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Securities Law Alert

Year in Review:

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2024

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Supreme Court Decisions and Developments

Supreme Court: Overturns *Chevron* Deference

Overturning nearly 40 years of precedent, on June 28, 2024, the Supreme Court held by a 6-3 vote: "*Chevron* is overruled." *Loper Bright Enters. v. Raimondo*, 144 S. Ct. 2244 (2024) (Roberts, C.J.).[1] Under *Chevron v. Natural Resources Defense Council*, 104 S. Ct. 2778 (1984), federal courts were required to defer to an administrative agency's interpretation in cases involving statutory questions of agency authority as long as the agency's interpretation was not unreasonable. Writing for the majority, Chief Justice Roberts concluded that *Chevron* could not be reconciled with the Administrative Procedure Act ("APA"), which governs federal administrative agencies, because the APA requires a reviewing court to exercise its independent judgment in deciding whether an agency has acted within its statutory authority, but *Chevron* requires the court "to *ignore*, not follow," the reading the court would have reached had it exercised this independent judgment.

The Court further criticized *Chevron*'s presumption–that Congress understood that a statutory ambiguity would be resolved, first and foremost, by the agency, and desired the agency to possess whatever degree of discretion the ambiguity allows–stating that it "is misguided because agencies have no special competence in resolving statutory ambiguities." Chief Justice Roberts stated that "[t]he very point of the traditional tools of statutory construction–the tools courts use every day–is to resolve statutory ambiguities." He noted that this is particularly true when the ambiguity concerns the scope of the agency's own power, which he described as "perhaps the occasion on which abdication in favor of the agency is *least* appropriate."

Although the Court found that past judicial decisions have shown *Chevron* to be "unworkable" and unreliable as a result of inconsistent application by the lower courts, it did "not call into question prior cases that relied on the *Chevron* framework." Rather, the Court concluded that "[t]he holdings of those cases that specific agency actions are lawful—including the Clean Air Act holding of *Chevron* itself—are still subject to statutory *stare decisis* despite our change in interpretive methodology."

1. The Court's decision arose from a pair of cases, *Loper Bright Enterprises v. Raimondo* and *Relentless v. Department of Commerce*, where the District of Columbia Circuit and the First Circuit, respectively, upheld a regulation issued by a federal agency as a reasonable interpretation of a federal statute.

Supreme Court: In-House SEC Tribunals Violate Securities Fraud Defendants' Seventh Amendment Right

On June 27, 2024, the Supreme Court held that the SEC's adjudication of an enforcement action, seeking civil penalties for alleged securities fraud in an in-house tribunal before an administrative law judge, violated defendants' Seventh Amendment right to a jury trial. *SEC v. Jarkesy*, 144 S. Ct. 2117 (2024) (Roberts, C.J.). By a 6-3 Justice majority, the Court concluded that this action implicates the Seventh Amendment because the antifraud provisions at issue "replicate common law fraud, and it is well established that common law claims must be heard by a jury," considering the Seventh Amendment's guarantee that in "suits at common law the right of trial by jury shall be preserved."

The case arose when the SEC initiated an in-house enforcement action against an investment fund founder and an investment adviser seeking civil penalties and other remedies, alleging that defendants had violated the antifraud provisions of the Securities Act, the Securities Exchange Act, and the Investment Advisers Act. The proceedings resulted in a final order against defendants with a civil penalty of $300,000. Defendants petitioned for judicial review and a divided Fifth Circuit panel vacated the final order, holding that adjudicating the matter in-house violated defendants' Seventh Amendment right to a jury trial. *Jarkesy v. SEC*, 34 F. 4th 446 (5th Cir. 2022). After the Fifth Circuit denied rehearing *en banc*, the Supreme Court granted *certiorari*.

Writing for the majority, Chief Justice Roberts affirmed the Fifth Circuit's decision as consistent with the Court's rulings in *Granfinanciera, S. A. v. Nordberg*, 492 U. S. 33 (1989) and *Tull v. United States*, 481 U. S. 412 (1987). Under *Granfinanciera*, the Seventh Amendment "extends to a particular statutory claim if the claim is legal in nature." The Court explained in *Tull* that "[t]o determine whether a suit is legal in nature, we directed courts to consider the cause of action and the remedy it provides." The Court continued, that "[s]ince some causes of action sound in both law and equity, we concluded that the remedy was the more important consideration." The Court then stated that "the civil penalties in this case are designed to punish and deter, not to compensate. They are therefore a type of remedy at common law that could only be enforced in courts of law." The Court explained that its conclusion effectively decided that this suit implicated the Seventh Amendment and that a defendant would be entitled to a jury on these claims.

