COMMENT

Puffery or Promises: When Is Cheap Talk Actionable?

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Prof. James Coleman argues that a comparison of statements made by the same company to investors in securities disclosures as opposed to environmental regulators in comments could check the "crying wolf" problem and ferret out when a proposed regulation is genuinely too burdensome or infeasible to implement.[1]

Professor Coleman's thoughtful proposal warrants careful attention. There is no doubt that using a person's own words to respond to their arguments is a deft rhetorical gambit.[2] Yet it is not obvious that corporate disclosures to investors would routinely contain detailed, quantitative projections about the cost and feasibility of proposed regulation, so as to make systematic cross-checks practical. The meticulous empirical analysis that is the centerpiece of Professor Coleman's article sheds light on one aspect of the challenge. It convincingly shows that some companies made *different* statements to the EPA and to investors about the Renewable Fuel Standard and that there were *differences* in tone.[3] But measuring the aggregate number of positive as opposed to negative statements cannot by itself show that any particular statement was *false* or that any required disclosure was deficient.

This comment takes a step back and provides an overview of the securities disclosures framework and how upcoming regulations might fit in. It then looks at how courts distinguish between facts, opinions, forward-looking statements, and puffery when they evaluate fraud claims brought by private litigants. Finally, it concludes with some observations about how differences in tone or emphasis could provide valuable information even when they do not amount to actionable fraud.

I. Why Disclosure and What Disclosures?

Companies will often make predictions to investors about the business impact of proposed regulations. But not all such disclosures are of equal use for environmental regulators. For instance, a heavily caveated, qualitative sentiment couched in conditional terms does little to ease the "regulator's dilemma," unlike concrete, quantitative data about the "monetary cost and practical feasibility" of a proposal.[4]

Disclosure is one of the fundamental underpinnings of securities regulation. In the wake of the Great Depression, many urged a comprehensive system of federal "merit review" in which a securities offering would be allowed only if it was judged that the business was sound and that the investment was not unfair, unjust, or inequitable.[5] A competing view was championed by Justice (then Mr.) Louis Brandeis, who urged publicity and sunlight as the best of disinfectants to ills social and industrial. Carried forward by President Franklin Delano Roosevelt, Brandeis's philosophy of disclosure largely won out.

At bottom, the disclosure requirements are designed to arm investors with information to allow them to make informed decisions, which, in turn, fosters confidence in the markets and promotes the efficient allocation of capital. They represent, in F.D.R.'s words, a complement to the "ancient rule of *caveat emptor*"[6] by not only prohibiting affirmative frauds, such as misrepresentations and mislead-

1. James W. Coleman, *How Cheap Is Corporate Talk? Comparing Companies' Comments on Regulations With Their Securities Disclosures*, 40 Harv. Envtl. L. Rev. 47 (2016)).
2. *See generally* William Shakespeare, *Hamlet*, act III, scene 4, lines 206–207 ("For 'tis the sport to have the enginer/Hoist with his own petar . . . .").
3. Coleman, *supra* note 1, at 70–75. A significant number of companies endorsed comments submitted by industry trade associations, which do not typically themselves file securities disclosures. Trade association participation can be an attractive way to compile sectorwide information about current practices and modeling about the impact of proposed regulation, while at the same time creating distance from what may be unpopular stances. Jonathan Weinberg, *The Right to Be Taken Seriously*, 67 U. Miami L. Rev. 149, 181 (2012); Timothy F. Malloy, *The Social Construction of Regulation: Lessons From the War Against Command and Control*, 58 Buff. L. Rev. 267, 337–41 (2010).
4. *Cf.* Coleman, *supra* note 1, at 51.
5. *See* 1 Louis Loss & Joel Seligman, Securities Regulation §1C at p. 45 (6th ed. 2011).
6. H.R. Rep. No. 85, at 2, 73d Cong. 1st Sess. (1933); *see, e.g.*, SEC v. Zandford, 535 U.S. 813, 819 (2002).

ing-by-omission half-truths, but also by mandating disclosure of specified, pertinent information.[7]

What follows speaks in generalities, recognizing that the rules are peppered with special cases, exceptions, exemptions, and exceptions to the exemptions—all, happily, of no import for present purposes. Suffice it to say, many of the stakeholders that would be motivated to submit comments in connection with proposed environmental regulation are public companies that file annual reports (Form 10-K), quarterly reports (Form 10-Q), and reports when certain events occur (Form 8-K).[8]

