Clients&FriendsMemo

COVID-19 Update: Anticipating Securities Litigation in Response to the Pandemic

April 16, 2020

As COVID-19 has continued to spread globally, U.S. and foreign markets have been dramatically impacted, leading to the largest declines in stock prices since the 2008 credit crisis.[1] Given the extreme market volatility associated with the ongoing COVID-19 pandemic, a significant rise in stock-drop securities litigation seems likely. This is particularly so given the pre-existing trend of increased securities class action filings, even before the onset of COVID-19.[2] Indeed, investors already have filed at least two civil suits alleging that a public company violated the federal securities laws by making misleading public statements concerning COVID-19.[3] Others almost surely will follow.

This memorandum provides an overview of event-driven securities litigation, including the tools employed by the plaintiffs' bar in response to previous crises, and offers guidance for mitigating the risk of COVID-19-based securities litigation, including key defensive strategies for dismissing event-driven securities litigation at the pleading stage.

Background: Event-Driven Securities Litigation Based on Allegations of Material Misrepresentations or Omissions

While the circumstances presented by COVID-19 are unprecedented, the plaintiffs' bar is likely to draw on the same tools employed in prior crises. Under Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") and Rule 10b-5 promulgated thereunder, a plaintiff may seek

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1 *See, e.g.*, Gunjan Banerji, Anna Isaac & Joanne Chiu, *U.S. Stocks Drop Despite Fed's Latest Stimulus Move*, Wall St. J., https://www.wsj.com/articles/global-stock-markets-dow-update-3-23-2020-11584925602 (Mar. 23, 2020, 4:38 PM); Gunjan Banerji, *Stocks Suffer Biggest Weekly Losses Since 2008*, Wall St. J., https://www.wsj.com/articles/more-markets-head-toward-correction-territory-as-coronavirus-spooks-investors-11582864550 (Feb. 28, 2020, 6:36 PM).

2 *See* Cornerstone Res., *Securities Class Action Filings: 2019 Year in Review* at 3 (2020), https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2019-Year-in-Review.pdf ("Unlike in earlier years with heightened levels of filings (*e.g.*, at the time of the dot-com bust or the financial crisis), the current peaks have occurred despite a lack of financial market turbulence."). During 2019, plaintiffs filed 428 federal securities fraud class actions, surpassing 2017's record high of 413. This was nearly double the average number of filings over the past two decades. There were more than 1,200 filings from 2017 to 2019—a number that accounts for nearly 25% of all of the filings in the more than 20 years since 1997. *Id.* at 44.

3 *See* Complaint, *Douglas v. Norwegian Cruise Lines*, No. 1:20-cv-21107-RNS (S.D. Fla. Mar. 12, 2020), ECF No. 1; Complaint, *McDermid v. Inovio Pharm., Inc.*, No. 2:20-cv-01402-GJP (E.D. Pa. Mar. 12, 2020), ECF No. 1.

damages from a company and its directors and officers for a material misrepresentation or omission in connection with the purchase or sale of a security.[4] Additionally, under Section 20(a) of the Exchange Act, a plaintiff may bring suit against an entity or individual that controls the primary securities violator.[5] A plaintiff may also bring suit against an issuer under Sections 11 and 12 of the Securities Act of 1933 (the "Securities Act") for materially misleading misstatements or omissions in a registration statement or prospectus,[6] claims that, unlike 10b-5 claims, do not require the plaintiff to prove "scienter," or fraudulent intent.[7] In support of such claims, plaintiffs may also allege noncompliance with Item 303 of Regulation S-K, which requires the disclosure of "any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations," although the viability of a private right of action under Item 303 remains the subject of a circuit split.[8]

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4 *See* 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b-5. To state a claim under Section 10(b) of the Exchange Act and Rule 10b-5, a plaintiff must plead "(1) a material misrepresentation or omission by the defendant[,] (2) scienter[,] (3) a connection between the misrepresentation or omission and the purchase or sale of a security[,] (4) reliance upon the misrepresentation or omission[,] (5) economic loss[,] and (6) loss causation." *Stoneridge Inv. Partners, LLC v. Sci.-Atlanta, Inc.*, 552 U.S. 148, 157 (2008).

