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WHAT DID YOU KNOW AND WHEN DID YOU KNOW IT?: PUBLIC COMPANY DISCLOSURE AND THE MYTHICAL DUTIES TO CORRECT AND UPDATE

Gregory S. Porter*

INTRODUCTION

A LLEGATIONS of securities fraud generally can be broken down into two types of cases—those claiming fraud based upon what a corporation or its insiders have said, and those claiming fraud based upon what they have not said, but should have. A corporation can clearly be held liable under the federal securities laws if it makes false or misleading statements.1 Less well-defined are the circumstances under which a corporation can be held liable for what it has not said.

The express disclosure requirements for publicly traded companies are a jumble of statutes, rules, forms, and schedules promulgated by the Securities and Exchange Commission ("Commission"), and the interpretive gloss on these express disclosure requirements provided by the Commission.2 Outside this statutory and administrative rule framework, the traditional rule of corporate disclosure has long been

* The author is an associate in the Dallas office of Baker & McKenzie and practices in the areas of securities regulation and mergers and acquisitions. The author wishes to thank Hazel Landwehr Porter for her insightful criticism of early drafts of this Article.


2. Examples of the many explicit disclosure obligations include: (1) the detailed information required to be filed annually on Form 10-K; (2) quarterly information required to be filed on Form 10-Q; (3) Form 8-K's which are required to be filed within 10 days following certain material events such as a change of corporate control, significant acquisitions or dispositions of assets, and changes in a corporation's auditors; and (4) the detailed information required to be filed in a registration statement in connection with the sale of a security.
that corporations have no general duty to disclose information simply because that information is material.\(^3\) Additionally, absent a duty to disclose, there can be no liability for non-disclosure.\(^4\) Over the last several decades, plaintiffs and numerous commentators have urged the creation of a variety of implied disclosure duties to supplement the express disclosure requirements.\(^5\) Two of these implied disclosure duties, the duty to correct and the duty to update, if accepted and robustly applied, threaten to swallow the general rule and impose liability for any failure to disclose material information.\(^6\) In fact, one commentator has suggested that given the "smorgasbord" of statutes, rules, interpretive gloss, and judicially created disclosure duties, we are fast approaching a de facto continuous disclosure requirement for all material information, if we have not reached it already,\(^7\) while another commentator suggests that under current law, virtually any undisclosed information can be attacked under some plausible duty to disclose theory.\(^8\)

This Article argues that fears of a de facto continuous disclosure requirement through judicial fiat are unfounded. The duties to update and correct appear to have assumed a mythical status; they are widely discussed and generally assumed to exist (at least in some form), but very few people have actually seen them.\(^9\) Many cases discuss the

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3. See infra notes 12-33 and accompanying text.
4. See infra notes 20-23 and accompanying text.
5. See infra notes 44-177 and accompanying text.
6. See infra notes 68-113 and accompanying text.
7. See Dale A. Oesterle, The Inexorable March Toward a Continuous Disclosure Requirement for Publicly Traded Corporations: "Are We There Yet?", 20 Cardozo L. Rev. 135, 136-38 (1998). Professor Oesterle argues that the complex system of statutes and administrative rules, combined with inconsistent interpretations of the statutes and rules by federal courts, threatens to make corporate disclosure so difficult that securities lawyers will recommend to their clients that continuous disclosure of all material information is necessary to avoid liability. See id. He also argues that a system that expressly requires disclosure of all material information with certain exceptions might be preferable to the current system under which there is no requirement to disclose material information absent a duty. Identifying the duties, however, is extremely complex. See id. at 171-91. He further suggests that modifications to our current system of enforcing disclosure obligations could ameliorate the problems inherent in a continuous disclosure system. See id. at 158-65. Finally, he notes that the various stock exchanges have rules that effectively amount to a continuous disclosure system (although they are not generally enforced). See id. at 174-75, 220-25. Whether an express continuous disclosure system might be preferable to the current disclosure system is beyond the scope of this Article. This Article does, however, attempt to explain some of the compliance difficulties presented by a continuous disclosure system given the current enforcement framework.
9. See Robert H. Rosenblum, An Issuer's Duty Under Rule 10b-5 to Correct and Update Materially Misleading Statements, 40 Cath. U. L. Rev. 289, 315 (1991) (discussing the duties to correct and update, Rosenblum states that "relatively few courts have purported to impose liability for the breach of either duty, and few of the
duties, and the federal courts have often stated that they exist. Rarely, however, have the federal courts given any justification for them. Further, when actually faced with a plaintiff seeking damages, the federal courts have frequently found reasons not to impose the duties. Enough cases and commentators have nonetheless suggested that the duties exist, despite their narrow application to date, to chill the disclosure of forward-looking information, and to give justifiable concern to corporations and their counsel in navigating the maze of disclosure requirements.

Part I of this Article discusses the general rule that information is not required to be disclosed simply because it may be material, and analyzes the insider trading cases that created the first widely accepted disclosure duty outside the explicit requirements of the securities laws and the Commission's rules. Part II then examines the various forms the duties to correct and update have assumed, and describes how, if the duties were robustly applied, a continuous disclosure system could ensue. This part also shows the disparate treatment afforded historical factual statements and "forward-looking statements" by the federal courts. Finally, this part argues that despite the fears generated by a few poorly articulated cases, the federal courts have rarely imposed liability for failure to comply with the duty to correct or the duty to update.

Part III examines the justifications for the duties to correct and update. This Article first concludes that the duty to correct is a remedy in search of a problem. In all but the narrowest of circumstances, a remedy exists under current doctrine for the securities law violation that the duty to correct is purported to cover, rendering the duty to correct superfluous. With respect to the duty to update, this Article concludes that the duty to update is not compatible with section 10(b) of the Exchange Act or Rule 10b-5. The federal securities laws require statements be judged at the time they are made; they do not permit reference to subsequent changed circumstances to determine whether a statement is misleading. In addition, forward-looking statements by their nature are not capable of being correct or incorrect. They are only opinions as to the future. As such, when events fail to materialize as foretold, highlighting the impossibility of predicting the future, prior statements are not rendered misleading. Even if a duty to update did exist at one time, such a duty was largely eliminated by the Private Securities Litigation Reform Act of 1995 ("Reform Act").10 Part III also argues that

complying with a broadly interpreted duty to update would be virtually impossible.

Finally, Part IV offers suggestions for a new approach to analyzing forward-looking statements. This Article argues that Rule 10b-5 should be read to require that a corporation’s statements be viewed in light of the corporation’s prior forward-looking statements. Corporations should not be required to continually reevaluate all prior forward-looking statements; changed circumstances should not render prior forward-looking statements fraudulent. When corporations voluntarily choose to speak or are required to speak as a result of periodic or episodic filing requirements, however, they should be required to take into account their prior forward-looking statements. If at the time of such voluntary or required speech, circumstances have changed from those that existed when an earlier forward-looking statement was made, additional disclosure regarding the prior statements may be necessary in order to prevent the current statements from being misleading. In addition, when a corporation is required to speak in quarterly and annual filings, Item 303 of Regulation S-K may provide an independent basis to require corporations to update their prior forward-looking statements.

I. THE GENERAL RULE AND THE FIRST IMPLIED DISCLOSURE DUTY

One of the primary purposes of the federal securities laws is to require corporations to disclose information sufficient for investors to make rational investment decisions. Indeed, the federal securities laws explicitly require disclosure of a broad range of information, both periodically and based upon the occurrence of certain events. The

Act’s definition of forward-looking statements, and not all statements meeting that definition qualify for the safe harbor provisions. See infra notes 276-89 and accompanying text.


12. The preamble to the Securities Act states that the Securities Act is “[a]n Act [t]o provide full and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails, and to prevent frauds in the sale thereof.” Securities Act of 1933, Ch. 38, 48 Stat. 74 (1933) (codified as amended in 15 U.S.C. § 77a (1999)); see also Central Bank v. First Interstate Bank, 511 U.S. 164, 171 (1994) (stating that the purpose of the Securities Act was to replace caveat emptor with a system of full disclosure); Basic Inc. v. Levinson, 485 U.S. 224, 234 (1988) (same); SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963) (noting that a fundamental purpose of the securities laws was “to substitute a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the securities industry” (emphasis omitted)).

13. The periodic disclosure requirements include: (1) the annual filing of Form 10-K, which requires an extensive discussion of the corporation’s business for the preceding five years; (2) disclosure of audited financial statements for the immediately preceding three fiscal years, and management’s analysis of the changes in its financial condition and the results of its operations for the periods covered by its financial statements (known as the “MD&A”); and (3) quarterly filings of Form 10-Q,
The literal language of the federal securities laws, however, clearly does not require disclosure of all material information. The explicit provisions do not require disclosure of material developments occurring between periodic filings with the Commission and not coinciding with the episodic filing requirements.

During the 1960's and 1970's, numerous commentators argued over whether the general anti-fraud provisions of the securities laws, section 10(b) of the Exchange Act and Rule 10b-5, could be read to which require quarterly and year-to-date financial statements and an MD&A covering the quarter and year-to-date period. Episodic disclosure requirements include: (1) filing of a proxy statement preceding any meeting of the corporation's stockholders, which requires detailed information about the items to be voted on at the stockholder's meeting; (2) registration statements that are required to be filed prior to the sale of the corporation's securities, which requires an extensive disclosure regarding the contemplated offering; and (3) the filing of Form 8-K, which is required to be filed within 10 days following certain material events such as a change of control of the corporation, significant acquisitions or dispositions of assets, and changes in a corporation's auditors.

14. See Mitu Gulati, When Corporate Managers Fear a Good Thing is Coming to an End: The Case of Interim Nondisclosure, 46 UCLA L. Rev. 675, 678-79 (1999). The author states:

While the securities laws require the disclosure of a large quantity of information in the public offering context and otherwise, they do not create any standing rule or impose upon companies any general duty to disclose to the public all material information whenever such information becomes available to the company.


15. While the federal securities laws do not have a requirement to disclose all material information, each of the major stock exchanges do have such a requirement. See New York Stock Exchange Company Manual § 202.05 (1996); American Stock Exchange Guide § 401(a) (1992). The American Stock Exchange does provide an exception for "facts that are in a stock of flux" and information that would "prejudice the ability of the company to pursue corporate objectives." American Stock Exchange Guide § 402(a). Each of the exchanges has severe penalties for failure to comply with their rules, including delisting from the exchange, but such rules are rarely enforced. Moreover, the federal courts have held that there is no private right of action for violation of exchange rules. See, e.g., Walck v. American Stock Exchange, Inc., 687 F.2d 778, 780 (3d Cir. 1982) (holding no private right of action exists for violation of exchange rules), cert. denied, 461 U.S. 942.

16. Section 10(b) makes it unlawful:

[t]o use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.


17. Rule 10b-5 reads as follows:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
require prompt disclosure of all material information, thus filling in the gaps left by the explicit provisions of the securities laws. Those in favor of reading a requirement to promptly disclose all material information into the anti-fraud provisions made five primary arguments: (1) an implied representation existed that issuers of securities would deal fairly with the public; (2) fair dealing encompassed complete disclosure; (3) investor confidence in the securities markets required full disclosure; (4) full disclosure was necessary to effectively deal with insider trading; and (5) public policy deemed the federal securities laws' explicit disclosure requirements insufficient.

The Supreme Court, in *Chiarella v. United States*, rejected all arguments that section 10(b) of the Exchange Act or Rule 10b-5 requires disclosure of all material information. The Court stated: "When an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak. We hold that a duty to disclose under § 10(b) does not arise from the mere possession of nonpublic market information."

The *Chiarella* Court defined what has since become the general rule: corporations do not have a continuous duty to disclose all

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(c) To engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.


21. See id. at 233-34.

22. Id. at 235.
material information simply because the information may be material. The Court, however, also recognized the first disclosure duty not found in the explicit provisions of the federal securities laws—the duty of an insider to disclose all known material information or to abstain from trading.

Chiarella addressed the circumstances under which a person could be found guilty of securities fraud based upon trading while in possession of material information which is not generally available to the investing public (otherwise known as insider trading). The lower federal courts and the Commission had previously addressed the issue. In Cady, Roberts & Co., the Commission determined that a corporate insider must abstain from trading in the shares of his corporation unless he has first disclosed all material information known to him. In 1968, the Second Circuit in SEC v. Texas Gulf Sulphur Co., recognized this disclosure duty. The Supreme Court in Chiarella then put its imprimatur on the “disclose or abstain” duty. The Court, summarizing the position of the Commission, stated that the duty of insiders to either abstain or disclose arose from “(i) the existence of a relationship affording access to inside information intended to be available only for a corporate purpose, and (ii) the unfairness of allowing a corporate insider to take advantage of that information by trading without disclosure.” The Court’s reasoning in cases involving insider trading has been described as circular: “an affirmative duty to disclose exists when there is a relationship giving rise to an affirmative duty to disclose, and that a breach of such a duty

23. See generally Serabian v. Amoskeag Bank Shares, Inc., 24 F.3d 357, 359 (1st Cir. 1994) (holding that disclosures of past success do not by themselves impose a duty on a corporation to inform the market when circumstances change for the worse); In re Time Warner Inc. Sec. Litig., 9 F.3d 259, 267 (2d Cir. 1993) (“[A] corporation is not required to disclose a fact merely because a reasonable investor would very much like to know that fact.”); Roeder v. Alpha Indus., Inc., 814 F.2d 22, 24 (1st Cir. 1987) (rejecting the argument that the fraud on the market theory imposed a duty to update material information).


26. See id. at 911. The Commission stated that the obligation to disclose or abstain derives from:

[an affirmative duty to disclose material information [which] has been traditionally imposed on corporate “insiders,” particularly officers, directors, or controlling stockholders. We, and the courts have consistently held that insiders must disclose material facts which are known to them by virtue of their position by which are not known to person with whom they deal and which, if known, would affect their investment judgment.]

Id.

27. 401 F.2d. 833 (2d Cir. 1968).

28. The court stated that “anyone in possession of material inside information must either disclose it to the investing public, or . . . must abstain from trading in or recommending the securities concerned while such inside information remains undisclosed.” Id. at 848.

is fraudulent if it is fraudulent.” Nonetheless, the disclosure duty recognized in Chiarella became the first widely accepted implied disclosure duty.

The Chiarella Court, approaching the case solely as a question of non-disclosure, gave little guidance in determining when a “special relationship” would give rise to an affirmative disclosure duty. The acceptance of an implied disclosure duty and the limited guidance in determining when such duties arise, has opened the door for the lower courts to create additional implied disclosure duties. Since Chiarella, commentators and plaintiffs have argued that the explicit disclosure requirements should be supplemented with a variety of implied disclosure duties; the framework in Chiarella lends itself easily to additional implied duties. Commentators have sought to extend the “special relationship” found in Chiarella between corporate insiders and the corporation’s stockholders to a fiduciary duty running directly from the corporation to its stockholders. If such a fiduciary duty exists, it would be ever-present, and could be broad enough to support all types of implied disclosure duties, including a duty to correct and a duty to update.

II. THE CURRENT STATE OF THE LAW

From their first mention, no consensus has existed as to what is meant by a duty to correct or a duty to update. Commentators and plaintiffs have used the term “duty to correct” to advocate a variety of mandatory corrective disclosures, suggesting that a duty to correct might encompass everything from correcting a corporation’s prior

30. Rosenblum, supra note 9, at 293.
31. The Supreme Court could have reached the same conclusion in Chiarella without resorting to creating a new disclosure duty. The Court could have simply held under section 10(b) and Rule 10b-5(a) or (c) that trading in a security by a corporation or an insider while in possession of material undisclosed information is a fraudulent scheme or device. The court instead focused on Rule 10b-5(b) and the circumstances in which an omission would be fraudulent. See David M. Brodsky & Daniel J. Kramer, A Critique of the Misappropriation Theory of Insider Trading, 20 Cardozo L. Rev. 41, 57-58 (1998). As the Court made clear in Chiarella, the possession of material undisclosed information alone does not trigger a disclosure duty. See Chiarella, 455 U.S. at 233. The possession of material undisclosed information should trigger a duty to abstain from trading, making it unnecessary to discuss whether a disclosure duty existed.
32. Three years after Chiarella, the Court in Dirks v. SEC, 463 U.S. 646 (1983), gave some modest amount of additional guidance when it made clear that an additional factor must be present for an implied disclosure duty to arise, stating that not “all breaches of fiduciary duty in connection with a securities transaction, however, come within the ambit of Rule 10b-5.” Id. at 654 (citation omitted). The Court added the further requirement that there must also be manipulation or deception “where one takes advantage of information intended to be available only for a corporate purpose and not for the personal benefit of anyone.” Id. (citation omitted).
33. See Rosenblum, supra note 9, at 294.
inaccurate disclosure, to correcting inaccurate statements made by securities analysts and the media, and to correcting inaccurate rumors in the market (both where the corporation was the source of the inaccurate statements or rumors and situations where the corporation was not the source). In addition, the federal courts and plaintiffs have indiscriminately used the terms "duty to update" and "duty to correct" when discussing whether additional disclosure is required to update or supplement prior accurate statements when circumstances change from those that existed at the time the statements were made. The duties to update and correct have at times been suggested to apply to historical factual statements, forward-looking statements, and other types of statements. The failure to use consistent terminology has made discussing the duty to correct without discussing the duty to update, or vice versa, impossible. The lack of consistent language has also led to great confusion as to the types of statements that might be subject to a duty to correct or a duty to update, as well as the scope of these duties. Some definitions are in order.