Regulation S-K describes what must be included in these filings.[9] For example, Item 503(c) instructs a company to discuss the "most significant factors that make the offering speculative or risky."[10] Item 303 asks for narrative information "necessary to an understanding of [the company's] financial condition," including the company's future prospects.[11] That item requires a discussion and analysis of "known trends or uncertainties that have had or that the [company] reasonably expects will have a material" impact on revenues.[12] And as an overarching matter, Exchange Act Rule 12b-20 requires, in addition to anything expressly required to be disclosed, "such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they [were] made not misleading."[13]

It is easy to see why proposed or pending regulations could trigger these standards and thus require disclosure.[14] Yet, such a discussion would not necessarily contain the level of detail and specificity that the company might include in comments—especially if it was trying to persuade EPA that a proposal was not technically feasible. These disclosure items are largely principles-based in that they identify general topics and rely on context-specific judgments about what discussion is necessary.[15] The touchstone is materiality: Whether there is objectively a "substantial likelihood" that a "reasonable investor" would attach importance to the information in making an investment decision.[16]

Just as airing pertinent information can empower investors, unnecessary detail can, as Justice Thurgood Marshall wrote, "bury . . . shareholders in an avalanche of trivial information."[17] Disclosure guidance has therefore consistently encouraged companies to "emphasize material information and de-emphasize" the immaterial.[18] This guidance has also stated that, in some cases, "[q]uantification of the material effects of known material trends and uncertainties can promote understanding" and "may be required to the extent material if quantitative information is reasonably available."[19] At the same time, it has recognized that not all the "substantial amount of financial and non-financial information available" to companies in evaluating such trends and uncertainties is itself material, and supplying this unfiltered, underlying data might result in "information overload" from the perspective of investors.[20] Such judgments must be made on a case-by-case basis, considering not only the underlying facts and circumstances, but also what has already been said and what is already widely known.[21]

There is, in sum, ample reason to expect that many companies would address exposure to regulatory risk in their investor communications. Often, such disclosures will be mandatory and, in any event, conspicuously ignoring the elephant in the room may lead shareholders to assume the worst.[22] But it is by no means clear that these disclosures would address issues with the level of detail, specificity, and quantification that environmental regulators would find most useful.[23]

II. Facts, Opinions, Predictions, or Puffery?

If a company asserts directly contradictory, concrete, and material facts to two different audiences, it might expect to receive a fair bit of attention from regulators and the private securities bar alike. But what about statements like:

7. *See* Restatement (Second) of Torts §551 (stating the common-law rule).
8. *See* 15 U.S.C. §78m; 17 C.F.R. §§240.13a-1, 240.13a-11, 240.13a-13; 1 Loss & Seligman, *supra* note 5, §6B(1)(a)-(b) at pp. 670–78.
9. *See* Adoption of Integrated Disclosure System, 47 Fed. Reg. 11,380 (Mar. 3, 1982).
10. 17 C.F.R. §229.503(c).
11. 17 C.F.R. §229.303(a); Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations, 68 Fed. Reg. 75,056, 75,056 (Dec. 19, 2003) [hereinafter 2003 Guidance].
12. 17 C.F.R. §229.303(a)(3)(ii).
13. 17 C.F.R. §240.12b-20.
14. Whether these requirements create an actionable duty to disclose in a private fraud case is currently before the Supreme Court. *See* Leidos, Inc. v. Ind. Pub. Retirement Sys., 818 F.3d 85 (2d Cir. 2016), *cert. granted*, No. 16-581 (Mar. 27, 2017).
15. Concept Release: Business and Financial Disclosure Required by Regulation S-K, 81 Fed. Reg. 23,916, 23,925, 23,954 (Apr. 13, 2016) [hereinafter 2016 Concept Release]; 2003 Guidance, *supra* note 11, at 75,060–61.
16. TSC Indus., Inc. v. Northway, 426 U.S. 438, 449 (1976); 17 C.F.R. §240.12b-6. Item 303 contains its own, two-step materiality standard. Interpretive Release: Management's Discussion and Analysis of Financial Condition and Results of Operations, 54 Fed. Reg. 22,427, 22,430 & n.27 (May 18, 1989) [hereinafter 1989 Interpretive Release].
17. *TSC Indus.*, 426 U.S. at 448–49.
18. 2016 Concept Release, *supra* note 15, at 23,942; 2003 Guidance, *supra* note 11, at 75,057, 75,060–62.
19. 2003 Guidance, *supra* note 11, at 75,062; 1989 Interpretive Release, *supra* note 16, at 22,429.
20. 2003 Guidance, *supra* note 11, at 75,057, 75,061–62.
21. *Compare, e.g.*, Pension Fund Group v. Tempur-Pedic Int'l, Inc., 614 F. App'x 237, 244 (6th Cir. 2015); J&R Mktg. v. Gen. Motors Corp., 549 F.3d 384, 394 (6th Cir. 2008); In re Lyondell Petrochem. Co. Sec. Litig., 984 F.2d 1050, 1052–53 (9th Cir. 1993), *with* Litwin v. Blackstone Group, L.P., 634 F.3d 706, 718–19 (2d Cir.2011); Helwig v. Vencor, Inc., 251 F.3d 540, 561 (6th Cir. 2001) (en banc).
22. *See generally* George Akerlof, *The Market for Lemons: Quality Uncertainty and the Market Mechanism*, 74 Q.J. Econ. 488 (1970).
23. For example, one study found that most climate change disclosures did not attempt to quantify impacts or risks. *See* Robert G. Eccles & Michael P. Krzus, The Integrated Reporting Movement: Meaning, Momentum, Motives, and Materiality 138 (2014). The sufficiency of such disclosures cannot, of course, be evaluated without more information and analysis.