5 *See* 15 U.S.C. § 78t(a). Rule 12b-2 provides that control may be established by showing that the defendant possessed "the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise." 17 C.F.R. § 240.12b-2; *see also S.E.C. v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1472-73 (2d Cir. 1996) (affirming the district court's conclusion that the CEO and owner of First Jersey Securities was personally liable under Section 20(a) of the Exchange Act given his hands-on management of the firm).

6 *See* 15 U.S.C. §§ 77k, 77l. To state a claim under Section 11(a) of the Securities Act, a plaintiff must plead that: "(1) she purchased a registered security, either directly from the issuer or in the aftermarket following the offering; (2) the defendant participated in the offering in a manner sufficient to give rise to liability under section 11; and (3) the registration statement '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.'" *In re Morgan Stanley Information Fund Secs. Litig.*, 592 F.3d 347, 358-59 (2d Cir. 2010); *see also* 15 U.S.C. § 77k(a). To state a claim under Section 12(a)(2) of the Securities Act, a plaintiff must plead that "(1) the defendant is a 'statutory seller'; (2) the sale was effectuated 'by means of a prospectus or oral communication'; and (3) the prospectus or oral communication 'include[d] an untrue statement of a material fact or omit[ted] to state a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading.'" *In re Morgan Stanley*, 592 F.3d at 359 (quoting 15 U.S.C. § 77l(a)(2)).

7 *See Herman & MacLean v. Huddleston*, 459 U.S. 375, 382 (1983) (under Section 11, "[l]iability against the issuer of a security is virtually absolute, even for innocent misstatements"); *Fed. Housing Fin. Agency v. Nomura Holding Am., Inc.*, 104 F. Supp. 3d 441, 568 (S.D.N.Y. 2015) ("Section 12(a)(2) imposes strict liability for statements that are materially false."). However, Section 12(a)(2) provides for a "defense of reasonable care," which is "less demanding than the duty of due diligence" under Section 11, and which may be asserted by all "sellers" under Section (a)(2), including the issuer of a security. *In re WorldCom, Inc. Sec. Litig.*, 346 F. Supp. 2d 628, 663 (S.D.N.Y. 2004).

8 17 C.F.R. § 229.303(a)(3)(ii); *see Stratte-McClure v. Morgan Stanley*, 776 F.3d 94, 107-08 (2d Cir. 2015) (recognizing private cause of action); *Oran v. Stafford*, 226 F.3d 275, 287-88 (3d Cir. 2000) (no private cause of action); *In re NVIDIA Corp. Sec. Litig.*, 768 F.3d 1046, 1054-56 (9th Cir. 2014) (no private cause of action). In June 2018, the U.S. Supreme Court dismissed a petition to resolve the issue, leaving the circuit split intact. *See Ind. Pub. Ret. Sys. v. SAIC, Inc.*, 818 F.3d 85 (2d Cir. 2017), *cert. dismissed*, 138 S. Ct. 2670 (2018).

These provisions have all been utilized in the past by plaintiffs in event-driven stock-drop litigation concerning events such as the 2008 financial crisis,[9] the 2014 Ebola outbreak,[10] the BP oil spill,[11] the early 2000s internet bubble,[12] the California energy crisis,[13] the #MeToo movement,[14] and data breaches resulting in theft of confidential or sensitive information.[15] Presumably, event-driven stock-drop suits will factor prominently in the COVID-19 litigation landscape as well. As summarized below, securities litigation premised on similar theories has already begun to materialize in response to COVID-19.

Recently Filed COVID-19 Securities Litigation

At least two cases have been filed alleging violations of Sections 10(b) and 20(a) of the Exchange Act with regard to COVID-19: *Douglas v. Norwegian Cruise Lines* in the U.S. District Court for the Southern District of Florida, and *McDermid v. Inovio Pharmaceuticals, Inc.* in the U.S. District Court for the Eastern District of Pennsylvania.[16]

In *Norwegian Cruise Lines*, a putative class of shareholders asserted claims under Sections 10(b) and 20(a) against the cruise line and several of its officers, alleging that the defendants deceived investors through public statements in Forms 8-K and 10-K filed with the SEC touting the company's positive outlook for the coming year and its preventative measures in response to COVID-19.[17] In public statements included in its Form 8-K filing in February 2020, for instance,

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9 *See, e.g.*, *Police Ret. Sys. of St. Louis v. Intuitive Surgical, Inc.*, No. 10-CV-03451-LHK, 2012 WL 1868874, at *9 (N.D. Cal. May 22, 2012) (securities litigation triggered by statements regarding the company's ability to sustain growth in light of the 2008 financial crisis), *aff'd,* 759 F.3d 1051 (9th Cir. 2014).

