MVA Litigation Client Advisory Update
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Judge Refuses to Dismiss SEC Action Against RPM International and Its General Counsel Alleging Loss Contingency Disclosure Failures

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On Friday September 29, 2017, U.S. District Judge Amy Berman Jackson denied the motions to dismiss filed by RPM International, Inc. and its general counsel, Edward Moore. Memorandum Opinion at 2, *SEC v. RPM Int'l, Inc.*, No. 16-1803 (ABJ), 2017 U.S. Dist. LEXIS 160997, at *4 (D.D.C. Sept. 29, 2017).

Judge Jackson concluded the SEC's allegations stated plausible fraud claims against RPM and Moore and RPM and Moore had failed in their duty to disclose and accrue for a Department of Justice investigation pursuant to generally accepted accounting principles, in particular Accounting Standards Codification ("ASC") 450. *Id.* at 2, 23, 29, 2017 U.S. Dist. LEXIS 160997, at *34-*35, *43.

THE COURT'S CONCLUSIONS

Judge Jackson agreed with the SEC that the whistleblower's *qui tam* action filed against RPM constituted an *asserted* claim that under ASC 450-20-50 had to be disclosed as a loss contingency if there was at least "'a reasonable possibility' that a loss may be incurred, even if the amount cannot be reasonably estimated." *Id.* at 24, 26-27, 2017 U.S. Dist. LEXIS 160997, at *36, *39-*40; *see also* ASC 450-20-50-2. And, the SEC sufficiently alleged RPM and Moore knew or should have known of this reasonable possibility because by October 2012 they knew about the *qui tam* action, had estimated RPM's liability, and had been in communication with the DOJ about its estimated amount. *Id.* at 29, 2017 U.S. Dist. LEXIS 160997, at *42-*43.

The court also ruled that even if the *qui tam* action were considered an *unasserted* claim against RPM, ASC 450 disclosure guidelines would require disclosure because by October 2012, DOJ had "'manifested' an 'awareness of a possible claim' by issuing subpoenas and engaging in communications with RPM and RPM's counsel" related to the action. *Id.* at 27, 2017 U.S. Dist. LEXIS 160997, at *40 (quoting ASC 450-20-50-6).

Importantly, with attention to the impact of *Omnicare, Inc. v. Laborers Dist. Council Constr. Indus. Pension Fund*, 135 S. Ct. 1318 (U.S. 2015), the court rejected the defendants' argument that the disclosures in RPM's Q1 and Q2 2013 SEC filings that described RPM's process of accruing

loss contingencies and the financials that reflected those judgments applying the ASC 450 "subjective accounting standard" were statements of opinion and, therefore, could not be false or misleading. *Id.* at 35-40, 2017 U.S. Dist. LEXIS 160997, at *52-*61. The court held RPM's omission of facts known about the *qui tam* case would make those opinion statements actionably misleading under the objective standard of the perspective of a reasonable investor. *Id.* at 37-38, 2017 U.S. Dist. LEXIS 160997, at *56-*57. And, characterizing the statements as opinions did not insulate RPM from the conclusion RPM's statements about contingencies "did not rest on meaningful inquiry, and did not fairly align with the facts known at the time." *Id*.

The court dismissed as "beside the point" RPM's argument that it did not have a duty to disclose or accrue for the DOJ investigation because ASC 450 does not require the disclosure of contemplated settlement offers. *Id.* at 29, 2017 U.S. Dist. LEXIS 160997, at *43-*44.

The court refused to hold that any alleged misrepresentations were immaterial even if, as argued by RPM, its eventual disclosure did not negatively impact its stock price. *Id.* at 33-35, 2017 U.S. Dist. LEXIS 160997, at *49-*52.

Judge Jackson found "unpersuasive" Moore's argument that the SEC had failed to demonstrate that he had acted unreasonably in the exercise of his judgment evaluating RPM's obligations to disclose at the time. *Id.* at 51, 2017 U.S. Dist. LEXIS 160997, at *76-77. Indeed, considering Moore's communications with RPM's auditors and his approval of the reports filed with the SEC, the court found the SEC sufficiently alleged Moore had indirectly or directly caused RPM's records to be falsified. *Id*.

CONCLUSION

Judge Jackson's decision demonstrates that at least some courts will be receptive to arguments by the SEC that companies are required to make early disclosure of loss contingencies based upon their internal evaluations, privileged or not. The SEC's aggressive posture, including the allegations of fraud for failing at the time an accrual was taken and reported to disclose it should have been done in a prior quarter, has to be in the mix when considering a disclosure or accrual.

If you have any questions about or would like to discuss this Client Advisory, please contact James P. McLoughlin, Jr. or Neil T. Bloomfield in Moore & Van Allen's White Collar, Regulatory Defense, and Investigations team.