We're proud of our flexibility and we believe we're better positioned than competitors to adapt the proposed regulation.

A rule identical to the proposed regulation increased widget production costs by 37% for our overseas factory.

No doubt it would be uncomfortable for a CEO to be confronted with these statements at a hearing on the Hill. Yet is the first statement necessarily false (and fraudulently so) if the second one is true? These potential conceptual mismatches may make it difficult to rely on securities disclosures as a self-implementing check on the accuracy of comments to regulators. Courts have distinguished between various categories of representations in assessing whether they may be the basis for a fraud action by an aggrieved investor.[24] Four are pertinent here: Assertions of fact, opinions, forward-looking statements, and puffery.

Facts: A "fact is 'a thing done or existing' or '[a]n actual happening,'"[25] which may include presently existing or past states of mind.[26] It is a straightforward enough matter that misstatements of fact can be actionable as fraud, subject to the usual requirements of materiality, scienter (if applicable), and the like.

Opinions: An opinion is "a belief,"[27] and, unlike a fact, an opinion "does not imply . . . definiteness . . . or certainty."[28] It may involve matters for which "individual judgments may be expected to differ."[29] An opinion is not false merely because it turns out to be wrong; still, an opinion may be fraudulent if it is not sincerely believed or it contains embedded false statements of fact.[30] And an opinion can also be misleading in virtue of what has been *omitted*, if under the circumstances it impliedly and falsely represents that there is a sufficient basis for the belief and that no known, undisclosed facts are incompatible with it.[31]

Predictions[32]: For decades, the disclosure of forward-looking information was generally unlawful, due to the perception "that such information was inherently unreliable, and that unsophisticated investors would place undue emphasis" on it.[33] Beginning in the 1970s, that policy began to change so as to foster discussion of future plans or risks, while not inviting litigation over good-faith predictions proven incorrect in hindsight. Courts developed the "bespeaks caution" doctrine, under which a predictive statement may be immaterial (or cannot reasonably be relied upon) if accompanied by sufficiently substantive and tailored cautionary language.[34] Regulators[35] and eventually Congress devised safe harbors as well, culminating in the Private Securities Litigation Reform Act of 1995's "forward-looking statements" provision.[36]

Puffery: Finally, courts have concluded that certain kinds of statements are so vague or indefinite as to be inactionable. Puffery includes buzzword-filled "general statements" about whether a company "set[s] the standard"[37] or broad expressions of "corporate optimism" about leveraging "compelling opportunities."[38] The rationale is that puffery does not convey any substance that a reasonable person would deem important to, and rely upon in making, an investment decision.[39]

III. Conclusion

If projections or predictions were too easily re-characterized as promises or guarantees, the resultant chilling effect could lead to less information being available to regulators and investors alike. Nor does every inconsistency in tone or shift in emphasis amount to fraud. But it does not follow that environmental regulators, or others with an interest in assessing how companies adapt to proposed regulation, should neglect Professor Coleman's proposal.

After all, an agency engaged in rulemaking need not prove that a commenter's feasibility projections are fraudulent. Regulators decide how much weight to give each comment. Under the Administrative Procedure Act's "arbitrary and capricious" standard of judicial review,[40] the agency should consider significant comments, but ultimately the record need only reasonably support the premises for the agency's decision.[41] Further, in making "judgmental or predictive" determinations, the agency receives more deference still, and may rely on the informed forecasts of its own

