

Securities Law Alert

KEY DEVELOPMENT IN SHAREHOLDER LITIGATION

Ninth Circuit: COVID-19 Antibody Statements Not Materially Misleading When Read in Context

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On March 25, 2024, the Ninth Circuit affirmed the dismissal of a securities fraud class action alleging that a biopharmaceutical company and two of its executives falsely claimed early on in the pandemic that the company's new antibody was a cure for COVID-19. *Zenoff v. Sorrento Therapeutics*, 2024 U.S. App. LEXIS 6979 (9th Cir. 2024) (Callahan, J.). The Ninth Circuit held that, "in context, Defendants' representations were not false, and [plaintiff's] pleadings do not support the requisite strong inference of scienter." The court explained that "[a] fair reading of the press release and the articles reveals that there was no promise of an immediate 100% cure."

Background

In May 2020, the company announced its development of a COVID-19 antibody. This litigation arose from three documents from May 15, 2020: (i) a company press release entitled "STI-1499, A Potent Anti-SARS-COV-2 Antibody Demonstrates Ability to Completely Inhibit In Vitro Virus Infection In Preclinical Studies" (the "May 15 Press Release"); (ii) a news article entitled "California biopharmaceutical company claims coronavirus antibody breakthrough" (the "May 15 News Article"); and (iii) an online news article entitled "Sorrento IDS Antibody Against COVID-19 That Appears 100% Effective" (the "May 15 Online Article"). The company's stock price increased following the initial announcement. However, within a week, published articles and short seller reports questioned the importance of the company's development after which the company experienced a stock drop.

Plaintiff filed suit alleging that the company had falsely claimed to have developed a COVID-19 cure, misleading investors in violation of Section 10(b) of the Exchange Act and SEC Rule 10b-5. The complaint focused on various statements to the media such as, "We want to emphasize there is a cure. There is a solution that works 100 percent," and "if we have the neutralizing antibody in your body, you don't need the social distancing. You can open up a society without fear." In 2022, the district court granted the company's motion to dismiss, rejecting plaintiff's argument that defendants had misled investors. The district court found the assertion of a cure and a solution that works 100% were "a statement of corporate optimism" that "cannot state an actionable material misstatement of fact under federal securities law." The district court concluded that "in reviewing each of these statements within the context of each entire article, [plaintiff] has not sufficiently pled the existence of false or misleading statements." In support of this, the court noted that the May 15 News Article reported one executive as

stating that the company anticipated having enough material to start a Phase I trial within two months. The May 15 News Article also noted that “quick” FDA approval “would be needed to make the antibody treatment available within months.” Plaintiff appealed the dismissal.

Plaintiff Failed to Adequately Plead That the Statements Were False as Opposed to Overstated

Rejecting plaintiff’s contention that the company “told the world multiple whoppers concerning a 100% cure for COVID-19” the Ninth Circuit concluded that while defendants’ “enthusiasm . . . might have been overblown, in context, their statements were not materially misleading.” Reviewing defendants’ statements, the court pointed out that:

- The May 15 Press Release began that the company’s antibody “demonstrated 100% inhibition of SARS-CoV-2 virus infection in an in vitro virus infection experiment at a very low antibody concentration.”
- The May 15 News Article’s headline “California biopharmaceutical company claims coronavirus antibody breakthrough” had a bold-print subsection entitled “possible coronavirus vaccine enters human testing trial.”
- The May 15 Online Article stated that “if the Phase 1 trial starts by the beginning of July, they will know within a week or two whether the antibody is having an effect.”

The court concluded that, despite defendants’ enthusiasm, in context, all of the articles revealed that the antibody’s development was only at the lab testing stage. The court determined that plaintiff failed to show “that a reasonable person reading the articles would think that Defendants were representing that [the antibody], without further testing, was an immediate cure for COVID-19.”

The Ninth Circuit also stated that the “only basis” plaintiff offered to support his claim that the representations were knowingly false was that there is still no cure for COVID-19. However, the court pointed out that plaintiff did not address whether, in May 2020, the antibody “showed some promise as a cure for COVID-19.” Taking issue with plaintiff’s reasoning that because there is still no cure for COVID-19 that defendants could not have thought that the antibody was a cure, the court pointed out that the failure to survive the testing required for FDA approval “is hardly evidence that the developer’s initial enthusiasm was unwarranted or inherently false at the time.”

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