As used in this Article, a "duty to correct" refers to a duty to provide additional disclosure to correct previous statements if such statements were inaccurate when they were originally made. This duty to correct would arise once it is discovered that the prior disclosure was inaccurate. The duty to correct has also been suggested to require correcting inaccurate statements made by securities analysts and the media or responding to inaccurate rumors in the market. To the extent that a corporation was not the source of an inaccurate statement or rumor, the federal courts have almost uniformly rejected any duty to "correct" the statements or rumors.

34. The confusion exists, however, only to the extent that there are other types of statements other than historical statements and forward-looking statements. This Article argues that the term "forward-looking statements" covers all statements other than historical factual statements.

35. For example, courts holding that companies have a duty to correct prior inaccurate disclosure have cited prior cases that used the term "duty to correct" improperly. See, e.g., In re MobileMedia Sec. Litig., 28 F. Supp. 2d 901, 937 (D.N.J. 1998) (supporting its holding that companies have a duty to correct prior inaccurate statements, the district court cited Weiner v. Quaker Oats Co., 129 F.3d 310 (3d Cir. 1997), which used the term "duty to correct," but applied it to a forward-looking statement that was not misleading when made but was alleged to have become misleading due to changed circumstances). For additional discussion of the In re MobileMedia case, see infra notes 63-67 and accompanying text.


37. See Wright v. Ernst & Young LLP, 152 F.3d 169, 176 (2d Cir. 1998) (stating that accountants are not required to "correct" statements made by their client that were made attributable to them); Electronic Specialty Co. v. International Controls Corp., 409 F.2d 937, 949, 957 (2d Cir. 1969) (reversing the district court's conclusion
Where a corporation was the source of an inaccurate statement made by others or the source of an inaccurate rumor, the federal courts have treated the statement as one made by the corporation itself, and as such, any duty to correct inaccurate statements by others or to respond to rumors is not a separate duty but is more properly subsumed under a general duty to correct. 38  

The “duty to update,” as that term is used in this Article, describes a duty to provide additional disclosure to supplement or update prior accurate disclosure when circumstances have changed since the original statement was made. 39 The duty has at various times been suggested to apply to all statements, to forward-looking statements only, or to other types of statements. Thus, defining and separating the concept of “forward-looking statements” from historical factual statements is also necessary. Historical factual statements include financial data describing prior fiscal periods and factual statements describing the current environment in which a corporation operates. The federal courts and commentators without defining it have often used the term “forward-looking statement.” The term sometimes has been used as defined by the Commission in Rule 175, 40 promulgated under the Securities Act:

(1) A statement containing a projection of revenues, income (loss), earnings (loss) per share, capital expenditures, dividends, capital structure or other financial items; (2) [a] statement of management’s plans and objectives for future operations; (3) [a] statement of future economic performance contained in management’s discussion and analysis of financial condition and results of operations included pursuant to Item 303 of Regulation S-K . . . ; or (4) [d]isclosed

that a corporation was required to correct an inaccurate newspaper article because there was no indication that the defendant was responsible for the inaccurate statements); see also Rosenblum, supra note 9, at 327 n.158 (listing cases that held that an issuer does not have a duty to correct misleading statements made by third parties).

38. A long line of cases exist positing that a company can become sufficiently intertwined with a third party who makes an inaccurate statement that the courts will deem that the company made the statement itself. See generally Manns, supra note 36, at 1255-64 (discussing cases where the duty to correct has been found for statements made by corporate and extracorporate parties); Sheffey, supra note 18, at 779-95 (same).


40. See 17 C.F.R. § 230.175 (1999). Rule 175 provides that a forward-looking statement (as defined by the rule) contained in a document filed with the Commission will not be misleading under Rule 10b-5 if it was made with a reasonable basis and honestly believed when made. See id. § 230.175(a). For additional discussion of Rule 175 and the Commission’s treatment of forward-looking statements, see infra notes 247-64 and accompanying text.
statements of the assumptions underlying or relating to any of the statements described in paragraphs [(1), (2), or (3)] of this section.\footnote{Id. § 230.175(c).}

Forward-looking statements, as defined by Rule 175, essentially involve management’s projections of the corporation’s future economic performance.

More recently, those discussing the term “forward-looking statement” have referred to the definition in the Reform Act.\footnote{See 15 U.S.C. § 77z-2(i)(1) (1994 & Supp. IV 1998).} While the exact wording is slightly different, the definition in the Reform Act is virtually identical to the definition in Rule 175. Clearly, though, the term does not mean the same thing to everyone. For example, some have suggested that statements of future intent as to corporate actions are distinct from forward-looking statements,\footnote{See infra notes 226-30 and accompanying text.} and whether courts and commentators would include opinions within the definition of forward-looking statements (which may not specifically speak to the future, but may state an opinion, the truth of which will be impossible to determine until a later time) is unclear.\footnote{Opinions would not likely be forward-looking statements under Rule 175 of the Reform Act. \textit{See infra} note 233 and accompanying text.}

This Article uses the term “forward-looking statement” in its broadest sense, intending inclusion of any statement other than one of historical fact. Examples of the types of statements considered in this Article to be forward-looking statements include projections, estimates, statements of intent as to future activities or actions, opinions, or any other statements that in some way speak to the future.\footnote{Forward-looking information is a subset of soft information that includes prospective financial information, predictions, projections, and forecasts. \textit{See} Carl W. Schneider, \textit{Nits, Grits, and Soft Information in SEC Filings}, 121 U. Pa. L. Rev. 254, 255 (1972). Schneider describes soft information as anything other than an objectively verifiable fact. \textit{See id.} at 254-56.}

\textbf{A. Case Law—Duty to Correct}

Numerous cases discuss a “duty to correct.”\footnote{Generally, a duty to correct involves historical factual statements. A couple of cases, however, have suggested that a duty to correct also applies to a forward-looking statement if the statement was misleading when made because it did not have a reasonable basis. \textit{See In re Burlington Coat Factory Sec. Litig.}, 114 F.3d 1410, 1431 (3d Cir. 1997) ("[W]e think the duty to correct can also apply to a certain narrow set of forward-looking statements."). The court then describes a situation where a company makes a forecast of its sales based upon an inaccurate calculation of its past sales. \textit{See id.; infra} notes 196-97, 214 and accompanying text.} Most, however, do not mean a duty to correct as the duty is defined in this Article, i.e., a duty to provide additional disclosure to correct previous statements once a corporation discovers the statements were inaccurate when made. The cases discussing a duty to correct instead discuss what this
Article defines as a duty to update, i.e., a duty to provide additional disclosure to supplement or update prior statements when circumstances change from those in existence when the original statements were made.\textsuperscript{47}

Of those cases actually referring to the "duty to correct" as a duty to correct inaccurate prior statements, the existence of the duty generally is not at issue. Instead, such cases generally involve plaintiffs claiming violation of a duty to update or a violation of some other disclosure duty not explicitly found in the federal securities laws or the Commission's rules. Prior to discussing the existence of the duty in question, the courts in these cases passingly refer to the existence of the duty to correct as "an obvious duty."\textsuperscript{48} None of the cases, however, contain any discussion, analysis, or support of the duty to correct other than a basic statement that it exists.\textsuperscript{49}

After discarding all of the cases that confuse the duty to update

\textsuperscript{47} See, e.g., Weiner v. Quaker Oats Co., 129 F.3d 310, 316 (3d Cir. 1997) (quoting the Third Circuit's interpretation of the duty to correct in \textit{In re Phillips Petroleum Sec. Litig.}, 881 F.2d Supp. 2d 1236 (3d Cir. 1989)); Eisenstadt v. Centel Corp., 113 F.3d 738, 744 (7th Cir. 1997) ("[T]here is no duty to correct a prediction falsified by subsequent events....") (emphasis added); Rubinstein v. Collins, 20 F.3d 160, 170 n.41 (5th Cir. 1994) ("We note that, at least facially, it appears that defendants have a duty under Rule 10b-5 to correct statements if those statements have become materially misleading in light of subsequent events.") (emphasis added); \textit{In re Phillips}, 881 F.2d at 1245 ("There can be no doubt that a duty exists to correct prior statements, if the prior statements were true when made but misleading if left unrevised.") (emphasis added). \textit{Compare In re HealthCare Compare Corp. Sec. Litig.}, 75 F.3d 276, 282 (7th Cir. 1996) (obliterating the distinction between the duty to correct and the duty to update, \textit{with In re International Bus. Machs. Corporate Sec. Litig.}, 163 F.3d 102, 109 (2d Cir. 1998) (holding that "[a]lthough plaintiffs phrase their claim as a duty to correct, we believe plaintiffs are alleging a violation of a duty to update")), and \textit{Stransky v. Cummins Engine Co.}, 51 F.3d 1329, 1331-32 (7th Cir. 1995) (explaining the difference between the duty to correct and the duty to update where the plaintiff had alleged a duty to correct but intended to allege a duty to update).\textsuperscript{48}

\textsuperscript{48} See, e.g., Wright v. Ernst & Young LLP, 152 F.3d 169, 177-78 (2d Cir. 1998) (stating that a duty to correct existed prior to discussing the existence of a duty for accountants to correct statement made by others); \textit{In re Burlington Coat Factory}, 114 F.3d at 1431-32 (same); \textit{Stransky}, 51 F.3d at 1331-32 (stating that a duty to correct exists prior to discussing the existence of a duty to update); Backman v. Polaroid Corp., 910 F.2d 10, 16-17 (1st Cir. 1990) (same); Rudolph v. Arthur Andersen & Co., 800 F.2d 1040, 1043-44. (11th Cir. 1986) (stating that a duty to correct exists prior to discussing the existence of a duty of accountants to disclose fraud by their clients); United States v. Natelli, 527 F.2d 311, 319 (2d Cir. 1975) (stating in dicta that a duty to correct existed in a case where the defendant was found guilty of participating in fraud under section 32(a) of the Exchange Act); Sharp v. Coopers & Lybrand, 83 F.R.D. 343, 346 (E.D. Pa. 1979) (stating that a duty to correct exists prior to discussing the existence of a duty for accountants to update a historical statement).

\textsuperscript{49} See \textit{In re Burlington Coat Factory}, 114 F.3d at 1430-31 (quoting \textit{Stransky} and \textit{Polaroid}); \textit{Stransky}, 51 F.3d at 1331 ("The duty to correct applies when a company makes a historical statement that, at the time made, the company believed to be true, but as revealed by subsequently discovered information actually was not. The company then must correct the prior statement within a reasonable time."); \textit{Polaroid}, 910 F.2d at 16-17 ("Obviously, if a disclosure is in fact misleading when made, and the speaker thereafter learns of this, there is a duty to correct it.").
with the duty to correct and those that state a duty to correct exists
but involve other disclosure duties, only three cases have been found
that impose liability for failure to comply with the duty to correct.
The first case, SEC v. Shattuck Denn Mining Corp.,50 purports to hold
the defendant guilty of securities fraud for failure to correct historical
statements.51 A close reading of the case, however, shows that the
case is nothing more than a routine insider trading case. The
defendant was found guilty of securities fraud after selling stock in the
corporation of which he was president.52 Prior to the time the
defendant sold the stock, he had made statements to a reporter, later
published, that his company had reached terms for a substantial
acquisition.53 Although this statement was true when made, the
parties were no longer in agreement as to “vital terms” at the time the
defendant sold the stock due to a subsequent falling out. 54 The
defendant sold the stock without making public the current status of
the acquisition.55 Although the court described the defendant’s
actions as violating a duty to correct his previous statements, the
defendant in essence traded in his corporation’s stock while in
possession of material undisclosed information.56 Instead of a duty to
correct the previous statement, the defendant had the duty not to
trade in his company’s stock while he had undisclosed knowledge that
there was now no agreement as to the acquisition, which was material
in light of his previous statement that an agreement had been
reached.57

The second case, Fischer v. Kletz,58 held that accountants have a
duty to correct statements they made in certifying their client’s
financial statements when they later find out that information in the
financial statements is inaccurate.59 The court found, however, that
the duty to correct existed under common law and not as an implied
disclosure duty under Rule 10b-5.60 The court specifically reserved
judgement on the plaintiff’s claim under Rule 10b-5.61 Unfortunately,

51. See id.
52. See id. at 476.
53. See id. at 475-76.
54. Id. at 475.
55. See id.
56. See id. at 476.
57. Shattuck Denn Mining Corp. has also been cited as the first case to hold that
there is a duty to update prior statements. See Oesterle, supra note 7, at 147 n.52.
While it would be more proper to describe the case as a duty to update case rather
than a duty to correct case, as the statements made by the defendant were correct
when made, there is no reason to create a new disclosure duty in this case, as the
insider trading doctrine covers this situation.
59. See id. at 188.
60. See id. at 186.
61. See id. at 194.
*Fischer* has been frequently incorrectly cited as support for the proposition that a duty to correct exists under Rule 10b-5.62

The third case may truly be one of the only cases to impose liability for failure to comply with the implied duty under Rule 10b-5 to correct statements that were inaccurate when made. In *In re MobileMedia Securities Litigation*,63 MobileMedia made statements that indicated its operations were in compliance with FCC regulations in its filings with the Commission relating to a public offering of its securities.64 MobileMedia later discovered and subsequently disclosed that it had not been in compliance with FCC regulations at the time it made the statements.65 The court held that sufficient facts in the record existed to give rise to a duty to correct.66 Why the court even referred to a duty to correct, however, is unclear. Because the statements were inaccurate when made, and assuming that the requisite scienter existed, the inaccurate statements violated Rule 10b-5, and the court’s discussion of a duty to correct was unnecessary.67

In conclusion, despite the almost universal acceptance of the duty to correct, there is very little case law to support its existence. Support for the duty to correct rests primarily on the bald statements in dicta by numerous federal courts that the duty exists, with no explanation or justification. The duty to correct has been applied in only a single case, *In re MobileMedia*, which provided no explanation as to why it was necessary to rely on the duty to correct, as the case could have been decided under Rule 10b-5 without the necessity of resorting to a duty to correct. Section B details a surprisingly similar lack of support for a duty to update.

### B. Case Law—The Duty to Update

The first cases to discuss the duty to update suggested an extremely expansive application of the duty. The duty’s expansive application

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62. See, e.g., Rudolph v. Arthur Andersen & Co., 800 F.2d 1040, 1043-44 (11th Cir. 1986) (citing *Fischer* as support for the proposition that Rule 10b-5 imposes a duty on accountants to correct misstatements discovered in previous financial statements); IIT, an International Inv. Trust v. Cornfeld, 619 F.2d 909, 927 (2d Cir. 1980) (same).
64. See id. at 913-17.
65. See id. at 920-21.
66. See id. at 937.
67. Interestingly, the court cited the statements made by the Third Circuit in *Weiner* and *In re Burlington Coat Factory* as support for the proposition that a duty to correct existed under Rule 10b-5. See id. Although purporting to hold that a duty to correct existed, the Third Circuit was referring to a duty to update. See id. The court stated that “[i]f a statement made by or on behalf of a corporation is later found to be misleading, the corporation must correct the statement within a reasonable period of time” and that “[t]here can be no doubt that a duty exists to correct prior statements, if the prior statements were true when made but misleading if left unrevised.” See id. (quoting *Weiner* v. Quaker Oats Co., 129 F.3d 310, 315 (3d Cir. 1997)).
was primarily the result of the federal courts' failure to distinguish the types of statements subject to a duty to update.