Supreme Court: Pure Omissions Not Actionable Under Rule 10b-5(b)

On April 12, 2024, the Supreme Court issued a unanimous opinion holding that a company's failure to make disclosures required by Item 303 of SEC Regulation S-K[2] cannot in itself support a private securities claim under Section 10(b) of the Securities Exchange Act of 1934, which makes it unlawful to use or employ any manipulative or deceptive device or contrivance in connection with the purchase or sale of any security, and Rule 10b-5(b)[3] thereunder where the omission did not render any of the company's affirmative statements misleading. *Macquarie Infrastructure Corp. v. Moab Partners, L.P.*, 144 S. Ct. 885 (2024) (Sotomayor, J.). "Pure omissions are not actionable under Rule 10b-5(b)." The opinion resolves a circuit split on the issue between the Second Circuit, on the one hand, and the Third and Ninth Circuits, on the other.

2. Item 303 of SEC Regulation S–K requires companies to "describe any known trends or uncertainties that have had or that are reasonably likely to have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations." 17 CFR § 229.303(b)(2)(ii).

3. Among other things, Rule 10b-5 makes it unlawful for issuers of registered securities 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." 17 CFR §240.10b–5(b).

This litigation began when an investor sued alleging that the defendant company's public statements were false and misleading because it concealed from investors that its subsidiary's single largest product was No. 6 fuel oil, which was subject to a United Nations regulation that would significantly restrict its use. Plaintiff claimed that under Item 303 the company had "a duty to disclose" how much of its subsidiary's storage capacity was devoted to No. 6 fuel oil and, by violating that duty, the company violated Section 10(b) and Rule 10b-5. The district court dismissed, concluding that plaintiff had not actually pled an uncertainty that should have been disclosed or in what SEC filing or filings the company should have disclosed it. The Second Circuit reversed, concluding that the company's Item 303 violation alone was enough to sustain claims under Section 10(b) and Rule 10b-5.

Justice Sotomayor, writing for the Court, explained that Rule 10b-5(b), in essence, prohibits false statements and prohibits "omitting a material fact necessary to make the statements made not misleading." The Court stated that the issue was "whether this second prohibition bars only half-truths or instead extends to pure omissions[,]" which occur "when a speaker says nothing, in circumstances that do not give any particular meaning to that silence." Concluding that "Rule 10b-5(b) does not proscribe pure omissions" the Court reasoned that "the Rule requires identifying affirmative assertions (*i.e.*, statements made) before determining if other facts are needed to make those statements not misleading." Citing *Matrixx Initiatives, Inc. v. Siracusano*, 563 U. S. 27 (2011), the Court emphasized that Section 10(b) and Rule 10b-5(b) do not create an affirmative duty to disclose any and all material information, and that disclosure is required under these provisions only when necessary to make statements already made not misleading.

Supreme Court: Dismisses Both Securities Suits That It Took Up This Term

On November 22, 2024 and December 11, 2024, the Supreme Court issued *per curiam* opinions stating that the writs of *certiorari* granted in *Facebook v. Amalgamated Bank*, No. 23-980 and *Nvidia v. E. Ohman J:Or Fonder AB*, No. 23-970 were dismissed as improvidently granted. Decisions in these cases were eagerly anticipated as they could have potentially provided insights concerning the Private Securities Litigation Reform Act ("PSLRA"). In *Facebook*, the issue concerned whether public company risk disclosures are false or misleading if they do not disclose that a risk has materialized in the past. In *Nvidia*, the issue concerned pleading requirements, namely whether expert witness allegations about internal company documents must plead with particularity the documents' contents and whether an expert opinion can substitute for particularized allegations of fact. Following the Court's dismissals, each case is expected to return to a California federal district court for further proceedings.