10 *See, e.g.*, *Jackson v. Halyard Health, Inc.*, No. 16-CV-05093-LTS, 2018 WL 1621539, at *4-5 (S.D.N.Y. Mar. 30, 2018) (securities litigation triggered by statements made in relation to the Ebola outbreak), *appeal docketed*, No. 19-1300 (2d Cir. May 1, 2019).

11 *See, e.g.*, *In re BP p.l.c. Sec. Litig.*, 922 F. Supp. 2d 600, 624-25 (S.D. Tex. 2013) (securities litigation triggered by an oil company's statements concerning its risk management system's ability to address the BP oil spill).

12 *See, e.g.*, *In re Merrill Lynch & Co. Res. Reps. Sec. Litig.*, 568 F. Supp. 2d 349, 351-52 (S.D.N.Y. 2008) (securities litigation triggered by positive research reports on an internet holding company despite the company's severe liquidity problems following the burst of the internet bubble).

13 *See, e.g.*, *In re Calpine Corp. Sec. Litig.*, 288 F. Supp. 2d 1054, 1085-86 (N.D. Cal. 2003) (securities litigation triggered by power company's public statements concerning the cause of the California energy crisis).

14 *See, e.g.*, *Constr. Laborers Pension Tr. for S. Cal. v. CBS Corp.*, No. 18-CV-7796 (VEC), 2020 WL 248729, at *13 (S.D.N.Y. Jan. 15, 2020) (securities litigation triggered by statements made at industry event regarding the #MeToo movement and company's knowledge of problems of workplace sexual harassment).

15 *See, e.g.*, *In re Equifax Inc. Sec. Litig.*, 357 F. Supp. 3d 1189, 1216 (N.D. Ga. 2019) (securities litigation triggered by statements made regarding company's cybersecurity and efforts to protect consumer data).

16 *See* Complaint, *Douglas v. Norwegian Cruise Lines*, No. 1:20-cv-21107-RNS (S.D. Fla. Mar. 12, 2020), ECF No. 1; Complaint, *McDermid v. Inovio Pharm., Inc.*, No. 2:20-cv-01402-GJP (E.D. Pa. Mar. 12, 2020), ECF No. 1.

17 *See* Complaint ¶¶ 18-21, *Douglas v. Norwegian Cruise Lines*, No. 1:20-cv-21107-RNS (S.D. Fla. Mar. 12, 2020), ECF No. 1.

Norwegian Cruise Lines stated that "[d]espite the current known impact from COVID-19 coronavirus outbreak, as of the week of February 14, 2020, the Company's booked position remained ahead of prior year and at higher prices on a comparable basis."[18] In making such statements, the plaintiffs allege that: (1) Norwegian Cruise Lines failed to disclose the potential impact of COVID-19 on its business, operations, and prospects; and (2) the Company failed to disclose questionable sales tactics, motivated by the desire to hit sales quotas and designed to conceal the risks of COVID-19 to customers.[19] Such sales tactics allegedly included managers "ask[ing] sales staff to lie to customers about COVID-19 to protect the company's bookings" and instructing sales staff to inform potential customers that COVID-19 "has caused a huge surge in demand" for all of the other non-Asia cruises.[20] Following the disclosure of the alleged sales tactics and declining cruise reservations, the company's stock price initially fell 26.7% on March 11, 2020, and then fell another 35.8% on March 12, 2020.[21]

In *Inovio Pharmaceuticals, Inc.*, a putative class of shareholders asserted claims under Sections 10(b) and 20(a) against Inovio Pharmaceuticals, Inc. and its CEO, J. Joseph Kim, alleging that management made misleading public statements indicating that the company had created a vaccine for the COVID-19 virus, leading to a jump in the company's stock price.[22] Among other things, Plaintiffs base their claims on a statement made by Inovio's CEO, J. Joseph Kim, after a meeting with President Trump, that Inovio was "able to fully construct [its] vaccine within three hours" and that Inovio planned to start trials for the vaccine in April 2020.[23] Following reports from a third party indicating that Inovio had not, in fact, developed a COVID-19 vaccine, the company's stock price plummeted on March 9, 2020, from $18.72 to $9.83, and fell again on March 10, 2020 to $5.70.[24]

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18 *Id.* ¶ 18.