The first reported case to suggest that a duty to update might exist was *Ross v. A.H. Robins Co.* The district court ultimately granted the defendant's motion for summary judgement based upon the plaintiffs' failure to adequately plead fraud with particularity as required by Rule 9(b) of the Federal Rules of Civil Procedure. Having thus disposed of the lawsuit, the district court, for reasons unknown, addressed the merits of the case. The plaintiffs in *A.H. Robins* claimed that Robins's failure to "correct" statements it made regarding its product, the Dalkon Shield violated section 10(b) of the Exchange Act and Rule 10(b)(5). Robins made favorable statements regarding the safety and effectiveness of the Dalkon Shield and painted a favorable picture of the product's future. The plaintiffs argued that as medical evidence became available questioning the safety and effectiveness of the Dalkon Shield and numerous class action product liability suits were filed against Robins, Robins had a duty to provide additional disclosure revealing the information. The court agreed, stating: "It is now clear that there is a duty to correct or revise a prior statement which was accurate when made but which has become misleading due to subsequent events."

The court did not discuss whether it believed that Robins's statements were forward-looking statements or factual statements, and it is impossible to decipher from the opinion whether such a distinction would have affected the court's decision. Presumably, since the court did not address the nature of Robins's statements, the duty described by the court would apply to statements of any kind. As the court resolved *A.H. Robins* based upon failure to properly plead fraud, the court's statements regarding this duty to "correct," i.e., update, are clearly dicta. The Second Circuit ultimately agreed with the district court that the plaintiffs failed to adequately plead fraud, but reversed the district court's dismissal, allowing the plaintiffs the opportunity to replead. The Second Circuit specifically declined to discuss whether any duty to provide additional disclosure existed.

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69. See id. at 913.
70. See id. at 906.
71. See id.
72. See id. at 906-07.
73. Id. at 908. The court cites as support A. Jacobs, *The Impact of Rule 10b-5 § 88.04(b)*, at 4-14 and the cases cited therein. See id. Although the court used the term "duty to correct" the court was clearly referring to a duty to update as there is no indication that the plaintiffs had alleged that the statements were inaccurate when made. The court then stated that the duty existed as long as the statement remained "alive" in the market. See id.
74. See id. at 909.
75. See *Ross v. A.H. Robins Co.*, 607 F.2d 545, 559 (2d Cir. 1979).
76. See id. at 559 n.21.
A three-judge panel decision of the First Circuit in *Backman v. Polaroid Corp.* intensified concern that a duty to update might be broadly applied to all types of statements. Polaroid's 1978 third quarter report announced record earnings and sales for the quarter and first nine months of 1978. Polaroid featured its new product, Polavision, on the cover of the report. Expectations for the product were high, but Polavision proved to be a commercial flop. The First Circuit panel held that, although the plaintiffs did not claim any statements made by Polaroid were false or misleading, Polaroid was required to update statements made in the third quarter report once it became apparent Polavision would not be the success Polaroid had previously anticipated.

In a rehearing by the First Circuit en banc, the court withdrew the panel decision and significantly narrowed the scope of the duty to update. The court determined that Polaroid's statements were solely statements of historical fact and were precisely correct at the time they were made. As a result, there was no duty to update the earlier statements regardless of a subsequent change of circumstances. Alas, the First Circuit, much like the district court in *A.H. Robins*, felt compelled to make additional statements not necessary to decide the case. The court stated that:

> Obviously, if a disclosure is in fact misleading when made, and the speaker thereafter learns of this, there is a duty to correct it. In special circumstances, a statement, correct at the time, may have a forward intent and connotation upon which parties may be expected to rely. If this is a clear meaning, and there is a change, correction, more exactly, further disclosure, may be called for.

It is unfortunate that the district court in *A.H. Robins* and the panel decision generated a substantial amount of criticism. See Dennis J. Block et al., *A Post-Polaroid Snapshot of the Duty to Correct Disclosure*, 1991 Colum. Bus. L. Rev. 139, 141 (stating that the panel's decision "appeared to mandate disclosure of all subsequently obtained material facts related to the subject matter of previously disclosed information—even if the previously disclosed information was accurate at the time of the original disclosure . . . ."); Edward Brodsky, *The Duty to Update Information*, N.Y. L.J., Mar. 7, 1990, at 3 (describing the panel decision as "imposing a difficult if not impossible disclosure requirement"); Carl W. Schneider, *Update on the Duty to Update: Did Polaroid Produce the Instant Movie After All*, 23 Rev. Sec. & Commodities Reg. 83, 87-90 (1990) (noting the panel decision "took the updating process to an unworkable extreme").

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78. 910 F.2d 10, 15 (1st Cir. 1990) (en banc).
79. See id.
80. See id. at 16.
81. The panel decision generated a substantial amount of criticism. See Dennis J. Block et al., *A Post-Polaroid Snapshot of the Duty to Correct Disclosure*, 1991 Colum. Bus. L. Rev. 139, 141 (stating that the panel's decision "appeared to mandate disclosure of all subsequently obtained material facts related to the subject matter of previously disclosed information—even if the previously disclosed information was accurate at the time of the original disclosure . . . ."); Edward Brodsky, *The Duty to Update Information*, N.Y. L.J., Mar. 7, 1990, at 3 (describing the panel decision as "imposing a difficult if not impossible disclosure requirement"); Carl W. Schneider, *Update on the Duty to Update: Did Polaroid Produce the Instant Movie After All*, 23 Rev. Sec. & Commodities Reg. 83, 87-90 (1990) (noting the panel decision "took the updating process to an unworkable extreme").
82. Polaroid Corp., 910 F.2d 10 (1st Cir. 1990).
83. See id. at 16-17.
84. See id. This statement by the First Circuit, despite the fact that it is clearly dicta, has become the most frequently cited statement in support of a duty to update forward-looking statements.
decision in *Polaroid* used the term "duty to correct" (now recognized as a duty to update) when discussing the company's disclosure obligations. The duty the plaintiffs urged the courts to accept was analytically no different from a duty to disclose all material information, which was rejected in *Chiarella*. Public companies are required on a regular basis to make factual, historical statements on a wide variety of topics. All material developments represent a change in circumstances from those that existed when previous historical statements were made. Under the analysis used by the district court in *A.H. Robins* and the panel in *Polaroid*, every material development would allow a plaintiff to point to a "misleading" prior statement. As an example, assume a company had a good year in 1999, generating record profits. As required, the company filed a Form 10-K annual report with the Commission, in which it included audited financial statements showing the profit for the year and statements that the company had a "record year" in the MD&A section of its 10-K. Now assume that the company hits hard times in the first quarter of 2000, and prior to the time it is required to file its first quarter 10-Q, the company begins to lose money. The fact that the company is now losing money is undoubtedly material. It is, however, still true that the company was profitable in 1999. If an obligation to disclose all material information existed, the company would have to disclose the fact that it was losing money in the first quarter of 2000 prior to the mandated 10-Q filing date. To claim that the company has no duty to disclose all material information, and then to allow an argument that the losses in 2000 make an earlier true statement "misleading" thereby requiring additional disclosure, is nonsensical. A duty to update historical factual statements is simply a duty to disclose all material information in disguise.

85. See Herbert S. Wander et al., *Developments in Disclosure: Special Problems in Public Offerings—Forward-Looking Information, Including the Private Securities Litigation Reform Act of 1995*, 33 San Diego L. Rev. 1027, 1059 (1996) ("The 'duty to update' theory is a misnomer which threatens to negate the established principle that an independent trigger of a duty to disclose is a distinct element of a Rule 10b-5 action.").


87. The approach taken by the First Circuit in *Roeder v. Alpha Indus., Inc.*, 814 F.2d 22 (1987), can be contrasted with the approach taken by the district court in *A.H. Robins* and the First Circuit panel in *Polaroid*. In *Roeder*, Alpha was sued for failing to disclose that it paid bribes to win a defense department subcontract. *See id.* at 23. As a defense contractor, Alpha was likely required to discuss its compliance with
Following the decision in *Polaroid*, most commentators believed, and most federal courts have held, that a duty to update, to the extent that it exists, applies to forward-looking statements and possibly other non-historical statements. 88 Despite this general agreement, and despite the fact that a duty to update historical factual statements appears inseparable from a duty to disclose all material information, one commentator has suggested that a recent First Circuit decision has imposed a continuous disclosure obligation on any company that files a shelf registration statement, 89 and that a recent Second Circuit case can be read as an attempt to revive a duty to update historical factual statements. 90

In *Shaw v. Digital Equipment Corp.*, 91 Digital filed a “shelf” registration statement with the Commission giving Digital the ability to issue up to one billion dollars of various classes of debt and equity securities. 92 Several months later, Digital filed a prospectus supplement and commenced an offering of securities four days prior to the end of the third fiscal quarter of 1994. 93 The plaintiffs complained that at the time of the offering Digital was aware of, and should have disclosed that it was anticipating a significantly larger loss for the third quarter than was expected by the market. 94 The First Circuit held that the prospectus supplement was deficient because Digital omitted material information. 95 One view holds that by

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89. See Oesterle, *supra* note 7, at 137 (discussing Shaw v. Digital Equip. Corp., 82 F.3d 1194 (1st Cir. 1996)).
91. 82 F.3d 1194 (1st Cir. 1996).
92. See id. at 1200. Under SEC Rule 415, 17 C.F.R. § 230.415, certain large sophisticated companies are permitted to file a registration statement to cover the offering of securities that they reasonably expect may be issued over a two year period with only the barest information concerning the offering. See 17 C.F.R. § 230.415 (1999). The securities are said to be on “the shelf.” When ready to sell the securities, the company files a prospectus supplement, which provides the details regarding the specific securities to be offered, the details of the offering and updated information regarding the company. The securities are then said to be taken down from the shelf and the offering commences.
93. See Shaw, 82 F.3d at 1200.
94. See id.
95. See id. at 1202-03. The plaintiff and the court were really suggesting that the prospective supplement should have been amended or updated to disclose...
requiring the disclosure of management's expectations relative to market expectations, the court in essence was imposing a continuous disclosure requirement for the entire period that the registration statement is outstanding. In fact, the court used the words "continuous disclosure" stating: "[t]he rule permits offerings to be made on a 'continuous' or 'delayed' basis because it envisions 'continuous' disclosure."

The case should, however, be read less broadly. Despite the language in Rule 415 permitting offerings on a "continuous" basis, in reality, most shelf offerings are made periodically and not continuously. A more appropriate reading of the case would require a company selling securities under a shelf registration statement to include all material information through the date of the offering in its registration statement as opposed to simply satisfying its periodic disclosure obligations. The court made clear that Digital was required to disclose information about the quarter in progress not simply because Digital had filed a shelf registration statement, but because it was actually selling securities under the shelf registration statement, and it could have avoided any disclosure requirement by delaying the sale of securities. Instead of imposing a continuous disclosure obligation, Digital represents an application of the insider trading doctrine to the situation of a company selling its securities

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96. See Oesterle, supra note 7, at 142-43.
97. Shaw, 82 F.3d at 1209.
98. Rule 415(a), 17 C.F.R. § 230.415(a) (1999), states that "[s]ecurities may be registered for an offering to be made in the future on a continuous or delayed basis in the future..."
99. Mechanically, a company could include all material information in its registration statement by filing a post-effective amendment, filing a prospectus supplement, stickering the prospective supplement and delivering it to the buyer, or by filing a Form 8-K disclosing the material information (which under the Commission's rules would be incorporated into the registration statement).
100. Digital had argued that it should be under no obligation to disclose any information regarding the current fiscal quarter until its next Form 10-Q was required to be filed with the Commission (which, pursuant to Commission rules, would be automatically incorporated into the registration statement). See Shaw, 82 F.3d at 1209.
101. See id. at 1209 n.20 ("Of course, if the issuer desires not to disclose the information prior to quarter's end, then the flexibility of the shelf registration procedure permits the issuer to 'delay' a planned offering until after the quarter is completed and the results from the quarter are publicly reported."); see also Adoption of Integrated Disclosure System, Securities Act Release No. 6383 [1937-82 Transfer Binder—Accounting Series Releases] Fed. Sec. L. Rep. (CCH) ¶ 72,328, at 63,015 (March 3, 1982) (clarifying the disclosure requirements of a shelf registration prior to an offering). The Commission stated that Rule 415(a)(2), 17 C.F.R. § 230.415(a)(2), and Item 512(a) of Regulation S-K, 17 C.F.R. § 229.512(a), discuss when and how a shelf registration statement is required to be updated, and that the rules made "clear that there is no need to maintain an accurate and current, or 'evergreen,' prospectus when no offers or sales are being made pursuant to the shelf registration." Id.
under a shelf registration statement. Alternatively, the court in Digital could have relied upon Item 303 of Regulation S-K to support the decision that the intra-quarterly information had to be disclosed. Item 303 requires inclusion in a registration statement and periodic filings of any "known trends or uncertainties" expected to have an effect on sales or revenue. To the extent that Digital was aware of an emerging negative trend in earnings in the third quarter, Item 303 would require disclosure of the decline.

In In re Time Warner Inc. Securities Litigation, the Second Circuit, like the district court in A.H. Robins, failed to identify the types of statements that would be subject to the duty to update. The plaintiffs in In re Time Warner claimed that a number of statements made by Time Warner became misleading over time. Some of the statements on which the plaintiffs based their case are clearly forward-looking statements. Other statements were arguably historical.

102. The court analogized the situation in Shaw to that in insider trading cases where an insider or a corporation can avoid any disclosure obligation by refraining from trading. See Shaw, 82 F.3d at 1203-04. It has been argued, however, that the insider trading doctrine does not clearly fit this sort of situation. See Gulati, supra note 14, at 723.

103. Several courts have rejected claims based on Item 303 under the theory that there is no private right of action for failure to comply with Item 303. See, e.g., In re Burlington Coat Factory Sec. Litig., 114 F.3d 1410, 1419 n.7 (3d Cir. 1997) (noting that it is an open issue whether violations of Item 303 create an independent cause of action, but declining to reach the issue); In re Canandaigua Sec. Litig., 944 F. Supp. 1202, 1209 n.4 (S.D.N.Y. 1996) ("It is far from certain that the requirement that there be a duty to disclose under Rule 10b-5 may be satisfied by importing the disclosure duties from S-K 303."). But see Wallace v. System & Computer Tech. Corp., No. 95-CV-6303, 1997 U.S. Dist. LEXIS 14677, at *89 (Sept. 22, 1997) (allowing a 10b-5 claim to proceed predicated upon a violation of Item 303 noting that "disclosures mandated by law are presumably material." (citation omitted)). Item 303, however, need not provide a private right of action. Item 303 serves as a source of a disclosure duty under section 11 of the Securities Act and Rule 10b-5. See Gulati, supra note 14, at 725-26.

104. Gulati, supra note 14, at 725 (emphasis omitted).

105. It has been argued that a claim based upon non-disclosure of intra-period information is really a claim that current period forecasts should have been disclosed (which are not required to be disclosed pursuant to Instruction 7 of Item 303(a)). See id. at 716-17. Professor Gulati, however, makes a strong argument that this confuses unripe hard data with forecasts of full quarter results. See id. at 717. Companies can satisfy Item 303 with disclosure of known intra-period data that suggest an emerging trend, without disclosing forecasts of the full quarter results. See id. Practically, companies may choose to disclose their forecasts of the full quarter in order to satisfy Item 303, but this is not the same as requiring disclosure of forecasts. See id. at 717-18.

106. 9 F.3d 259 (2d Cir. 1993).

107. See supra notes 68-74 and accompanying text.

108. See In re Time Warner, 9 F.3d at 262.

109. Statements that Time Warner "expected" to complete a strategic alliance transaction within a certain time period, and claims by Time Warner that it was seeking strategic alliance partnerships to raise capital became misleading once Time Warner began to consider a stock sale instead of a strategic alliance. See id. at 266.