In *Facebook*, plaintiff shareholders alleged that a social media company and certain of its executives violated Section 10(b) and Rule 10b-5(b) by making materially misleading statements and omissions when the company warned of the risk of improper access to user data when in fact improper access had already occurred. After the case's dismissal, the Ninth Circuit partially reversed in 2023 holding that plaintiffs adequately pled the falsity of the company's risk statements in its 2016 10-K concerning the risk of third parties improperly accessing and using user data as purely hypothetical while the company allegedly knew that a political consulting firm had already done so when it filed its 10-K. The Ninth Circuit further held that plaintiffs adequately pleaded falsity as to the statements warning that misuse of user data could harm the company's business, reputation, and competitive position.

In its Supreme Court *certiorari* petition, the company asked "[a]re risk disclosures false

or misleading when they do not disclose that a risk has materialized in the past, even if that past event presents no known risk of ongoing or future business harm?" The company urged the Justices to rule that public companies need not disclose past events if there is no known risk of future harm. At the November 6, 2024 oral argument, the company's attorney initially urged the Justices to adopt an approach where a typical risk disclosure cannot be misleading simply because the triggering event had occurred in the past but a forward-looking risk disclosure could be misleading based on an embedded premise about the current state of affairs, depending on the statement's content. Justice Sotomayor observed that it appeared the company was in fact seeking a categorial rule (such that risk disclosures under Item 105 make no implied representation about a company's past experiences) and would consider context only as to whether there was a misrepresentation, not a misleading representation. Justice Barrett similarly noted that it appeared the company was advocating for a categorical rule. Justice Barrett also noted the difficultly of drafting a rule, asking how to articulate a rule that would handle anything more than the case before the Court. Chief Justice Roberts pointed out that if the Court adopted the standard that a probabilistic statement could sometimes carry an inference that something has already occurred then it would lead to a substantial expansion of disclosure obligations. Justice Kavanaugh expressed concern that if the Court required disclosure it would create separation of powers and fair notice issues, stating that "[t]he SEC knows how to write regulations that require disclosure of past events." He further questioned whether such a requirement would result in over disclosure.

In *Nvidia*, plaintiff shareholders alleged that a technology company, its CEO and two officer defendants violated Section 10(b) and Rule 10b-5 by failing to state or substantially understating the extent to which the company's revenue growth for its processers depended on crypto mining rather than video gaming.[4] Plaintiffs claimed that the CEO made public statements that were contrary to the company's internal reports. However, plaintiffs' allegations did not rely on actual internal reports and instead relied on a retained expert's analysis of the company's cryptocurrency market share and its cryptocurrency revenues to conclude that defendants understated the company's crypto-related sales by over $1 billion. The district court dismissed plaintiffs' amended complaint under Rule 12(b)(6) for failing to sufficiently plead that defendants' allegedly false or misleading statements were made knowingly or recklessly.[5]

The Ninth Circuit affirmed in part and reversed in part, holding that plaintiffs stated a claim under Section 10(b) and Rule 10b-5 against the company and CEO, but not the other two officer defendants. *E. Ohman J:Or Fonder AB v. Nvidia*, 81 F.4th 918 (9th Cir. 2023). The Ninth Circuit held that plaintiffs sufficiently alleged that the CEO made false or

4. The significance of this is that crypto-related demand is "notoriously volatile" because cryptocurrency prices can swing wildly causing mining to become unprofitable. This leads crypto miners, who use the processors to mine cryptocurrency, to stop purchasing the processors and to resell them on the secondary market at steep discounts.

5. The district court found that allegations did not raise a strong inference of scienter as plaintiffs did not adequately tie the specific contents of any data sources about crypto-related demand to particular statements to show that each specified statement was knowingly or recklessly false. The district court did not reach the question of whether the amended complaint failed to sufficiently plead that the statements were materially false or misleading.

misleading statements and did so knowingly or recklessly.[6] The Ninth Circuit found that plaintiffs sufficiently pleaded scienter under the PSLRA as to the CEO because the allegations supported "a strong inference" that he reviewed sales data showing that a large share of the processors sold were being used for crypto mining. The Ninth Circuit also held that the plaintiffs had sufficiently pleaded falsity based on the analyses of plaintiffs' expert as well as an international investment bank, which reached an "almost identical" conclusion. The Ninth Circuit noted that "the PSLRA nowhere requires experts to rely on internal data and witness statements to prove falsity." The Ninth Circuit pointed out that to do so "would place an onerous and undue pre-discovery burden on plaintiffs in securities fraud cases. We decline to turn the PSLRA's formidable pleading requirement into an impossible one."