24. Unlike a private plaintiff, the government need not show "justifiable reliance," *SEC v. Morgan Keegan & Co., Inc.*, 678 F.3d 1233, 1244 (11th Cir. 2012), and is not subject to various statutory safe harbors and heightened pleading requirements, *e.g.*, 15 U.S.C. §77z-2(c)(1); SEC. v. Tambone, 550 F.3d 106, 119 (1st Cir. 2008), *reinstated in relevant part on reh'g*, 597 F.3d 436, 450 (1st Cir. 2010) (en banc).
25. Omnicare, Inc. v. Laborers Dist. Council Const. Indus. Pension Fund, 135 S. Ct. 1318, 1325 (2015) (quoting Webster's New International Dictionary 782 (1927)).
26. Restatement (Second) of Torts §525 cmts. d–e.
27. *Omnicare*, 135 S. Ct. at 1325 (quoting Webster's New International Dictionary 1509 (1927)).
28. *Id.* (internal quotation marks omitted).
29. Restatement (Second) of Torts §538A cmt. b.
30. *Omnicare*, 135 S. Ct. at 1326–27; Virginia Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1092 (1991); Restatement (Second) of Torts §525 cmt. d.
31. *Omnicare*, 135 S. Ct. at 1328–30; Restatement (Second) of Torts §539(1); Restatement (Second) of Contracts §168.
32. Some opinions are also forward-looking statements (or vice versa), but the inquiries are analytically distinct. In re Vivendi, S.A. Sec. Litig., 838 F.3d 223, 243–44 (2d Cir. 2016). Likewise, "some predictions about the future can represent interpretations of present facts." Iowa Pub. Emps.' Ret. Sys. v. MF Global, Ltd., 620 F.3d 137, 143 n.13 (2d Cir. 2010).
33. Concept Release: Safe Harbor for Forward-Looking Statements, 59 Fed. Reg. 52,723, 52,723–24 (Oct. 19, 1994).
34. *Id.* 52,727–28; *see, e.g.*, In re Donald J. Trump Casino Sec. Litig., 7 F.3d 357, 371 (3d Cir. 1993); Loss & Seligman, *supra* note 5, §6C(5)(b) at 787–90.
35. *See, e.g.*, Safe Harbor for Projections, 44 Fed. Reg. 38,810 (July 2, 1979); 17 C.F.R. §229.303(a), Instruction 7 (specifying that "forward-looking information supplied [in Item 303] is expressly covered by the safe harbor rule," 17 C.F.R. §240.3b-6); Loss & Seligman, *supra* note 5, §2D(2)(a) at 230–35.
36. 15 U.S.C. §§77z-2(c)(1)(A), (i)(1), 78u-5(c)(1); *see, e.g.*, Slayton v. Am. Exp. Co., 604 F.3d 758, 772 (2d Cir. 2010) (collecting cases).
37. ECA, Local 134 v. JP Morgan Chase Co., 553 F.3d 187, 206 (2d Cir. 2009).
38. Grossman v. Novell, Inc., 120 F.3d 1112, 1119–21 (10th Cir. 1997).
39. *See, e.g.*, City of Monroe Employee Ret. Sys. v. Bridgestone Corp., 399 F.3d 651, 671 (6th Cir. 2005); Raab v. Gen. Physics Corp., 4 F.3d 286, 289 (4th Cir. 1993).
40. 5 U.S.C. §706(2)(A).
41. *See, e.g.*, CTS Corp. v. EPA, 759 F.3d 52, 62 (D.C. Cir. 2014); McGregor Printing Corp. v. Kemp, 20 F.3d 1188, 1194 (D.C. Cir. 1994).

experts.[42] As Professor Coleman recognizes, even when comments and securities disclosures are not *technically* inconsistent, it could be reasonable for environmental regulators to discount doom-and-gloom predictions coming from a company simultaneously making rosy reassurances to investors.[43] Other audiences exist as well. Today, virtually all federal rulemaking dockets are online and searchable through the regulations.gov web portal,[44] and there is no reason to believe that investors will ignore this potential source of information about the competitive impact of proposed or pending rules.[45]

42. FCC v. Nat'l Citizens Comm. for Broad., 436 U.S. 775, 813–14 (1978); *see also* Marsh v. Ore. Nat. Res. Council, 490 U.S. 360, 378 (1989); Chamber of Com. v. SEC, 412 F.3d 133, 142 (D.C. Cir. 2005).
43. Coleman, *supra* note 1, at 76–78.
44. ABA Comm. on the Status & Future of Fed. E-Rulemaking, Achieving the Potential: The Future of Federal E-Rulemaking 3 (2008).
45. Halliburton Co. v. Erica P. John Fund, Inc., 134 S. Ct. 2398, 2410 (2014) (endorsing "premise that market professionals generally consider most publicly announced material statements about companies") (internal quotation marks omitted); *cf.* Jonathan L. Rogers et al., *Run EDGAR Run* (Chicago Booth School of Business Research Paper No. 14-36, 2014) (describing computerized analysis of company filings on another government website).