaker as well as the matter discussed. That reading comports with the language of Section 11 while avoiding potentially abusive litigation.