110. These include Time Warner's statements regarding ongoing talks, which the plaintiff claimed became misleading when such talks did not proceed well. See id. at
The court, however, made no effort to distinguish between the two. In fact, the court suggested in a footnote that the duty to update could apply to historical statements.\textsuperscript{111} Time Warner made statements that talks regarding a strategic alliance partnership were ongoing.\textsuperscript{112} The court stated that “if this factual assertion ceased to be true, [Time Warner] would have had an obligation to update their earlier statements.”\textsuperscript{113} Although the court failed to address whether it intended the duty to update to apply to historical factual statements, the nature of the statement and the fact that the court used the words “factual assertion” suggest that the duty might apply to all types of statements.\textsuperscript{114} To the extent that \textit{In re Time Warner} suggests that a duty to update historical factual statements is different than a duty to disclose all material information, or that the general rule that disclosure of material information is not required absent a duty to speak is no longer good law, \textit{In re Time Warner} stands alone.\textsuperscript{115}

In contrast to a duty to update that would apply to historical factual statements, a plausible basis exists for distinguishing a duty to update forward-looking statements from a duty to disclose all material information. In general, forward-looking statements are not required to be disclosed,\textsuperscript{116} and are made much less frequently. Unlike historical factual statements, a change in circumstances would render a prior forward-looking statement “misleading” only if the change was related to the forward-looking statement. Forward-looking statements, unlike historical factual statements, have been suggested to contain an implicit representation that they will be updated if circumstances change.\textsuperscript{117}

\begin{thebibliography}{9}
\bibitem{267} See id. at 267 n.4.
\bibitem{111} See id.
\bibitem{112} Id.
\bibitem{113} See id.
\bibitem{114} See id.
\bibitem{115} See \textit{Stransky v. Cummins Engine Co.}, 51 F.3d 1329, 1332 n.3 (7th Cir. 1995).
\bibitem{116} The court held: No duty to update an historical statement can logically exist. By definition an historical statement is addressing only matters at the time of the statement. Thus, that circumstances subsequently change cannot render an historical statement false or misleading. Absent a duty to speak, a company cannot commit fraud by failing to disclose changed circumstances, with respect to an historical statement. See id; Gwyn & Matton, \textit{supra} note 39, at 379 (stating that a company “cannot logically be under a ‘duty to update’ a statement of fact”).
\bibitem{117} Certain forward-looking information is required to be disclosed. Item 303 of Regulation S-K, 17 C.F.R. \textsection 229.303 (1999), requires disclosure of presently known trends reasonably expected to effect future sales, earning or liquidity, while disclosure of other forward-looking information is encouraged. See 17 C.F.R. \textsection 229.303, Instruction 7 (1999). The line separating the two is often blurry. See Mark S. Croft, \textit{MD&A: The Tightrope of Disclosure}, 45 S.C. L. Rev. 477, 484-86 (1994).
\end{thebibliography}
The early existence of the duty to update forward-looking statements rested upon the dubious support of *A.H. Robins*, the dicta in *Polaroid*, the Third Circuit opinion in *Greenfield v. Heublein Inc.*, in which the court announced an extremely broad duty to update with no analysis or support, and the Third Circuit's decision in *In re Phillips Petroleum Securities Litigation* in which the duty to update should have been limited to the specific facts in the case.

In several instances, the Commission's rules explicitly require information contained in certain forms and schedules to be updated when circumstances change. For example, under Rule 13d, any person who acquires five percent or more of the outstanding shares of a publicly traded corporation is generally required to file a Schedule 13D. Rule 13d-2 requires the Schedule 13D to be amended "[i]f any material change occurs in the facts set forth in the [statement]."

Importantly, only information contained in specified forms and schedules filed with the Commission, and not all information, is explicitly required to be updated.

material information. Numerous commentators see a duty to update, even if limited to forward-looking statements, to impose a duty to disclose all material information. See Wander, *supra* note 85, at 1059 ("Although a narrower duty to update only 'so-called forward-looking' statements appears more palatable, in practice it would be an unworkable and dangerous precedent.").

118. 607 F.2d 545 (2d Cir. 1979). Although the district court in dicta found a duty to update, the Second Circuit reversed on other grounds and expressly refused to address the issue of a duty to update. See id. at 118.

119. 742 F.2d 751 (3d Cir. 1984).

120. The court in *Greenfield* recited a broad duty to update stating "if a corporation voluntarily makes a public statement that is correct when issued, it has a duty to update that statement if it becomes materially misleading in light of subsequent events." Id. at 758. The court in *Greenfield* was faced with the question of whether Heublein was required to update factual statements. See id. at 755. The NYSE had contacted Heublein regarding unusual trading activity in its stock during the time in which the defendant was involved in merger negotiations with two different parties. See id. at 754. In response to the NYSE request, Heublein stated that it knew of no reason that would explain the activity in its stock. See id. The Third Circuit concluded that as a matter of law the statement was not misleading when made because there had been no agreement in principal regarding a merger. See id. at 759-60. Heublein argued that it was not required to update its statements because the statement spoke only as to activity on the date the statement was made. See id. at 759. The court determined that it did not have to reach the question because at no time during the plaintiff's class period did Heublein reach an agreement in principle. This case was decided before the Supreme Court's decision in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), which rejected the agreement-in-principle test for determining whether merger discussions are material. See id. at 236. Had this case been decided after *Basic*, the court likely would have been forced to decide whether Heublein had a duty to update under these facts.

121. 881 F.2d 1236 (3d Cir. 1989).


123. 17 C.F.R. § 240.13d-2(a).

124. Other examples of various updating requirements include information regarding tender offers contained in a Schedule TO, 17 C.F.R. § 240.14d-6(c), information regarding issuer self-tender offers and going-private transactions
In *In re Phillips*, the plaintiffs sued an entity controlled by T. Boone Pickens for securities fraud based upon statements made in a Schedule 13D filed with the Commission in the course of a hostile tender offer. In the Schedule 13D filing, and in press releases announcing the tender offer, Pickens, who had been paid greenmail following previous hostile tender offers, stated that he would not sell his shares back to Phillips except on the same terms available to all stockholders. Ultimately, Pickens sold back the shares he had acquired at a price significantly higher than that available to the other stockholders. The plaintiffs claimed that once Pickens’ intentions regarding the Phillips shares changed, he was required to communicate his change of intentions. The Third Circuit agreed, stating that “[t]here can be no doubt that a duty exists to correct prior statements, if the prior statements were true when made but misleading if left unrevised.”

The specific language of Rule 13d-2 quite clearly imposes a duty to provide additional disclosure when information in a Schedule 13D filed with the Commission changes, and the rule would have provided a sufficient basis for the court’s holding. Unfortunately, the court failed to clearly confine the duty to “correct prior statements” to those statements made in a Schedule 13D, or to instances when the Commission’s rules clearly require updating. The court’s ruling can be, and has been, read to apply to any statement of intent or forward-looking statement.

Over the ten years following the *Polaroid* decision, the federal appellate courts generally have stated that the duty to update exists.
Despite numerous cases in which the existence of the duty to update was the central issue in the case, and the frequency with which the duty to update has been stated to exist, no cases, however, provide any rationale or basis for imposing a duty to update. In contrast, the Seventh Circuit explicitly has rejected the existence of the duty to update.\textsuperscript{132}

The Third Circuit decision in \textit{Weiner v. Quaker Oats Co.}\textsuperscript{133} represents one of the more blatant examples of a court expressing support for the duty to update without any explanation other than citing to prior precedent. The court held that a statement made by Quaker Oats about the company's general guideline for its debt-to-equity ratio could require updating when Quaker Oats began contemplating an acquisition which, if financed with debt, would materially increase the ratio.\textsuperscript{134} The Third Circuit, citing only \textit{In re Phillips} for its holding, stated that "there can be no doubt" that the duty to update exists.\textsuperscript{135}

The Second Circuit in \textit{In re Time Warner} made equally broad statements as the \textit{Weiner} court with no more explanation. The plaintiffs in \textit{In re Time Warner} alleged that Time Warner, heavily in debt, made statements regarding its efforts to find "international 'strategic partners' who would infuse billions of dollars of capital into the company," but later "misrepresented the status of ongoing partnership discussions and failed to disclose" the stock offering.\textsuperscript{136} The court held: "when a corporation is pursuing a specific business goal and announces that goal as well as an intended approach for reaching it, it may come under an obligation to disclose other approaches to reaching the goal when those approaches are under active and serious consideration."\textsuperscript{137} As described earlier, the \textit{In re Time Warner} Court even failed to describe the types of statements covered by such an obligation, and the statements by the court can be

\textsuperscript{132} See, e.g., Stransky v. Cummins Engine Co., 51 F.3d 1329, 1332 (7th Cir. 1995). The court stated that "[s]ome have argued that a duty to update arises when a company makes a forward-looking statement—a projection—that because of subsequent events becomes untrue.... This court has never embraced such a theory, and we decline to do so now." \textit{Id.} (citations omitted). The court further held that Rule 10b-5 "implicitly precludes basing liability on circumstances that arise after the speaker makes the statement." \textit{Id.} in \textit{Eisenstadt v. Centel Corp.}, 113 F.3d 738 (7th Cir. 1997), the Seventh Circuit went even further, stating that "it is true . . . that in this circuit, and maybe now in all circuits (as a result of the recent amendments to the securities laws), there is no duty to correct a prediction falsified by subsequent events...." \textit{Id.} at 744. The Seventh Circuit, however, has not been entirely consistent. See infra notes 198-207 and accompanying text.

\textsuperscript{133} 129 F.3d 310 (3d Cir. 1997).

\textsuperscript{134} See \textit{id.} at 317.

\textsuperscript{135} \textit{id.} at 316 (quoting \textit{In re Phillips Petroleum}, 881 F.2d 1236, 1245 (3d Cir. 1989)).

\textsuperscript{136} \textit{In re Time Warner}, 9 F.3d at 262.

\textsuperscript{137} \textit{id.} at 268.
interpreted as applying the duty to update even to historical factual statements.\textsuperscript{138}

It appears that recent courts have felt bound by the decisions in \textit{A.H. Robins, Greenfield, In re Phillips,} and \textit{Polaroid} to state that the duty to update exists. Notwithstanding the decisions in \textit{Weiner} and \textit{In re Time Warner,} the federal courts, even when stating that the duty to update exists, have generally found reasons not to impose the duty to update upon the facts in the particular cases at bar. Frequently, the courts have avoided the application of the duty to update by concluding that the forward-looking statement was immaterial, as there can be no duty to update an immaterial statement.\textsuperscript{139} The courts have used three separate approaches to conclude that a statement is not material.\textsuperscript{140}

First, courts have relied on the "bespeaks caution" doctrine. The bespeaks caution doctrine provides that if a forward-looking statement is accompanied by sufficient cautionary language, the statement is immaterial as a matter of law.\textsuperscript{141} In \textit{In re International Business Machines Corporate Securities Litigation,} IBM made several statements concerning its plan to maintain its current dividend levels in the face of mounting losses.\textsuperscript{143} When ultimately forced to cut its dividend payments, the plaintiffs claimed that IBM should have updated its statements once the company realized that its dividend

\begin{itemize}
  \item \textsuperscript{138} See supra notes 106-11 and accompanying text.
  \item \textsuperscript{139} See \textit{In re International Bus. Machs. Corporate Sec. Litig.}, 163 F.3d 102, 110 (2d Cir. 1998).
  \item \textsuperscript{140} There is a significant body of case law concerning whether a forward-looking statement is misleading when made. Cases involving a duty to update have often borrowed from this line of cases. Frequently, the issues arise together, with plaintiffs alleging that a forward-looking statement was misleading when made, or alternatively, if not misleading when made, it “became misleading” at a later time giving rise to a duty to update. See Hillson Partners Ltd. Partnership v. Adage, Inc., 42 F.3d 204, 219 (4th Cir. 1994).
  \item \textsuperscript{141} See \textit{In re Donald J. Trump Casino Sec. Litig.}, 7 F.3d 357, 371-72 (3d Cir. 1993).
\end{itemize}

The court described the doctrine as follows:

> [W]hen an offering document's forecasts, opinions or projections are accompanied by meaningful cautionary statements, the forward-looking statements will not form the basis for a securities fraud claim if those statements did not affect the "total mix" of information the document provided investors. In other words, cautionary language, if sufficient, renders the alleged omissions or misrepresentations immaterial as a matter of law.


\textsuperscript{142} 163 F.3d 102 (2d Cir. 1998).

\textsuperscript{143} See \textit{id.} at 105.
levels could not be maintained.\textsuperscript{144} The Second Circuit concluded that sufficient cautionary language existed to indicate that the statements were only short-term predictions, rendering the statements immaterial.\textsuperscript{145} In \textit{San Leandro Emergency Medical Group Profit Sharing Plan v. Philip Morris Cos.},\textsuperscript{146} the Second Circuit found as a matter of law that statements made by Philip Morris regarding its product pricing strategies were not misleading when accompanied by statements indicating the difficulty in predicting the strategy's impact.\textsuperscript{147}

A second approach courts have taken to find a statement not to be material is to find that clear statements of specific projections are no more than general expressions of optimism, or are simply too vague, to be considered material.\textsuperscript{148} In \textit{In re Burlington Coat Factory Securities Litigation},\textsuperscript{149} a Burlington Coat Factory ("BCF") officer stated that he believed that BCF's net earnings would continue to grow at a rate faster than sales.\textsuperscript{150} The Third Circuit concluded that the statement was a "general, non-specific statement of optimism or hope that a trend will continue."\textsuperscript{151} The court then held that the statement was vague and thus immaterial as a matter of law.\textsuperscript{152} The statement made by BCF appears to have been anything but vague. BCF spoke of two clear, quantifiable concepts, and BCF was equally clear as to the relationship of the two.\textsuperscript{153} Only the rate of growth of either sales or earnings, or the amount earnings growth was expected to exceed sales growth, was unclear.\textsuperscript{154} The simple fact that earnings growth was expected to exceed sales growth, however, would have been particularly important to many investors.\textsuperscript{155}

A third approach courts have taken to avoid finding a statement material is to hold that a projection is immaterial unless worded as a

\begin{footnotesize}
\begin{enumerate}
\item 144. See id. at 109.
\item 145. See id. at 108.
\item 146. 75 F.3d 801 (2d Cir. 1996).
\item 147. See id. at 811.
\item 148. See \textit{In re Time Warner Inc. Sec. Litig.}, 9 F.3d 259, 267 (2d Cir. 1993).
\item 149. 114 F.3d 1410 (3d Cir. 1997).
\item 150. See id. at 1427.
\item 151. Id.
\item 152. See id. at 1427-28. \textit{In re Burlington Coat Factory} has been read as holding that a duty to update applies only when a forward-looking statement concerns fundamental changes in the nature of a company. See \textit{In re Home Health Corp. of America, Inc. Sec. Litig.}, 1999 U.S. Dist. LEXIS 1230, at *55 (E.D. Pa. Jan. 28, 1999).
\item 153. See \textit{In re Burlington Coat Factory}, 114 F.3d at 1427.
\item 154. Id.
\item 155. First, such a statement implies that earnings are expected to grow which is in and of itself material. Second, sales growth rates are generally easier to predict than earnings growth rates, as earnings are affected not only by sales but also by a variety of other factors. If an investor knew that management believed that earnings growth rates would exceed sales growth rates, and if he could predict a company's sales growth (either based on information provided by the company or otherwise), he would be able to approximate management's projections of earnings.
\end{enumerate}
\end{footnotesize}
guarantee. In *IBM*, the Second Circuit, in addition to relying on the bespeaks caution doctrine, stated that the statements by IBM were opinions and not guarantees and therefore were immaterial as a matter of law.156 The court reached this conclusion despite the fact that the statements were undeniably clear. On several occasions, IBM stated that it had no intention of cutting its $1.21 per share dividend.157 The Fourth Circuit has held similarly. In *Hilson Partners Ltd. Partnership v. Adage, Inc.*,158 the plaintiffs alleged that Adage made numerous forward-looking statements predicting record earnings, and that Adage had a duty to update the predictions when the company realized the predicted earnings levels would not be met.159 The court held that predictions of sales growth or earnings projections, even when specifically quantified, were immaterial as a matter of law.160

In addition to relying on concepts of immateriality to avoid application of the duty to update, the courts have also recognized that companies have a legitimate need for confidentiality. In *San Leandro*,161 Philip Morris made statements about its product pricing strategy.162 When Phillip Morris subsequently announced that it was changing its strategy, the plaintiffs sued, claiming Phillip Morris should have updated its earlier statements when it first began to consider changing its strategy.163 The Second Circuit rejected the plaintiffs’ claims stating that it was “concerned . . . about interpreting the securities laws to force companies to give their competitors advance notice of sensitive pricing information.”164

Finally, courts have narrowly construed the scope of the original statement, finding no duty to update if the undisclosed information is outside the scope of the original statement. In *Evanowski v. Bankworcester Corp.*,165 the defendant announced that it had received a cash merger proposal at $22.50 per share.166 The merger was subject to certain conditions, which the defendant was ultimately unable to meet.167 Subsequently, the defendant and the bidder began

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157. See *id.* at 108. The court stated that “[i]t would be unreasonable, as a matter of law, for an investor to rely on these projections as long-term guarantees.” *Id.*
158. 42 F.3d 204 (4th Cir. 1994).
159. See *id.* at 208.
160. See *id.* at 212 (relying on its prior decisions in Rabb v. General Physics Corp., 4 F.3d 286 (4th Cir. 1993) and Malone v. Microdyne Corp., 26 F.3d 471 (4th Cir. 1994)).
161. 75 F.3d 801 (2d Cir. 1996).
162. See *id.* at 805-07.
163. See *id.* at 805.
164. *Id.* at 809-10.
166. See *id.* at 612.
167. See *id.* at 613.
renegotiating at a substantially reduced price. The defendant made several statements that the negotiations were continuing without disclosing that they were discussing a deal on substantially different terms. In a truly strained reading of the original statement the court held that the statement was precisely correct and the fact that the parties were renegotiating core terms of the deal was outside the scope of the original statement. Although the original statement may have remained technically correct, the terms of the renegotiations were substantially different from those described in the original statement.