19 *Id.* ¶ 21. A sample sales script instructed employees to address customer concerns with allegedly false statements, such as "the Coronavirus can only survive in cold temperatures, so the Caribbean is a fantastic choice for your next cruise[.]" *Id.* ¶ 22.

20 *Id.*

21 *Id.* ¶¶ 24, 27. Notably, March 12, 2020, was a particularly volatile day for the markets in general—the S&P fell 9% and the Dow plunged 10%, its largest decline since "Black Monday" on October 19, 1987. *See* Pippa Stevens, Maggie Fitzgerald & Fred Imbert, *Stock Market Live Thursday: Dow Tanks 2,300 in Worst Day Since Black Monday, S&P 500 Bear Market*, CNBC, https://www.cnbc.com/2020/03/12/stock-market-today-live.html (Mar. 12, 2010, 5:12 PM). Given these historic declines, plaintiffs will likely face an uphill battle in proving that the declines suffered by Norwegian Cruise Lines were in fact caused by Norwegian's public statements.

22 *See* Complaint ¶¶ 3-6, *McDermid v. Inovio Pharm., Inc.*, No. 2:20-cv-01402-GJP (E.D. Pa. Mar. 12, 2020), ECF No. 1.

23 *Id.* ¶¶ 5, 18.

24 *Id.* ¶¶ 6, 26.

With courts across the country freezing or reducing dockets due to COVID-19, there may be a short—but temporary—reprieve in such litigation. In the meantime, as outlined below, there are number of steps companies can take to help mitigate the risk of litigation.

Mitigating the Risk of COVID-19-Based Securities Litigation

Recognizing the significance of COVID-19 to the securities markets, the U.S. Securities and Exchange Commission ("SEC") issued an unusual Press Release on March 4, 2020, reminding "all companies to provide investors with insight regarding their assessment of, and plans for addressing, material risks to their business and operations resulting from the coronavirus to the fullest extent practicable to keep investors and markets informed of material developments."[25] Notably, the SEC's Press Release underscored that "[h]ow companies plan and respond to the events as they unfold can be material to an investment decision[.]"[26]

In addition, on March 25, 2020, the SEC's Division of Corporate Finance issued additional Disclosure Guidance, including a non-exhaustive list of questions that should be considered in making COVID-19 disclosures.[27] Further, on April 8, 2020, SEC Chairman Jay Clayton and the SEC Director of the Division of Corporation Finance, William Hinman, released an unprecedented joint Public Statement urging public companies to provide forward-looking guidance in their quarterly earnings statements and calls.[28] The SEC's statements on COVID-19 offer several practical takeaways.

First, according to the SEC's March 4 press release, as a first line of defense, companies should carefully "consider their activities in light of their disclosure obligations" and, if a company has become aware of a material risk related to COVID-19, it should "refrain from securities related transactions with the public" until that risk is fully disclosed.[29] Such activities include stock issuances and buybacks, mergers, acquisitions, tender offers, and joint ventures.

Second, in disclosing a risk related to COVID-19, the SEC advises companies, consistent with Regulation FD, to take "necessary steps to avoid selective disclosures and to disseminate"

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25 *See* Press Release, U.S. Sec. & Exch. Comm'n, *SEC Provides Conditional Regulatory Relief and Assistance for Companies Affected by the Coronavirus Disease 2019 (COVID-19)* at 1 (Mar. 4, 2020), https://www.sec.gov/news/press-release/2020-53.

26 *Id.*

27 *See* Guidance, U.S. Sec. & Exch. Comm'n Div. of Corp. Fin., *CF Disclosure Guidance: Topic No. 9 – Coronavirus (COVID-19)* at 1-2 (Mar. 25, 2020), https://www.sec.gov/corpfin/coronavirus-covid-19.

28 *See* Public Statement, U.S. Sec. & Exch. Comm'n, *The Importance of Disclosure – For Investors, Markets and Our Fight Against COVID-19* at 1-2 (Apr. 8, 2020), https://www.sec.gov/news/public-statement/statement-clayton-hinman.