Cases such as Hillson, IBM and Burlington Coat Factory strongly suggest that the federal courts are attempting to avoid the application of the duty to update, or to so narrow the scope of the duty to update that it will cease to exist. If a duty to update were going to be imposed, the facts of these three cases seemingly presented the best opportunity to apply the duty. Hillson involved clear statements regarding expectations that the company would exceed a specific amount of earnings, IBM involved concrete statements as to expectations of maintaining a specific dividend rate, and Burlington Coat Factory involved specific earnings projections.

The extent to which the courts in Hillson, IBM, and Burlington Coat Factory have gone to avoid the application of the duty to update appears to be the result of their concern for the burdens that would be associated with imposing a duty to update. The Fourth Circuit in Hillson stated:

To require Adage continually to correct and modify its projections would inevitably discourage the types of disclosure the securities laws seek to encourage. . . . Because of the frequency and volatility of these projections, the imposition of a duty to disclose them would have required virtually constant statements by [the issuer] in order not to mislead investors. Under these circumstances, we deem the projection disclosures urged by [appellant] to be impractical, if not unreasonable.

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168. See id.
169. See id.
170. For criticism of the Evanowski decision, see Oesterle, supra note 7, at 185-87.
171. See Evanowski, 788 F. Supp. at 614.
172. Indeed, the Third Circuit, after acknowledging that it had previously found a duty to update in In re Phillips and Greenfield, seemed to suggest that a duty to update might not exist at all. See In re Burlington Coat Factory Sec. Litig., 114 F.3d 1410, 1433-34 (3d Cir. 1997). The court stated that “the duty to update, to the extent it might exist, would be a narrow one.” Id. at 1434 n.20. The court also stated that although they had previously recognized that a duty to update might exist in In re Phillips and Greenfield, they had never clarified the circumstances when it might apply. See id. at 1431-32; see also Hillson Partners Ltd. Partnership v. Adage, Inc., 42 F.3d 204, 219 (4th Cir. 1994) (“Assuming that there can ever be a ‘duty to update,’ there was no such duty here.”).
173. Hillson, 42 F.3d at 219 (alterations in original) (citations omitted) (quoting...
The Fourth Circuit recognized the burdens that an almost continuous disclosure regime would impose on reporting companies.

The Third Circuit has expressed similar concerns regarding the potentially overwhelming burdens corporations would face with a duty to update. In Burlington Coat Factory, a company officer, in addition to stating that he believed that BCF's earnings would continue to grow faster than sales, also expressed comfort with analyst projections of BCF's earnings. The court expressed great concern that if a duty to update was imposed in this case, it would create a continuous duty to update the earning forecasts. The court was not convinced that a single, ordinary, run-of-the-mill earnings forecast contained an implicit representation that the company would update the market with all material information relevant to the forecast. Finally, the court expressed concern that a "judicially created rule that triggers a duty of continuous disclosure . . . would likely result in a drastic reduction in the number of such projections" which would be contrary to the intent of the federal securities laws. The court concluded that for these reasons, a duty to update would not be imposed upon ordinary earnings forecasts.

The concern that the courts have expressed for the burdens associated with a broadly applied duty to update, when combined with the efforts to which the courts have gone to avoid the application of the duty to update, demonstrates that the support for the duty to update is neither firm nor widespread. Cases such as Hillson, IBM, and Burlington Coat Factory beg the question of whether the duty to update should exist at all.

III. ANALYSIS OF THE JUSTIFICATIONS FOR THE DUTIES TO CORRECT AND UPDATE

Part II addressed the courts' reluctance to find the existence of either a duty to correct or a duty to update. Part III of this Article examines existing justifications for the duties, concluding they are scant. Further, a duty to update would be inconsistent with the federal securities laws and a duty to correct superfluous.
A. Duty to Correct

Although acceptance that a duty to correct does and should exist appears to be nearly universal,179 no one has attempted to articulate the purpose of such a duty or why one is needed.180 In order to invoke the duty to correct, a material misstatement must first exist. A material misstatement or material omission made in a registration statement or a prospectus is actionable under section 11 of the Securities Act.181 Issuers of securities are strictly liable for such misstatements or omissions,182 and, therefore, a duty to correct such statements would be superfluous. Any other materially misleading statement or material omission, whether made in an Exchange Act filing, a press release, or a statement made to securities analysts, is actionable under section 10(b) of the Exchange Act and Rule 10b-5, if made with the requisite level of scienter.183 If such a material misstatement is made with scienter, the maker would face liability and there is no need to imply a duty to correct.

The duty to correct has been stated as not really applying in a situation where a company makes an inaccurate statement (i.e., this would be a violation in and of itself) but only "operates simply as a means of limiting existing"184 liability. Under one scenario, however, a

179. See Brill, supra note 39, at 617 ("The courts and authorities have not questioned the existence of this duty to correct."); Hayes, supra note 86, at 953 ("Under 10b-5(2), the corporation clearly has an affirmative duty to correct statements it made that were inaccurate when made." (emphasis added)).
180. But see, e.g., Rosenblum, supra note 9, at 289 (attempting to rationalize the existence of a duty to correct). In discussing the duties to update and correct, Rosenblum states that despite the "near unanimity of courts in acknowledging an issuer's duty to correct ..., relatively few courts have purported to impose liability for the breach of either duty, and few of the cases have attempted to provide a detailed explanation of the bases of those duties." Id. at 314-15.
In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security [may sue] every person who signed the registration statement.
182. See id. All persons other than the issuer have a due diligence defense. See 15 U.S.C. § 77k(b)(3).
183. See Ernst & Ernst v. Hochfelder, 425 U.S. 185, 194-214 (1976) (holding that section 10(b) of the Exchange Act's language embodies a scienter requirement); Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 476 (1977) (stating that the word manipulative in section 10(b) "refers generally to practices ... that are intended to mislead investors by artificially affecting the market activity."). In the context of Rule 10b-5, the federal courts have generally held that it is enough for a company to be aware that a statement was inaccurate and of its propensity to mislead, or to be reckless as to the accuracy of the statement. See SEC v. Falstaff Brewing Corp., 629 F.2d 62, 77 (D.C. Cir. 1980).
184. Cox et al., Securities Regulation: Cases and Materials 714 (2d ed. 1997). By correcting prior inaccurate disclosure, a company would limit the potential class of plaintiffs to those who purchased or sold stock prior to the date of the correction. See id.
duty to correct could potentially serve a purpose. If a company innocently makes a material misstatement, other than in a Securities Act registration statement, no scienter would exist, and no liability would arise. At some later point, if the company realized its error, but failed to correct it, its subsequent failure to correct could potentially be used to provide the missing scienter.\textsuperscript{185}

No cases appear to have addressed the exact fact pattern described above. In \textit{In re MobileMedia},\textsuperscript{186} one of the few cases to actually impose liability for failure to comply with the duty to correct, the court did not address whether scienter existed at the time of the misstatement, and thus whether there was any need to address a duty to correct.\textsuperscript{187}

Whether the discovery of a misstatement with no other action on the part of a company would be sufficient to find scienter is unclear. Merely discovering the inaccuracy is not sufficient.\textsuperscript{188} Some additional action or reason for the company to benefit from failing to correct the misstatement would likely be necessary to find an intent to deceive.\textsuperscript{189} It is not enough that the failure to correct a known misstatement is unfair,\textsuperscript{190} it must also be fraudulent.\textsuperscript{191} In addition, in order to make out a colorable claim of securities fraud, a plaintiff must comply with Rule 9(b) of the Federal Rules of Civil Procedure, which requires that fraud be pleaded with particularity.\textsuperscript{192} If the plaintiff cannot identify a

\textsuperscript{185} See Oesterle, \textit{supra} note 7, at 147-48.

\textsuperscript{186} 28 F. Supp. 2d 901 (D.N.J. 1998).

\textsuperscript{187} Nor did the court address the proper class period, which presumably would begin only when the material misstatement was discovered, as opposed to when the misstatement was originally made. Had the court addressed the issue of the proper class period, it might have been forced to conclude that a plaintiff who purchased a security after the material misstatement, but prior to the time the company learned of the misstatement, would not be entitled to damages because no scienter existed at the time of the misstatement. Additionally, it would have concluded that a later buyer of the same security who purchased her stock after the company learned of the misstatement but failed to correct it would be entitled to damages based upon the material misstatement that caused the loss to both. Imaging that a court would treat two plaintiffs so differently when both were equally harmed by the misstatement is difficult, yet this result would seem to be required by a duty to correct. To see how the court did address the issue, see \textit{In re MobileMedia Securities Litigation}, 28 F. Supp. 901, 923 (D.N.J. 1998).

\textsuperscript{188} See \textit{In re HealthCare Compare Corp. Sec. Litig.}, 75 F.3d 276 (7th Cir. 1996). The Seventh Circuit held that a company could be liable for failure to correct a forward-looking statement but held that the case must be dismissed because the plaintiff failed to sufficiently plead motive and intent. \textit{See id.} at 283.

\textsuperscript{189} See Rosenblum, \textit{supra} note 9, at 318-19 ([A]n issuer who had nothing to gain from an increase or decrease in the price of its securities caused by its breach of a duty to correct or update is less likely to have had the requisite intent to support a Rule 10b-5 violation.").


\textsuperscript{191} \textit{See Dirks v. SEC}, 463 U.S. 646, 654 (1983) ("There must also be manipulation or deception."). (quoting \textit{Santa Fe Indus., Inc. v. Green}, 430 U.S. 462, 472 (1977)).

\textsuperscript{192} \textit{See In re Burlington Coat Factory Sec. Litig.}, 114 F.3d 1410, 1418 (3d Cir. 1997) (stating that a plaintiff must "allege specific facts that give rise to a 'strong
tangible benefit to the company from failing to correct the misstatement, he is unlikely to survive a motion to dismiss. But in many cases where a company would receive such a tangible benefit sufficient to overcome the Rule 9(b) pleading requirements, a remedy would exist without the necessity of resorting to a duty to correct. For instance, if a company were to discover that it had made a material misstatement by underestimating the value of the company or its earning potential, and then proceeded to repurchase its stock without correcting the misstatement, this would clearly be fraudulent. The actions of the company would, however, constitute insider trading under existing case law, making an independent duty to correct unnecessary. Thus, the practical reality is that even in narrow situations where a duty to correct might provide a remedy for a misstatement where one would not otherwise exist, a plaintiff would be unlikely to overcome the Rule 9(b) pleading requirements.

Even if the pleading and scienter requirements are met, a strong argument exists that the language of Rule 10b-5 does not permit examining events that occur after a statement is made. The language of Rule 10b-5 implies that the determination of whether a misleading statement is actionable must be made as of the time the statement was made. The Seventh Circuit in Stransky has espoused this view, in addition to at least one commentator. If statements must be judged at the time they are made, the subsequent discovery of a misstatement cannot be used to provide the scienter missing at the time of the misstatement.

The duty to correct has generally been discussed in the context of historical factual statements. There have recently been arguments made to extend the duty to correct to forward-looking statements. A forward-looking statement that is misleading when made, such as a projection based upon inaccurate data, has been suggested as possibly triggering a duty to correct in addition to any duty to update that might be triggered upon a subsequent change of circumstance. Extending the duty to correct a forward-looking statement that is misleading when made, is extremely troubling. It represents an effort by plaintiffs, aware of efforts by the federal courts to narrow or avoid completely the application of the duty to update, to recharacterize a
duty to update a claim as a duty to correct a claim. The plaintiff's effort to recharacterize a duty to correct is best illustrated by the Seventh Circuit case of *In re HealthCare Compare Corp. Securities Litigation*.\(^{198}\) In early February 1993, HealthCare Compare expressed comfort with analyst projections of its net income for fiscal 1993.\(^{199}\) On February 24, an internal memorandum was prepared that lowered internal estimates of fiscal 1993 revenues and net income.\(^{200}\) At the end of March, HealthCare Compare then expressed discomfort with analysts' estimates.\(^{201}\) When the company's stock price dropped following this statement, the plaintiffs filed suit alleging securities fraud, claiming that HealthCare Compare was required to "correct" the February 1993 statement.\(^{202}\) The plaintiffs also claimed that factual information was available prior to the February expressions of comfort that should have alerted HealthCare Compare that it was not on track to meet analyst expectations.\(^{203}\)

The defendants argued that based upon the Seventh Circuit's earlier decision in *Stransky v. Cummins Engine*, they had no duty to update. The court replied:

> Reliance on *Stransky* is somewhat misplaced. . . . This is not a case where things unexpectedly went wrong; rather, plaintiffs allege that the circumstances which made the comfort statements false . . . arose prior to the statements—even if only realized by HealthCare on February 24.

> Thus we decline to hold that *Stransky* adopted a bright-line rule that no duty to correct exists in any case. Rather, we are persuaded that plaintiffs can only show that a duty to correct arose by alleging facts sufficient to demonstrate that the internal memorandum was certain and reliable, not merely a tentative estimate.\(^{204}\)

The court's decision is somewhat difficult to decipher.\(^{205}\) The court apparently meant that if the data used to arrive at the lower earnings estimate in the February 24th memorandum existed at the time the earlier statement was made, even if the defendant was not aware the data existed or had yet to process the data and arrive at the new lower

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198. 75 F.3d 276 (7th Cir. 1996).
199. See id. at 278.
200. See id.
201. See id.
202. See id. at 278-79.
203. See id. at 279.
204. Id. at 282.
205. Despite the pains taken by the Seventh Circuit in *Stransky* to differentiate between the “duty to correct” and the “duty to update”, the court in *In re HealthCare Compare* misuses the terms. For instance, the court stated that in *Stransky*, it had “declined to find a duty to correct,” despite the fact that the issue in *Stransky* was whether or not to recognize a duty to update. See id. *In re HealthCare Compare* appears to involve a duty to correct because the circumstances giving rise to the plaintiff's allegations arose prior to the forward-looking statements, but were recognized by HealthCare Compare only after the statements were made. See id.
earnings estimate, then the earlier earnings estimate was incorrect and required correction.

The extension of the duty to correct to forward-looking statements suffers from all of the problems previously identified. More importantly, extending the duty to correct to forward-looking statements would in many circumstances serve as a substitute for a duty to update. In a situation where a duty to correct a forward-looking statement would apply, a duty to update, if one exists, would also apply. In jurisdictions that have rejected or limited the duty to update, plaintiffs could simply recharacterize their duty to update claim to allege a duty to correct. For example, assume a situation similar to that in *A.H. Robins*. A company develops a new product that it believes to be safe and effective based upon all research done up to that point, and it issues a press release to that effect. Subsequently, additional research shows that the product is either not as effective as first thought or is in some way dangerous. Obviously, if the product is not now safe and effective, it was not safe and effective when the original statement was made, and it could be argued that the forward-looking statement was incorrect when made and requires correcting. Clearly, if a duty to update exists, it would apply here.

Importantly, in both *In re MobileMedia* and *In re HealthCare* *Compare* the defendant companies corrected their prior misstatements. The plaintiffs were not complaining because the defendants failed to correct their misstatements but because they did not correct their misstatements soon enough. A company’s correction of its misstatement would seem to be the most likely way for a stockholder of the company to learn of the misstatement. The existence of a duty to correct may therefore create a disincentive for a company to correct its errors, because if the company’s stock price drops following the correction, plaintiffs will allege the company must have known about the misstatement at some point prior to the correction.

Ultimately, the creation of the duty to correct is unwarranted. The duty to correct appears to be a remedy in search of a problem. With limited exceptions, when a material misstatement is made, a remedy will exist without the need to create a duty to correct. Even in factual situations where the duty to correct might provide a remedy for a misstatement where one would not otherwise exist, the application of the duty to correct is problematic. The absence of scienter would likely limit the application of the duty to correct in many circumstances, and the language of 10b-5 may preclude the use of the

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206. See supra notes 179-205 and accompanying text.
207. See Harvey L. Pitt et al., *Promises Made, Promises Kept: The Practical Implications of the Private Securities Litigation Reform Act of 1995*, 33 San Diego L. Rev. 845, 857 (1996) ("[I]t takes only a deft keyboard stroke to allege that a duty to update was in fact a duty to correct." (emphasis omitted)).
doctrine altogether. In addition, companies that voluntarily correct their past misstatements, as the defendants did in *In re MobileMedia* and *In re HealthCare Compare*, leave themselves vulnerable to claims that they failed to correct the misstatement soon enough. The limited utility of the duty to correct is outweighed by both the increased litigation risk imposed upon public companies that wish voluntarily to correct their innocent errors and the danger of encouraging the creation of other implied disclosure obligations.

**B. Duty to Update**

Section B discusses the difficulty of complying with the duty to update, and the normative justifications for the duty. The section further addresses the Commission’s stance on the duty to update, traditional doctrine with respect to the duty, and the effect of the Reform Act on the duty.

1. Compliance with a Duty to Update

Compliance with a duty to update places a heavy burden on companies. As previously discussed, if firms were required to update historical factual statements, such a duty to update would be indistinguishable from a requirement to disclose all material information, in essence creating a continuous disclosure requirement. A duty to update forward-looking statements would create a similar continuous disclosure requirement. The problems associated with a continuous disclosure requirement have been extensively discussed in the academic literature.

Two problems are generally recognized as being associated with a continuous disclosure system. First, firms would be required to disclose information that they would prefer not to disclose. Information firms would prefer to keep confidential include

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208. See supra notes 67-86 and accompanying text.
209. The burden on firms would maybe be somewhat less as firms generally make fewer forward-looking statements as compared to the number of historical factual statements. A change of circumstances would not necessarily create a disclosure obligation, as a disclosure obligation would arise only to the extent that a firm had previously made a forward-looking statement related to the change in circumstances, while a change in circumstance would almost always bear upon a previous historical factual statement. But see Wander et al., supra note 85, at 1064 (“Because of the compliance difficulties it presents, acceptance of even a limited duty to update would eviscerate the traditional rule that issuers have no general duty to disclose.”).
211. See generally Mahoney, supra note 210, at 818 (“Disclosure of corporate information also carries the risk of liability.”).
information that harms a firm's competitive balance, such as the existence of preliminary merger discussions where secrecy concerning the transaction may affect a firm's ability to consummate the transaction. Second, a continuous disclosure system would "exacerbate the problems facing a legal system that is already overly litigious." This second problem has been referred to as the "liability cost" of mandated disclosure.

Imposing a duty to update forward-looking statements would impose an even higher liability cost than would a continuous disclosure system that only required disclosure of factual information. A duty to update would do more than just force a corporation to update its prior forward-looking statements once the corporation knew that results were not going to be as predicted. A duty to update would require a company to update its prior statements any time additional information cast doubt on the prior prediction or, if the company were to generate a new prediction, it would cause the corporation to formulate a different prediction. A duty to update may go further and require a company to update its predictions whether or not it actually had gathered and evaluated new information or generated a new prediction. For example, if a corporation in the first week of January released an estimate of its earnings for the full year, the estimate would have to be updated immediately once any new information existed that might change the estimate, even if this change of estimate occurred the following day. In essence, this would create a continuous duty to reevaluate prior predictive statements.

Predictions, to be reasonable, have to be based upon all available information at the time they are made. Most large companies have entire departments dedicated to gathering information on a regular basis and extrapolating that information to make predictions about the future. Because many large companies on a regular and quite frequent basis might develop new predictions, or at least have information available to make new predictions, the required disclosure of forward-looking statements could truly become continuous and require up-to-the-minute updating.

Trends are easy to spot in hindsight. They are not so easy to see when they happen in real time. When a previously successful company later falls on hard times, it is easy to look back at various points and suggest that the company should have recognized that the tide was beginning to turn. In a continuous disclosure system, it is plaintiffs who look back and say that the company should have told

212. Oesterle, supra note 7, at 191. Professor Oesterle characterizes these concerns as specious because such concerns assume that it is impossible to design a continuous disclosure system that would be without exceptions, and with which private litigation would be unimpeded. See id. at 188-89. Given our current system, even Professor Oesterle agrees that such concerns are legitimate.

213. See Mahoney, supra note 210, at 817-19.
them lean times were coming. Management, continually in the maelstrom, must examine each new data point to determine if it represents a departure from the past and from what is expected. For plaintiffs in subsequent litigation, the question becomes: What did you know and when did you know it?

When the continuous disclosure obligations are applied to forward-looking statements, the minutia become even more important to management in determining when they have a disclosure obligation, because the problem is not one of deciding whether there is enough new information to determine that a change is in the offing, but whether there is enough information that would justify a new and different prediction. For the plaintiffs in subsequent litigation, the question becomes: What did you believe, and when did you believe it?

Even if companies were to update their prior predictions, determining when to update would still be a daunting task. Determining materiality almost always involves difficult judgment calls. If disclosure obligations are tied to discrete points in time or to the occurrence of specified events, companies face a limited number of difficult disclosure decisions. In a continuous disclosure system, the number of difficult disclosure decisions is multiplied exponentially, with each decision subject to being second guessed in subsequent litigation.214

Take, for example, a small oil and gas exploration company, for which each new well is a material event. Part of the nature of energy exploration is that its ultimate success or the degree of success of a well may not be known for years after it is drilled, and as a result almost any information disclosed about a well will have a forward-looking component. In the absence of a duty to update, the exploration company, unless it was required to file a quarterly or annual report or was in the process of selling its securities, could choose the point or points at which to disclose information about the progress of the well. The company would likely choose to make disclosures at points at which it felt it had sufficient information to make an educated guess as to the prognosis of the well. It is not unusual for the prognosis of a well to change many times throughout the drilling and testing process. If a duty to update were to apply, the company would have to update its statements with each change in

214. See In re Burlington Coat Factory Sec. Litig., 114 F.3d 1410, 1432 (3d Cir. 1997) (stating that BCF would be subjected to a “continuous duty to update the public with either forecasts or hard information that would in anyway change a reasonable investor’s perception of the originally forecasted range”); Hillson Partners Ltd. Partnership v. Adage, Inc., 42 F.3d 204, 219 (4th Cir. 1994) (“Because of the frequency and volatility of these projections, the imposition of a duty to disclose them would have required virtually constant statements by [Adage] in order not to mislead investors. Under these circumstances, we deem the projection disclosures urged by [plaintiffs] to be impractical, if not unreasonable.” (quoting Walker v. Action Indus., 802 F.2d 703, 710 (4th Cir. 1986))).
prognosis. Each new prediction may only be marginally more likely to prove true than the prior prediction. The predictions may change from optimistic to pessimistic and back again and again.

A different disclosure problem is illustrated by the *Weiner*\(^{215}\) and *San Leandro*\(^{216}\) cases. In *Weiner*, Quaker Oats had on several occasions announced that its guideline for leverage would be to maintain a total debt-to-total capitalization ratio in the upper 60% range.\(^{217}\) At some point, Quaker Oats began negotiating to acquire Snapple, and ultimately reached an agreement to acquire Snapple for 1.07 billion. Quaker Oats financed the acquisition entirely through new debt, which raised its debt-to-equity ratio to approximately 80%.\(^{218}\) The plaintiffs sued Quaker Oats for failing to update its guideline for its debt-to-equity ratio when it became apparent that the impending acquisition of Snapple would significantly raise its leverage ratio.\(^{219}\)

In *San Leandro*, the plaintiffs sued Philip Morris after it announced that it was cutting the price of its Marlboro cigarettes.\(^{220}\) The plaintiffs claimed that the price cut represented a change in pricing strategy and that Philip Morris should have disclosed that its was considering the change in strategy.\(^{221}\)

Importantly, although the plaintiffs' claims in *Weiner* and *San Leandro* were couched as a failure to update prior statements, the defendants did update their predictions. Furthermore, it was the market's adverse reaction to the update that led to the lawsuit. Instead, plaintiffs were actually claiming that the predictions were not updated soon enough. What the plaintiffs in *Weiner* and *San Leandro* really wanted was for the companies to disclose the potential negative effects of a change in corporate strategy at the point the change came under consideration. In effect, they wanted disclosure of the effect on prior statements of potential future decisions prior to such decisions even being made.

2. What Statements Require Updating?

Even if a duty to update does not apply to historical statements, it can still be quite difficult to determine what statements require updating. Determining whether a statement is factual, or whether it has a forward-looking connotation is not always clear. Often, a statement involves both factual aspects and expectations for the

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215. 129 F.3d 310 (3d Cir. 1997).
216. 75 F.3d 801 (2d Cir. 1996).
217. See Weiner v. Quaker Oats Co., 129 F.3d 310, 313 (3d Cir. 1997).
218. See id.
219. See id. at 314.
221. See id.
future.\textsuperscript{222} Recall the situation in \textit{In re Time Warner}. Time Warner made statements that it was engaged in negotiations with a number of parties regarding a strategic alliance, and that it would complete a transaction within a certain time period that would involve a substantial capital infusion.\textsuperscript{223} These facts gave the court a fair amount of difficulty. Surely, part of the statements were forward-looking, such as the expectation as to the results of the negotiations or the time period for completing the transaction. But, parts of the statements were also purely factual. Time Warner stated that discussions were ongoing,\textsuperscript{224} which seems to be a statement of pure fact that is verifiable. If a statement is partially forward-looking, must a company update the entirety of the statement, even the factual portion?

To complicate matters further, some commentators have suggested that categories of statements in addition to historical factual statements and forward-looking statements may also require updating.\textsuperscript{225} Substantial uncertainty exists as to how soft information that does not fall within the definition of forward-looking statements in Rule 175 and the Reform Act should be treated.

A "statement of intent" has been suggested to be a category of statement separate from a forward-looking statement.\textsuperscript{226} Unfortunately, determining exactly what a statement of intent is or how it differs from a forward-looking statement is impossible. The Third Circuit in Phillips first described a statement of intent.\textsuperscript{227} The statements at issue were made in a Schedule 13D which described the filer's intent regarding the shares of stock it had acquired, as required by the Item 4 of Schedule 13D.\textsuperscript{228} Rule 13d-2 explicitly requires the Schedule 13D to be updated if the information changes. In holding that the information in the Schedule 13D had to be updated, the court failed to base its decision solely on Rule 13d-2, and the idea that statements of intent occupy some separate category of statement has

\begin{itemize}
\item \textsuperscript{222}See Stephen J. Schulte, \textit{Corporate Public Disclosure: Primer for the Practitioner}, 15 Cardozo L. Rev. 971, 984 (1994) ("There simply is no 'bright line' test between initially accurate statements which should be updated and those which need not be."); Wander, \textit{supra} note 14, at 1064 ("To distinguish statements of present fact from purely speculative and forward-looking disclosure is practically impossible.").
\item \textsuperscript{223}See \textit{In re Time Warner Inc. Sec. Litig.}, 9 F.3d 259, 262 (2d Cir. 1993).
\item \textsuperscript{224}See id. at 262-63.
\item \textsuperscript{225}See \textit{infra} notes 226-30.
\item \textsuperscript{226}See \textit{Stransky v. Cummins Engine Co.}, 51 F.3d 1329, 1332 n.4 (7th Cir. 1995) ("We express no opinion on whether the outcome would be the same if a plaintiff contested statements of intent to take a certain action."); Gwyn & Matton, \textit{supra} note 39 at 367 (suggesting that even if the Reform Act eliminated the duty to update for forward-looking statements, companies would still be required to update statements of intent).
\item \textsuperscript{227}See \textit{In re Phillips Petroleum Sec. Litig.}, 881 F.2d 1236, 1245 (3d Cir. 1989).
\item \textsuperscript{228}See \textit{id.} at 1239.
\end{itemize}
been perpetuated ever since. There is no analytical reason to treat statements of intent differently than forward-looking statements, and it seems clear that a statement of intent would fall within the definitions of forward-looking statement provided in Rule 175 and the Reform Act.

While the definition of a forward-looking statement in Rule 175 and in the Reform Act is broad, some types of soft information exist that would not be included. Possibly the largest category of soft information potentially outside the statutory definition of forward-looking statement are opinions. A good example is the statements made in *A.H. Robins*.

In *A.H. Robins*, the company stated that its birth control device was safe and effective, which later proved to be untrue. *A.H. Robins* has sometimes been cited as a duty to correct case, while other times it has been described as supporting a duty to update. How a court currently would evaluate the statements claimed to have been made by Robins is not clear. The statements cannot easily be categorized as a historical statement of fact. The statements are not descriptions of prior events, nor are they statements of fact such as sales volume, the veracity of which can readily be tested. On the other hand, the statements do not clearly make a projection as to the future as does an estimate of future sales. The statements are really opinions based upon known information, and later known information may or may not force a change of that opinion. Such opinions, however, share important similarities with forward-looking statements. The passage of time or the change of circumstances may not allow the opinion to be repeated without being misleading. It appears that what Robins meant to say was: “based upon all available scientific evidence, we currently believe the device is safe and effective and we expect that the device will ultimately be proven to be safe and effective.” Had Robins rephrased its statements in this way they would have clearly been forward-looking statements. Statements that have the same qualities as forward-looking statements, at least with respect to a duty to update, should be treated as other forward-looking statements, whether or not they fall within the definition of a forward-looking statement in Rule 175 or the Reform Act.

229. The Third Circuit later noted that Rule 13d-2 was the source of the duty to update in *In re Phillips*. See *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1433-34 (3d Cir. 1997).


232. See id. at 906.

233. Under current case law, it may not matter whether the statements made in *A.H. Robins* were factual or forward-looking. If the statements were factual, they may be viewed to have been incorrect when made, thus triggering a duty to correct. If the statements were forward-looking, they “became” misleading, thus triggering a duty to update.
Examining whether normative concerns justify the creation of a duty to update requires revisiting the general rule, which states that there is no duty to disclose all material information, and that there can be no liability for non-disclosure absent a duty to speak. As described earlier, a duty to update cannot be applied to historical factual statements without repealing the general rule. Thus, if the general rule is accepted, a duty to update, if it does exist, can only apply to forward-looking statements. The question then is whether there is a normative reason to justify creating an exception to the general rule that would require updating forward-looking statements.

Several reasons have been identified for treating forward-looking statements differently from historical factual statements. First, it is argued that the investment community reasonably expects that when a corporation makes projections, the corporation will assume the burden of updating the projections if circumstances change. For the investment community's expectations to be reasonable, however, they must be based upon the current regulatory structure—existing law and the federal court's interpretation of the law. The Burlington Coat Factory court described the regulatory structure as including: (1) the general rule that companies are not required to disclose all material information; (2) the well-settled principal that accurate reports of past success do not imply future success; and (3) the general desire on the part of the Commission to encourage forward-looking statements.

Given the current regulatory structure and the inconsistencies in recent federal court decisions, identifying any reasonable expectations regarding a duty to update is difficult. With all the efforts to narrow or avoid the application of the duty to update, possibly the only forward-looking statement that the investment community could reasonably expect corporations to update is one worded as a guarantee and related to an action that could cause a fundamental
change to the company, provided that the company both explicitly stated that it would update the statement and identified how long it intended to provide updates.\textsuperscript{241}

A second reason promulgated for treating forward-looking statements differently from historical factual statements rests upon the hypothesis that companies have vastly superior information about the company. Because corporations allegedly possess an information advantage, investors take projections very seriously, the projections provide a tempting vehicle for fraud.\textsuperscript{242} The serious regard of investors for projections might justify careful scrutiny of projections in general. No apparent connection exists, however, between preventing fraud and imposing a duty to update forward-looking statements. Whether the failure to update a forward-looking statement would provide any more opportunity for fraud than the failure to disclose any other material information is unclear. And, the failure to update a forward-looking statement does not lead to fraud unless the investment community would expect the company to update forward-looking statements, the company is aware of the expectation, and the company intentionally withholds updates to its advantage. In addition, where a company intends to take advantage of its failure to update a forward-looking statement, a remedy would generally be available for such fraud without the need to create a duty to update.\textsuperscript{243}

Third, the different treatment of forward-looking statements has been justified by suggesting that forward-looking statements contain an implicit representation by the maker that the statements will be updated if circumstances change. The implicit representation argument appears to have its genesis in the often-quoted dicta in \textit{Polaroid}: “We may agree that, in special circumstances, a statement, correct at the time, may have a forward intent and connotation upon which parties may be expected to rely. If this is a clear meaning, and there is a change, correction, more exactly, further disclosure, may be called for.”\textsuperscript{244} The court’s statement in \textit{Polaroid} has somehow evolved from a limitation on when a duty to update might arise—only when

\textsuperscript{241} This is the type of statement that might pass muster under the combined approaches by the courts in \textit{In re Burlington Coat Factory}, \textit{Hillson}, \textit{IBM}, and \textit{Polaroid}. Of course, no such forward-looking statements are ever made.