29 *See* Press Release, U.S. Sec. & Exch. Comm'n, *SEC Provides Conditional Regulatory Relief and Assistance for Companies Affected by the Coronavirus Disease 2019 (COVID-19)* at 2 (Mar. 4, 2020), https://www.sec.gov/news/press-release/2020-53.

information concerning COVID-19-related risks broadly. However, according to Chairman Clayton and Director Hinman's joint statement,[30] companies should avoid placing sole reliance on "generic, or boilerplate, disclosures" concerning the general risks of COVID-19.[31] For example, non-specific statements that COVID-19 has generally harmed the economy and securities markets are unlikely to satisfy an issuer's disclosure obligations with respect to its business in particular or to insulate an issuer from securities law lawsuits under the bespeaks caution or similar doctrines.[32]

Third, companies should also be careful not to overstate their preparedness to handle the crisis or downplay the material impact of the pandemic on their business. In particular, companies should keep a close watch over public statements by their directors and officers, as the SEC's Press Release cautions public companies to "take steps to prevent directors and officers"[33] from exaggerating the company's preparedness to handle COVID-19. Indeed, the SEC has reportedly suspended trading in three stocks as a result of potentially inaccurate claims regarding the companies' responses to COVID-19.[34]

Fourth, in light of Chairman Clayton and Director Hinman's statement urging public companies to make forward-looking disclosures concerning "how [the company's] operations and financial condition may change as all our efforts to fight COVID-19 progress,"[35] companies should carefully craft their forward-looking statements to minimize their risk of liability. In particular, the SEC's March 25, 2020 Disclosure Guidance "remind[s] companies that providing forward-looking information in an effort to keep investors informed about material developments, including known trends or uncertainties regarding COVID-19, can be undertaken in a way to avail the companies of the safe harbors in Section 27A of the Securities Act and Section 21E of the Exchange Act for this

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30 The joint public statement represents Chairman Clayton and Director Hinman's views, not the official position of the SEC. *See* Public Statement, U.S. Sec. & Exch. Comm'n, *The Importance of Disclosure – For Investors, Markets and Our Fight Against COVID-19* at 1 n.i (Apr. 8, 2020), https://www.sec.gov/news/public-statement/statement-clayton-hinman.

31 *See id.* at 4.

32 *See In re Veeco Instruments, Inc., Sec. Litig*, 235 F.R.D. 220, 235 (S.D.N.Y. 2006) (generic, boilerplate statements are insufficient); *Schottenfeld Qualified Assocs. v. Workstream, Inc.*, No. 05 Civ. 7092 (CLB), 2006 WL 4472318, at *3 (S.D.N.Y. May 4, 2006) (finding insufficient cautionary language that "refers to the most general of economic risks"); *In re Prudential Sec. Inc. Ltd. P'ships Litig.*, 930 F. Supp. 68, 72 (S.D.N.Y. 1996) (cautionary language must "precisely address the substance of the specific statement" that is at issue).

33 Press Release, U.S. Sec. & Exch. Comm'n, *SEC Provides Conditional Regulatory Relief and Assistance for Companies Affected by the Coronavirus Disease 2019 (COVID-19)* at 2 (Mar. 4, 2020), https://www.sec.gov/news/press-release/2020-53.

34 *See* Al Barbino, *SEC Enforcement Expected To Surge On COVID Volatility*, Law360 (Apr. 9, 2020), https://www.law360.com/articles/1262118/sec-enforcement-expected-to-surge-on-covid-volatility.

35 Public Statement, U.S. Sec. & Exch. Comm'n, *The Importance of Disclosure – For Investors, Markets and Our Fight Against COVID-19* at 1 (Apr. 8, 2020), https://www.sec.gov/news/public-statement/statement-clayton-hinman.

information."[36] As discussed in greater detail below, these provisions provide safe harbors for forward-looking statements accompanied by meaningful cautionary language.

Finally, the SEC's Division of Corporation Finance has identified several key questions to consider with respect to a company's present and future operations in the context of COVID-19 disclosures, including:

- "How has COVID-19 impacted your financial condition and results of operations?"
- "In light of changing trends and the overall economic outlook, how do you expect COVID-19 to impact your future operating results and near-and-long-term financial condition?"
- "Do you expect that COVID-19 will impact future operations differently than how it affected the current period?"
- "Have you experienced challenges in implementing your business continuity plans or do you foresee requiring material expenditures to do so? Do you face any material resource constraints in implementing these plans?"
- "Do you expect COVID-19 to materially affect the demand for your products or services?"
- "Do you anticipate a material adverse impact of COVID-19 on your supply chain or the methods used to distribute your products or services?"
- "Do you expect the anticipated impact of COVID-19 to materially change the relationship between costs and revenues?"
- "Will your operations be materially impacted by any constraints or other impacts on your human capital resources and productivity?"
- "Are travel restrictions and border closures expected to have a material impact on your ability to operate and achieve your business goals?"[37]

Strategies to Dismiss COVID-19-Related Securities Litigation at the Pleading Stage
If a company finds itself faced with a COVID-19-based securities claim, there are several tools available to defeat such a claim at the pleadings stage.

- **A defendant may defeat a claim by showing that the alleged misstatements are forward-looking statements protected by the PSLRA's Safe Harbor.** – The Private Securities Litigation Reform Act of 1995 ("PSLRA") provides an important safe harbor that protects forward-looking statements "accompanied by meaningful cautionary statements

[36] Guidance, U.S. Sec. & Exch. Comm'n Div. of Corp. Fin., *CF Disclosure Guidance: Topic No. 9 – Coronavirus (COVID-19)* at 2 (Mar. 25, 2020), https://www.sec.gov/corpfin/coronavirus-covid-19.

[37] *Id.*

identifying important factors that could cause actual results to differ materially from those in the forward-looking statement[.]"[38] In *Police Retirement System of St. Louis v. Intuitive Surgical, Inc.*,[39] for instance, the Northern District of California held that statements concerning a company's ability to sustain growth in light of the 2008 financial crisis were non-actionable forward-looking statements under the PSLRA's safe harbor. Because the alleged misrepresentations concerned the rate at which the company "expected to grow" and stated that the financial crisis had "not yet looked like a real issue," the court found that they were forward-looking.[40] Further, the court held that the challenged statements were accompanied by "meaningful cautionary language," including disclosures that the statements concerned "future financial performance" and that the financial crisis may "cause variance" in the company's performance.[41] Companies may similarly avail themselves of the safe harbor by cabining forward-statements about COVID-19 with meaningful warnings about the uncertainties posed by the virus. However, companies should remain wary that statements about the company's present ability to handle the COVID-19 outbreak may not be protected. In *In re BP p.l.c. Securities Litigation*,[42] the Southern District of Texas held that BP's statements concerning its new management system in response to the oil spill constituted a "mixed statement of present fact and future events," and any misstatements concerning the *then-present* effectiveness of the operating system were not protected by the safe harbor.

- **A defendant may defeat a claim by showing that the alleged misstatements are mere expressions of corporate optimism.** – Mere opinions or expressions of corporate optimism concerning COVID-19 also cannot support a securities fraud claim. A misrepresentation is actionable only if it is "material"—that is, there is a "substantial likelihood" that it "would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[43] If an alleged misrepresentation is deemed to be mere "puffery," or a generic expression of corporate optimism, it is considered immaterial and, thus, non-actionable.[44] For example, in *Intuitive Surgical*, discussed above, the Northern District of California held that even if alleged misrepresentations concerning the company's projections following the 2008 financial crisis were not shielded by the PSLRA's safe harbor, statements such as "we don't think we have hit a penetration ceiling," "we will come out stronger," and "we

38 *See* 15 U.S.C. § 77z-2(c)(1)(A)(i).

39 No. 10-CV-03451-LHK, 2012 WL 1868874, at *9 (N.D. Cal. May 22, 2012), *aff'd,* 759 F.3d 1051 (9th Cir. 2014).

40 *Id.* at *11.

41 *Id.* at *12.

42 922 F. Supp. 2d 600, 624-25 (S.D. Tex. 2013).

43 *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976) (citation omitted).

44 *See Singh v. Cigna Corp.*, 918 F.3d 57, 63 (2d Cir. 2019).

sit in a pretty good position" were too "vague and amorphous" to be material.[45] Thus, although companies making COVID-related disclosures have an obligation to report information accurately, they should not face liability merely for expressing general optimism that they will overcome difficulties caused by the pandemic.