\textsuperscript{242} See Oesterle, \textit{supra} note 7, at 151; \textit{see also} Brill, \textit{supra} note 39, at 672 (noting that because “the duty to update does provide the public with some protection against fraud, courts may continue to recognize the duty”). Brill does not, however, discuss how the duty to update provides such protection.

\textsuperscript{243} For example, assume that a company makes a forward-looking statement and fails to update it when circumstances change. The company then sells shares of its stock in the market. In that case, the company is trading in its securities while in possession of undisclosed material information. The company would be liable for securities fraud under a theory of insider trading. Alternatively, any registration statement prepared in connection with the sale of the stock would be materially deficient and would subject the company to liability.

\textsuperscript{244} Backman v. \textit{Polaroid Corp.}, 910 F.2d 10, 17 (1st Cir. 1999) (emphasis added).
there is a clear statement that a company intends to update a forward-looking statement,\textsuperscript{245} to a justification for imposing the duty—the duty is justified because it is implicit in forward-looking statements that a company will update them.\textsuperscript{246} Absent an express statement of an intention to update, nothing inherent in forward-looking statements implies such an intent to update.\textsuperscript{247}

Two additional arguments have been put forward in favor of a duty to update. First, the fiduciary duty a corporation owes to its stockholders should give rise to a duty to update.\textsuperscript{248} Second, a policy argument suggests that a duty to update is warranted to insure that markets receive all necessary information to prevent distortion of prices,\textsuperscript{249} or is warranted because the duty to update supports the full disclosure goal of securities laws.\textsuperscript{250} The problem with both of these arguments is that each equally supports a duty to update historical factual statements. Without some additional basis to explain why forward-looking statements should be subject to a duty to update but historical factual statements should not, these arguments alone are not sufficient to justify imposing a duty to update forward-looking statements.

The inability to distinguish why a duty to update should be imposed on forward-looking statements but not on historical factual statements is highlighted by the anomalous outcome of the following example. Assume that two companies, Alpha Company and Beta Company, each make the following statements on January 1:

Alpha Company: We are not involved in any negotiations regarding a material acquisition.

Beta Company: We do not plan to make any material acquisitions this year.

The statement by Alpha Company is a factual statement. The

\textsuperscript{245} See Carl W. Schneider, \textit{The Uncertain Duty to Update—Polaroid II Brings a Welcome Limitation}, 4 Insights 2, 10 (1990) (arguing that \textit{Polaroid} may require an intent to induce or exploit an investor’s expectation that a company will update a statement if circumstances change).

\textsuperscript{246} See Rosenblum, \textit{supra} note 9, at 317 (“A forward-looking statement may become misleading as a result of subsequent events because such a statement, by its terms, purports to remain valid beyond the date it was made.”).

\textsuperscript{247} See \textit{In re Burlington Coat Factory Sec. Litig.}, 114 F.3d 1410, 1432-33 (3d Cir. 1997) (“[T]he market knows that companies have neither a specific obligation to disclose internal forecast nor a general obligation to disclose all material information . . . . [F]orecasts contain no more than the implicit representation that the forecasts were made reasonably and in good faith.” (citations omitted)); Bruce A. Hiler, \textit{The SEC and the Courts’ Approach to Disclosure of Earnings Projections, Asset Appraisals, and Other Soft Information: Old Problems, Changing Views}, 46 Md. L. Rev. 1114, 1116, 1126 (1987) ("[O]nly truly factual elements involved in a projection are the implicit representations that the statements are made in good faith and with a reasonable basis.").

\textsuperscript{248} See Rosenblum, \textit{supra} note 9, at 294-97.

\textsuperscript{249} See id. at 315.

\textsuperscript{250} See Brill, \textit{supra} note 39, at 615.
statement by Beta Company has a forward-looking component. Now assume that on February 1, both Alpha Company and Beta Company each enter into negotiations regarding a material acquisition. Since the statement made by Alpha Company is not a forward-looking statement, as long as the statement was correct when first made, Alpha Company would have no duty to provide any additional information regarding its acquisition plans. Conversely, because the statement made by Beta Company has a forward-looking component, Beta Company would now be required to update its earlier statement if a duty to update exists. At a minimum, Beta Company would have to disclose that its expectations regarding material acquisitions over the coming year had changed. It may also be required to disclose additional details about its acquisition plans to ensure that its statement informing the public that its acquisition plans had changed would not be misleading. Beta Company would have to make such disclosures despite the fact that no acquisition has been consummated and despite the significant possibility that no acquisition will result from the current negotiations.

Following February 1, if either Alpha Company or Beta Company repeated the statement they made on January 1, such a statement would be misleading and could subject either company to liability. Following February 1, the stockholders of each company are in the same position. Each company is involved in ongoing negotiations regarding a material acquisition, and the stockholders of each company would presumably have the same amount of interest in knowing about such negotiations. No justification exists for holding Beta Company liable for not disclosing unquestionably material information when Alpha Company would not incur liability for withholding the same information.

4. The Commission’s Stance on the Duty to Update

Assertions that the Commission supports the duty to update have provided support for the judicial recognition of the duty.\(^251\) At least at one point, the Commission clearly believed that companies had a duty to update forward-looking statements.\(^252\) The Commission’s views

\(^{251}\) See Rosenblum, supra note 9, at 312 (“Commission pronouncements concerning an issuer’s duty to correct and to update its misleading statements generally support the imposition of those duties on issuers.”).


[T]he Commission reminded issuers of their responsibility to make full and prompt disclosure of material facts, both favorable and unfavorable, where management knows or has reason to know that its earlier statements no longer have a reasonable basis. With respect to forward-looking statements of material facts made in relation to specific transactions or events (such as proxy solicitations, tender offers, and purchases and sales of securities),
concerning forward-looking statements in general, however, have changed dramatically over the last thirty years.\textsuperscript{253} Until the early 1970's, the Commission prohibited the disclosure of forward-looking statements.\textsuperscript{254} It felt that such information was "inherently unreliable" and that "unsophisticated investors would place undue emphasis on the information."\textsuperscript{255} In response to severe criticism\textsuperscript{256} the Commission began to change its views.\textsuperscript{257}

By the mid-1970's, the Commission had come to regard the disclosure of forward-looking information as critical to the

there is an obligation to correct such statements prior to consummation of the transaction where they become false or misleading by reason of subsequent events which render material assumptions underlying such statements invalid. Similarly, there is a duty to correct where it is discovered prior to consummation of a transaction, that the underlying assumptions were false or misleading from the outset.

Moreover, the Commission believes that, depending on the circumstances, there is a duty to correct statements made in any filing, whether or not the filing is related to a specified transaction or event, if the statements either have become inaccurate by virtue of subsequent events, or are later discovered to have been false and misleading from the outset, and the issuer knows or should know that persons are continuing to rely on all or any material portion of the statements.

Id. at 81,943 (citation omitted).

\textsuperscript{253} See generally Gwyn & Matton, \textit{supra} note 39, at 366 ("[T]he SEC has significantly expanded the role of forecasts, predictions, and projections in the last twenty-five years . . . ."); Hiler, \textit{supra} note 247, at 1116 ("[T]he SEC's policy on disclosure of soft information has undergone significant revision over the last ten years."); Janet E. Kerr, \textit{A Walk Through the Circuits: The Duty to Disclose Soft Information}, 46 Md. L. Rev. 1071, 1072 (1987) ("[T]he SEC policy on [soft information disclosure] can only be described as one in rapid transition."); Joel Seligman, \textit{The SEC's Unfinished Soft Information Revolution}, 63 Fordham L. Rev. 1953, 1953 (1995) ("[T]he SEC has shifted its emphasis from historical information to its current emphasis on forward-looking information.").


\textsuperscript{256} See, e.g., Homer Kripke, \textit{The SEC, the Accountants, Some Myths and Some Realities}, 45 N.Y.U. L. Rev. 1151, 1198 (1970) (characterizing the Commission's views as "nonsense").

The Commission began to recognize that most investment decisions were based upon estimates of future performance and that a corporation's management was best qualified to make such projections.

In 1979, with the goal of encouraging the disclosure of projections and other forward-looking information, the Commission adopted Rule 175 under the Securities Act and Rule 3b-6 under the Exchange Act. The new rules provided a safe harbor for forward-looking statements, but only if the statements were made or reaffirmed in documents filed with the Commission. In the release adopting Rule 175 and Rule 3b-6, the Commission expressed its views that a duty to update forward-looking statements did and should exist. The Commission did not, however, discuss the source of this duty or any justification for its imposition. More important, the Commission did not, as part of the new rules, explicitly impose a duty to update forward-looking statements.

The safe harbor for forward-looking statements generated a substantial amount of criticism. In general, critics complained that the safe-harbor was too narrow to provide sufficient comfort to corporations to induce them to issue forward-looking statements. In 1994, the Commission published a concept release soliciting comments regarding the safe-harbor. The concept release also contained numerous proposals for new regulatory text submitted by various commentators, which would have broadened the safe-harbor.

The Commission acknowledged that a significant criticism of the safe harbor involved confusion over whether a duty to update

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259. See Kripke, supra note 256, at 1199.

260. See 17 C.F.R. §§ 230.175, 240.3b-6 (1999).

261. See 17 C.F.R. § 230.175(b)(1); 17 C.F.R. § 240.3b-6(b)(1).

262. See supra note 252 and accompanying text.


264. See id.

265. See id. at 85,778.

266. See id. at 85,782.
forward-looking statements existed, and if it did, the circumstances under which it would be applied.\textsuperscript{267} The Commission specifically sought comment as to whether a duty to update should exist, and whether the safe harbor for forward-looking statements should specifically eliminate any duty to update.\textsuperscript{268} One of the proposals included in the concept release, submitted by the Business Roundtable and the National Association of Manufacturers, eliminated any duty to update unless a corporation specifically and contemporaneously undertook to update the statement.\textsuperscript{269} Shortly after the publication of the concept release, Congress passed the Reform Act,\textsuperscript{270} which contained a number of the proposals discussed in the release. Whether because of passage of the Reform Act or because of internal dissension regarding broadening the safe harbor, the Commission has not taken any further action. At a minimum, however, it seems clear that the Commission considered eliminating the duty to update. Given the statements in the 1994 concept release, the Commission's support of the duty to update can no longer be assumed.

5. Traditional Doctrine

The principal argument favoring the creation of a duty to update is one that is sometimes unstated, but appears to be implicit both in federal court decisions stating that a duty to update exists and in the arguments of commentators supporting the duty. The argument is that a forward-looking statement, even if not misleading when made, becomes misleading or inaccurate over time when circumstances change.\textsuperscript{271} The argument seems to draw support from the rejection of a duty to update historical statements. A duty to update historical statements was rejected as illogical, because historical statements by definition speak only to a specific point in time, and nothing in the nature of a historical statement suggests a promise that circumstances will not change.\textsuperscript{272} Thus, no duty to update historical statements can

\textsuperscript{267} See id. at 85,792.

\textsuperscript{268} See id.

\textsuperscript{269} See id. at 85,794.


\textsuperscript{271} See Weiner v. Quaker Oats Co., 129 F.3d 310, 316 (3d Cir. 1997); Rubinstein v. Collins, 20 F.3d 160, 170 n.41 (5th Cir. 1994) ("We note that, at least facially, it appears that defendants have a duty under Rule 10b-5 to correct statements if those statements have become materially misleading in light of subsequent events." (emphasis added)); Backman v. Polaroid Corp., 910 F.2d 10, 17 (1st Cir. 1990); Greenfield v. Heublein, Inc., 742 F.2d 751, 758 (3d Cir. 1984); Gwyn & Matton. \textit{supra} note 39, at 377 (describing a duty to update as a duty to "update statements that are "correct when made, but which become materially misleading due to subsequent events"); Rosenblum, \textit{supra} note 9, at 289.

\textsuperscript{272} See Stransky v. Cummins Engine Co., 51 F.3d 1329, 1332 n.3 (7th Cir. 1995) ("By definition an historical statement is addressing only matters at the time of the statement. Thus, that circumstances subsequently change cannot render an historical
exist because historical statements cannot become misleading. Those supporting a duty to update forward-looking statements seem to argue that because a forward-looking statement speaks to the future, and not to a definite point in the past, a forward-looking statement can become misleading over time when circumstances change. This argument is seriously flawed.

Inherent in the nature of predictions is the reality that many, if not most, forward-looking statements will prove to be poor predictions, and the events foretold will not come to pass.273 As time passes following the making of a forward-looking statement, and as events unfold, new information will be gained. As new information is gained, a different prediction will often be more reasonable. Obviously, if the maker of the original forward-looking statement were to repeat the statement in light of this new information, the repeated forward-looking statement would be misleading, as the maker would no longer have a reasonable basis for making the forward-looking statement. This fact alone, however, is insufficient to render the original forward-looking statement misleading or inaccurate. Unless a forward-looking statement is repeated or deemed to be repeated, a forward-looking statement that was not misleading when made does not become misleading simply because new information exists suggesting that the prediction may not come true.274 Nothing inherent in the nature of a forward-looking statement suggests that it should be interpreted as continually repeated over time.275 A forward-looking statement is no

273. The Seventh Circuit has stated that "predictions of future performance are inevitably inaccurate because things almost never go exactly as planned." In re HealthCare Compare Corp. Sec. Litig., 75 F.3d 276, 281 (7th Cir. 1996) (quoting Arazie v. Mullane, 2 F.3d 1456, 1468 (7th Cir. 1993)).

274. See Kitch, supra note 210, at 808 n.141. Professor Kitch suggests that an appropriate defense to a duty to update claim would be to argue that the forecasts were correct as of the date they were provided and that there was no suggestion that the forecasts would remain correct and no promise to update the forecasts when they became "obsolete." See id.

275. There may be at least one situation in which a forward-looking statement would be deemed to be continually repeated. Companies now commonly place forward-looking statements on their web site. Moreover, the forward-looking statements are often not dated. In such cases, it would seem reasonable to deem the forward-looking statement to be repeated each time it was accessed. Investors encountering undated forward-looking statements would be entitled to assume that the statement represented management's current view of the future. Nonetheless, such a company would not be subject to a duty to update, at least not in the classic sense. Instead of facing liability for failure to update a previous forward-looking statement, such a company would instead face potential liability for making a material misstatement under existing doctrine. For a thorough discussion of the Internet and related disclosure obligations, see Robert A. Prentice, The Future of Corporate Disclosure: The Internet, Securities Fraud, and Rule 10b-5, 47 Emory L.J. 1 (1998).
different from a historical statement in that both are made as of a particular point in time. Although obviously different in temporal orientation, a forward-looking statement simply predicts the future based on the information that exists at the time the statement is made.

Assume, for example, that HighTech Company earned one dollar per share for the first fiscal quarter of 1999. The statement is either true or false. If true, it is always true, and the statement, if repeated six months or six years later, is still true when repeated. On the other hand, assume that HighTech Company makes the statement that it expects to earn one dollar per share in the 1999 fiscal year. When made the statement is neither true or false. It is simply a prediction, and it may be a good or bad prediction. Once the fiscal year ends, the accuracy of the prediction will be known. Prior to the end of the fiscal year, however, and prior to conclusively knowing the fiscal year's results, it is likely that one month, or even one week or one day following the original prediction, HighTech Company will have further information about its sales, future orders, and expenses for the current fiscal year, which will likely affect its predictions of earnings for the fiscal year. HighTech Company now likely has a new earnings prediction. The fact that HighTech Company might at a later date make a different prediction does not mean that the original prediction is false, or even misleading. It was just a bad prediction, as are most predictions.

The argument in favor of a duty to update has a circular nature. A duty to update is necessary because without such a duty a forward-looking statement becomes misleading when circumstances change. But such a forward looking statement misleads only if one is entitled to rely on it. And one is only entitled to rely on it if there is a duty to update it.

Even if a forward-looking statement becomes misleading over time, the literal language of Rule 10b-5(b) does not permit the examination of events that occur after a statement is made to determine whether the statement is misleading. Rule 10b-5(b) makes it unlawful to omit a material fact necessary to make statements that are made not misleading "in light of the circumstances under which they were made," implying that the determination of whether a statement is misleading must be made at the time it is made. The Seventh Circuit in Stransky has espoused this view, as have several commentators.

276. It could also be misleading when made, if the prediction was not honestly believed when made or if there was no reasonable basis for making the prediction.