- **A defendant may move to dismiss a claim for failure to plead that the alleged misstatement caused the plaintiff's losses.** – In order to establish securities fraud liability, a plaintiff must plead and prove a "causal link between the alleged misconduct and the economic harm ultimately suffered by the plaintiff."[46] To do so, the complaint must allege "'that the misstatement or omission concealed something from the market that, when disclosed, negatively affected the value of the security.'"[47] The Supreme Court has held, moreover, that allegations that investors paid an "artificially inflated purchase price" for the stock are insufficient, standing alone, to plead loss causation—investors also must plead that the revelation or materialization of the fraud caused the stock price to drop.[48] In *In re Merrill Lynch & Co. Research Reports Securities Litigation*,[49] for example, investors in an internet holding company brought securities fraud claims against certain broker-dealers alleging that, despite the company's liquidity problems, the defendants issued positive research reports on which the investors relied to their detriment. The Southern District of New York dismissed the claims for failure to plead that the decline in stock price was caused by the revelation of the fraud, rather than the coinciding "burst[] of the Internet bubble."[50] Because the complaint "fail[ed] to account . . . for the 'cratering' of the Internet market that occurred during the ten-month period" from December 1999 to October 2000 when the reports were issued, it failed to plead a connection between the fraud and the investors' harm.[51] Given recent market volatility, companies experiencing a stock decline concurrent with COVID-19's negative impact on markets may be able to avail themselves of a similar line of argument to dismiss securities claims at the pleading stage.
- **A defendant may move to dismiss a claim for failure to plead that the defendant made the misstatement with fraudulent intent.** – Finally, under the PSLRA, the complaint must allege "with particularity facts giving rise to a strong inference that the defendant acted

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45 *Police Ret. Sys. of St. Louis v. Intuitive Surgical, Inc.*, No. 10-CV-03451-LHK, 2012 WL 1868874, at *13-14 (N.D. Cal. May 22, 2012), *aff'd,* 759 F.3d 1051 (9th Cir. 2014).

46 *See Emergent Cap. Inv. Mgmt., LLC v. Stonepath Grp., Inc.*, 343 F.3d 189, 197 (2d Cir. 2003); 15 U.S.C. § 78u-4(b)(4).

47 *DoubleLine Cap. LP v. Odebrecht Fin., Ltd.*, 323 F. Supp. 3d 393, 456 (S.D.N.Y. 2018) (quoting *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 173 (2d Cir. 2005)).

48 *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 347 (2005).

49 568 F. Supp. 2d 349, 351 (S.D.N.Y. 2008).

50 *Id.* at 363.

51 *Id.* at 364.

with" fraudulent intent.[52] In *Jackson v. Halyard Health, Inc.*,[53] for example, the Southern District of New York dismissed securities fraud claims based on allegedly false statements concerning the effectiveness of a company's surgical gowns at preventing the spread of Ebola, concluding that the complaint failed to plead the requisite strong inference of scienter. According to the court, plaintiffs did not sufficiently allege that the defendants actually received or were aware of reports detailing the deficiencies in the surgical gowns, nor did it plead facts showing that they were reckless in failing to learn these facts, and thus the complaint failed to state a claim for securities fraud against them.[54] Likewise, the Southern District of New York, in *Sinay v. CNOOC Ltd.*,[55] dismissed 10b-5 claims alleging that an oil-drilling company misrepresented its preparedness to prevent and contain an oil spill for lack of scienter, concluding that "hindsight-based" allegations that the safety measures ultimately proved inadequate were "insufficient to support a strong inference of scienter," absent any factual allegations "undermining the accuracy of" the company's disclosures when made. Because the complaint was devoid of any allegations that the company's "inspections and plans" of its safety measures were ineffective or that its "estimates of the spills' magnitude was incorrect" the court dismissed the claims for lack of scienter.[56] Thus, as courts recognize, mere hindsight concerning the impact of a significant event like COVID-19 is insufficient to plead fraudulent intent.

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52 15 U.S.C. § 78u-4(b)(2)(A).

53 No. 16-CV-05093-LTS, 2018 WL 1621539, at *4-5 (S.D.N.Y. Mar. 30, 2018), *appeal docketed*, No. 19-1300 (2d Cir. May 1, 2019).

54 *Id.* at *5-8.

55 No. 12 CIV. 1513 (KBF, 2013 WL 1890291, at *8 (S.D.N.Y. May 6, 2013), *aff'd*, 554 F. App'x 40 (2d Cir. 2014) (Summary Order).

56 *Id.* It is well-settled that allegations of "fraud by hindsight," *i.e.*, misrepresentations that the speaker believed were true at the time they were made, but later proved to be false, are not actionable. *See Waterford Twp. Police & Fire Ret. Sys. v. Reg'l Mgmt. Corp.*, 723 F. App'x 20, 22 (2d Cir. 2018) (Summary Order).