277. See Stransky, 51 F.3d at 1332 ("The rule implicitly precludes basing liability on circumstances that arise after the speaker makes the statement.").

278. See Rosenblum, supra note 9, at 307; Carl W. Schneider, Duty to Update: Does a Snapshot Disclosure Require the Commencement of a Motion Picture?, 3 Insights 3, 6 (Feb. 1989) (imposing a duty to update "requires a very strained reading of Rule 10b-5").
It is axiomatic that in order for there to be liability under Rule 10b-5(b), there must first be a misleading statement or omission. Thus, there can be no liability under Rule 10b-5(b) for failure to update a forward-looking statement, because there is no misleading statement.

6. Effect of the Reform Act

Numerous commentators and even the Seventh Circuit have questioned whether a duty to update, if it did in fact exist, survived the enactment of the Reform Act. One of the Reform Act’s primary purposes was to encourage the publication of forward-looking statements. Congress perceived that a fear of litigation based upon unrealized projections restricted corporate management. The Reform Act, among other things, creates a statutory safe-harbor for

279. Santa Fe Indus. Inc. v. Green, 430 U.S. 462, 472 (1977) (applying the terms “manipulative” and “deceptive” in section 10b of the Exchange Act conditioned upon there being a misstatement or omission of a material fact; an allegation of unfair conduct is insufficient).

280. It is possible that the failure to update a forward-looking statement could be considered a “device, scheme, or artifice to defraud” under Rule 10b-5(a) or an “act, practice, or course of business which operates or would operate as a fraud or deceit upon any person” under Rule 10b-5(c). See Rosenblum, supra note 9, at 307 (citing 17 C.F.R. § 240.10b-5(a), (c) (1990)). This would, however, only shift the analysis from a question of whether there was a misleading statement to one of whether failing to update a forward-looking statement is fraudulent. Rosenblum argues that a company’s knowing failure to update can be considered fraud because the company’s shareholders may be deceived into paying too much for its securities. See id. at 306-07. This only begs the questions of how a previously made forward-looking statement that was not misleading when made can be deceptive, and how the failure to update a forward-looking statement can be fraudulent when the failure to disclose other material information is not fraud.


282. See Rosen, supra note 281, at 646 (“The single greatest impetus to passage of the Reform Act was the perception—amply supported by the evidence—that issuers had been deterred from making projections and from disseminating soft information because of a fear of liability if their public statements failed accurately to predict the future.”).

forward-looking statements. Under the Reform Act, a forward-looking statement cannot be the basis for liability if either the plaintiff fails to prove that the forward-looking statement was made with actual knowledge that it was inaccurate, or if the forward-looking statement is identified as such and is accompanied by cautionary statements indicating factors that may affect the outcome of the events predicted by the forward-looking statement.

The debate over the effect of the Reform Act has centered on a curious provision, which states that "[n]othing in this section shall impose upon any person a duty to update a forward-looking statement." Some commentators have argued that this language suggests Congressional intent to eliminate the duty to update, and that the language has no meaning otherwise, because safe-harbors by definition do not impose or create any additional duties. A few district courts have agreed. Others have argued that such language has no effect on the duty to update. Congress could have easily eliminated the duty to update if elimination was its intent. Read literally, the Reform Act only says that the Reform Act shall not create a duty to update. The Act does not indicate an intention to eliminate any duty to update that may have existed independently from the Reform Act. As such, the better argument is that this section of the Reform Act does not have any impact on the duty to update. The analysis, however, is not over.

First, the courts and commentators who have supported a duty to update have described the duty as arising when a forward-looking statement “become[s] materially misleading” as a result of changed circumstances. In essence, such courts and commentators are using

286. See John C. Coffee, Jr., The Future of the Private Securities Litigation Reform Act: Or, Why the Fat Lady Has Not Yet Sung, 51 Bus. Law. 975, 992 (1996) (stating that Congress’s “statement borders on the tautological”); Julia B. Strickland & Mary D. Manesis, Litigating a Safe Harbor: The Private Securities Litigation Reform Act of 1995 and the Bespeaks Caution Doctrine, at 157 (PLI/Corp Practice Course Handbook Series No. 147, 1996) (“This provision may make the statutory safe harbor particularly attractive to defendants in Circuits which have recognized a duty to update forward-looking statements.”); Wander, supra note 14, at 330 (“[T]he Reform Act implies that the duty to update no longer exists.”).
287. See In re Advanta Corp. Sec. Litig., 180 F.3d 525, 536-37 (3d Cir. 1999) (citing the Reform Act, the court stated that the defendant was under no duty to update); Karacand v. Edwards, 53 F. Supp. 2d 1236, 1245, 1253 (D. Utah 1999) (same).
288. See Brill, supra note 39, at 651 (“However, one can make an equally strong argument that the safe harbor does not reject the judge-created duty to update.”); Cochran & McCoy, supra note 278, at 17; John C. Coffee, Jr., Safe Harbor for Forward-Looking Statements, N.Y. L.J., Nov. 30, 1995, at 5 (“[The Reform Act] would seem to leave that duty unchanged and intact. Had Congress wanted to say that the maker of a forward-looking statement is under no duty to update, notwithstanding any contrary interpretation, it could have easily so provided. Instead, it appears to have compromised ambiguously.”).
289. See supra note 271 and accompanying text.
the forward-looking statement as the basis for liability. The explicit language of the Reform Act, however, does not allow this. In providing a safe harbor for forward-looking statements, the Reform Act provides that if a forward-looking statement meets the requirements of the safe harbor, no person shall be liable with respect to any forward-looking statement in any "private action... that is based on an untrue statement of a material fact or omission of a material fact necessary to make the statement not misleading."\(^{290}\)

Second, in creating the safe harbor, Congress has in essence codified the bespeaks caution doctrine.\(^{291}\) The bespeaks caution doctrine holds that contemporaneous cautionary statements can counteract the effect of a forward-looking statement in the overall mix of information, and can render a forward-looking statement immaterial as a matter of law.\(^{292}\) Although the Reform Act does not explicitly state that forward-looking statements are rendered immaterial by accompanying cautionary statements, the similarity between the safe harbor and the bespeaks caution doctrine suggests that Congress intended this effect. If the forward-looking statement is immaterial as a matter of law, logically, no duty to update the statement exists.\(^{293}\)

Of course, even if the Reform Act were interpreted as eliminating the duty to update, it would only apply to those forward-looking statements that fit the statutory definition. Soft information and opinions that do not fit the Reform Act definition of a forward-looking statement would be unaffected by the Reform Act. In addition, even if a statement satisfied the Reform Act's definition of a forward-looking statement, if it did not qualify for the safe harbor's protection, it could still be subject to a duty to update if one exists.

Although the Reform Act would not literally eliminate a duty to update those forward-looking statements that do not fall within the provision of the Reform Act, eliminating the duty to update entirely would seem consistent with the goals of the Reform Act. In addition to encouraging the publication of forward-looking statements, the Reform Act represents an attempt to replace the post hoc inquiry into "what a company knew and when it knew it" that is inherent in determining whether a forward-looking statement was misleading when made (i.e., was the forward-looking statement honestly believed

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291. See In re Home Health Corp. of America, Inc. Sec. Litig., No. 98-834, 1999 U.S. Dist. LEXIS 1230, at 6 (E.D. Pa. Jan. 29, 1999) (referring to the Reform Act as the corollary of the judicially created bespeaks caution doctrine); Karacand v. Edwards, 53 F. Supp. 2d at 1243 ("In enacting the Reform Act, Congress created a statutory version of the bespeaks caution doctrine."); see also Rosen, supra note 281, at 662 (observing that the Reform Act "codified" the bespeaks caution doctrine).
292. See supra notes 141-47 and accompanying text.
PUBLIC COMPANY DISCLOSURE

and was there a reasonable basis for making the forward-looking statement), with a more objective test: were there also cautionary statements made contemporaneously with the forward-looking statement. Eliminating a duty to update would further the goal of encouraging the publication of forward-looking statements and it would eliminate the need for any post hoc analysis.

IV. A NEW APPROACH TO ANALYZING FORWARD-LOOKING STATEMENTS

For a variety of reasons, a large number of companies that make forward-looking statements choose to update them. Certainly, many companies have been advised by their counsel that while there is uncertainty about the duty to update, they should update lest they find themselves sued in a jurisdiction that recognizes the duty to update. Other companies probably update their forward-looking statements because they believe that it is good business, recognizing that the market places a value on timely information, and may reward companies that voluntarily provide useful market information.

Two situations exist in which companies should be required to provide additional information regarding their prior forward-looking statements, not because the prior statements have become misleading, but to prevent their current statements from being misleading. First, as previously described, companies are required to disclose a substantial amount of information, both periodically and episodically. In addition, many companies voluntarily provide additional information to the public and to securities analysts. When companies are required to speak or do so voluntarily, they must speak truthfully. Companies must also comply with what is known as the "half truth" rule, which requires that they also disclose any additional information necessary to prevent their statements, while literally true, from being misleading "in light of the circumstances under which they were made."

The language, "in light of the circumstances under which they were made."

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294. See Rosen, supra note 281, at 646 ("Congress crafted a new rule that, it was thought, would enable judges to dismiss cases without inquiring into the state of mind of the defendants or the reasonableness of the assumptions underlying the forward-looking statement itself.").

295. See supra notes 1-2 and accompanying text.

296. See Virginia Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1098 (1991) (holding that literally accurate statements can be actionable if they are no more than half-truths); see also Oesterle, supra note 7, at 143 (labeling the doctrine relating to corporate culpability for providing misleading but technically accurate information the "half-truth" rule).

297. 17 C.F.R. § 240.12b-20 (1999); see 15 U.S.C. § 77q(a)(2) (1994) (covering any statement made in connection with the offer or sale of a security); 17 C.F.R. § 230.408 (same); id. § 240.10b-5(b) (covering all other statements).
made, should be read to include a company's prior forward-looking statements. This would require a company to consider its prior forward-looking statements when it has an obligation to speak or does so voluntarily. If circumstances have changed since the forward-looking statements were made, additional disclosure may be required to prevent the current statements from being misleading.

For example, assume that a company in the first quarter of its fiscal year makes a predictive statement about its earnings for the full year. When that company makes its next quarterly 10-Q filing or next discusses its expected earnings in a press release or with securities analysts, such a filing or statement should be viewed in light of the company's prior predictive statement. To the extent that the company has new information that casts doubt on the prior predictive statement, the company should be required to include such information to ensure its 10-Q, press release, or analyst statement is not misleading.

Item 10(b) of Regulation S-K supports the interpretation that a company in possession of new information regarding prior predictive statements should be required to disclose the additional information if required to speak or does so voluntarily. Regulation S-K contains the specific requirement of the disclosures required to be included in the episodic reports. Item 10(b) describes the Commission's policy on projections, and states that the Commission encourages the use of projections in documents filed with the Commission. Item 10(b) also contains guidelines to be considered in formulating and disclosing projections. Specifically, Item 10(b) states:

With respect to previously issued projections, registrants are reminded of their responsibility to make full and prompt disclosure of material facts, both favorable and unfavorable, regarding their financial condition. This responsibility may extend to situations where management knows or has reason to know that its previously disclosed projections no longer have a reasonable basis.

At first blush, this statement might suggest a continual duty to update prior projections. Regulation S-K, however, applies only to registration statements filed under the Securities Act and periodic and episodic reports filed under the Exchange Act. As such, Item 10(b) suggests a duty of companies to review, and possibly to provide additional disclosure, relative to their prior predictive statements, to prevent their registration statements and periodic and episodic reports from being misleading.

Second, Item 303 of Regulation S-K may provide the functional

298. 17 C.F.R. § 240.12b-20.
299. Id. § 229.10(b).
300. Id. § 229.10(b)(3)(iii).
301. See id. § 229.10(a).
302. Id. § 229.303.
equivalent of a duty to update forward-looking statements. Item 303 requires the disclosure, in registration statements, and periodic and episodic reports, of: "known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the [company's] liquidity increasing or decreasing in any material way,"303 "known material trends, favorable or unfavorable, in the [company's] capital resources,"304 and "known trends or uncertainties that have had or that the [company] reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations."305

Item 303 has been described as requiring the disclosure of "hard information about the current or immediate past that might materially change an investor's perception of the company's future."306 In order for a set of facts to represent a trend, it would have to represent a departure from what has occurred previously, or from what management expects to occur, which may be shown by a company's prior forward-looking statements.

Where a developing trend coincides with the subject of a prior forward-looking statement, Item 303 may provide the functional equivalent of a duty to update by requiring a company to disclose the change in circumstances. For example, assume, as in the previous example, that early in the year, a company makes a prediction about its earnings for the full year, and further assume that the earnings prediction is consistent with the company's historical earnings growth rate. Now assume that when the company makes its next quarterly 10-Q filing, it has information about its future sales or expenses, such as the termination of a long-term contract or a contractual increase in labor costs, suggesting that it is unlikely that it will reach its earnings forecast for the full year. Under such circumstances, Item 303 requires disclosure of the hard data that suggest the emerging trend. As a practical matter, companies may choose instead to satisfy their Item 303 obligations by updating their prior forward-looking statement.

The Commission has, in at least one instance, taken this position. In In re Caterpillar, Inc.,307 Caterpillar made statements to securities analysts that it believed that its 1990 net income would be at least as

303. Id. § 229.303(a)(1).
304. Id. § 229.303(a)(2)(ii).
305. Id. § 229.303(a)(3)(ii). For additional discussion of Item 303, see supra notes 103-05 and accompanying text.
306. Gulati, supra note 14, at 728.
high as the prior year.308 By the time Caterpillar filed its 10-Q for the first quarter of 1990, and possibly at the time the Caterpillar filed its 10-K for 1989, the corporation knew there was grave doubt about its ability to meet its earnings estimate for 1990.309 Nonetheless, Caterpillar did not revise its previous forecast until June 25, 1990.310 If the Commission believed that Caterpillar had a duty to update, this would have been a perfect opportunity to pursue enforcement action. Instead, the Commission claimed that Caterpillar's periodic reports were misleading as a result of its failing to comply with the requirements of Item 303.311 Caterpillar ultimately settled with the Commission and agreed to cease and desist from violating the Exchange Act.312

The distinction between this Article's approach to forward-looking statements and a duty to update is important. The duty to update focuses on prior statements, and the effect current developments have on such prior statements. With a duty to update, a company's prior statements "become misleading" when circumstances change. On the other hand, the approach of this Article focuses on current statements and uses the company's prior statements to place its current statements in context. Under this Article's approach, a company's current statement may be misleading if it fails to disclose a change in circumstances from those that existed at the time of its previous predictive statements.

The Article's framework is consistent with the goal of requiring full disclosure of material information without placing an unreasonable burden on companies. A company would be required to examine its prior predictive statements only when required to speak or when it chose to do so voluntarily. Corporations would not be required to continually monitor all prior predictive statements to determine whether they still honestly believed their predictions or whether the statements still had a reasonable basis. In addition, freeing companies from the burden of continually monitoring their prior predictions would eliminate much of the disincentive companies face in making forward-looking statements. This Article's framework encourages investors to place a proper weight on predictive statements: they are management's best guess about the future and not a guarantee as to the ultimate outcome, or a promise that management will provide

309. At its April 11, 1990 board of directors meeting, senior management discussed problems it was having with its Brazilian subsidiary, the likelihood that profits in Brazil would be substantially lower in 1990 than 1989 and the potential effect that would have on overall 1990 earnings. See id. at 63,051-52.
310. See id. at 63,052.
311. See id. at 63,055-56.
312. See id. at 63,056.
minute-by-minute updates as to all developments. Subsequent to the predictive statement, investors should not assume that circumstances will not change.

CONCLUSION

Despite more than twenty years of interpretation by the federal courts, there is still much confusion over the duties to correct and update. Much of the responsibility for this confusion lies with the Supreme Court. The Court, in Chiarella, stated: "[w]hen an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak." The unfortunate aspect of this statement is that it has encouraged plaintiffs and the federal courts to look for implied duties to speak where they have never been found to exist previously. What the Court should have said is that "absent an explicit duty to speak under the federal securities laws," there can be no fraud for non-disclosure.

The explicit disclosure requirements of the federal securities laws are detailed and extensive, and the task public companies face in complying with the explicit disclosure requirements is daunting. To the extent that Congress or the Commission believes that the current comprehensive disclosure system is insufficient, each has ample authority to fill the gap. The general anti-fraud rules should not be used to craft implied duties punishing those corporations that comply with all express disclosure requirements but fail to provide the potentially limitless amount of information desired by investors.