Defendants' petition for a writ of *certiorari* to the Supreme Court asked whether plaintiffs: (i) seeking to allege scienter under the PSLRA based on allegations about internal company documents must plead with particularity the contents of those documents; and (ii) can satisfy the PSLRA's falsity requirement by relying on an expert opinion to substitute for particularized allegations of fact. At the November 13, 2024 oral argument, several Justices noted that while defendants' petition initially seemed to propose new categorical legal rules aimed at clarifying the PSLRA, defendants' position shifted to a fact-bound application of agreed-upon legal principles. While defendants' attorney asserted that the Ninth Circuit did not engage in the comparative analysis required under *Tellabs v. Makor Issues & Rights*, 551 U.S. 308 (2007) (as to whether or not plaintiffs' allegations were as cogent and compelling as any competing inferences), Justice Gorsuch pointed out that the Ninth Circuit did perform a comparative analysis albeit, "may be not emphasized enough for your taste, and therefore, may be wrong as a matter of error correction." Noting that the Court does not often grant *certiorari* to error correct, Justice Sotomayor questioned "[i]s this entire case just error correction?" Justice Sotomayor continued, stating that "I'm not actually sure what rule we could articulate that would be clearer than our cases already say."

6. Securities fraud cases are subject to the PSLRA and to sufficiently plead scienter under the PSLRA, a plaintiff must "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2)(A). In the Ninth Circuit, the required state of mind includes intent to deceive, manipulate, or defraud, and deliberate recklessness.

Significant Circuit Court Decisions

Second Circuit: Decides Two Matters of First Impression Concerning Challenged Statements on Scientific Studies and Data Interpretation

On December 26, 2023, the Second Circuit affirmed the dismissal of a putative securities fraud class action against a tobacco products manufacturer and certain of its executives alleging that they made various false and misleading statements about the company's smoke-free products in violation of Section 10(b) and Rule 10b-5. *In re: Philip Morris Int'l Sec. Litig.*, 89 F.4th 408 (2d Cir. 2023) (Sullivan, J.). Notably, the panel decided two matters of first impression in the Second Circuit. First, the court held that a securities fraud defendant's challenged statements that its scientific studies complied with a methodological standard that is published and internationally recognized, but stated in general and inherently subjective terms, were properly analyzed as statements of opinion rather than fact. Second, the court held that where a securities fraud defendant's challenged statements express an interpretation of scientific data, which is later ultimately endorsed by the FDA, such statements are per se reasonable as a matter of law under *Tongue v. Sanofi*, 816 F.3d 199 (2d Cir. 2016).

By way of background, the FDA authorized the company to market its smokeless tobacco product in the U.S. in 2019 and later further authorized the company to market it with claims that it reduced exposure to harmful chemicals. Subsequently, investor plaintiffs alleged that defendants had made false or misleading statements regarding the methodology and results of the scientific studies that the company submitted in support of its FDA authorization applications. In 2021, the district court dismissed with prejudice finding that plaintiffs had failed to adequately plead falsity or scienter and concluding that each such finding provided an alternate basis for dismissal.

On appeal, plaintiffs challenged the district court's conclusion that defendants' statements—that the company's studies were "conducted according to Good Clinical Practice" ("GCP")—were inactionable statements of opinion because defendants failed to couch their statements with words like "we think" or "we believe" citing *Omnicare v. Laborers District Council Construction Industry Pension Fund*, 575 U.S. 175 (2015).[7] The Second Circuit stated that defendants' reliance on *Omnicare* was misplaced, explaining that under *Omnicare* "language like 'we believe' or 'we think' is *sufficient* – not *necessary* – to render a statement one of opinion rather than fact." The Second Circuit stated that *Omnicare* clarified that if a statement expresses an "inherently subjective" assessment then that is also sufficient to render it pure opinion. The Second Circuit concluded that whether the requirements of GCP (that clinical trials should be "scientifically sound," that "qualified" individuals should conduct the trials and that the investigator should have "adequate resources") were met, and the ultimate question of whether the clinical trials complied with GCP, were "all questions that require inherently subjective assessments, and thus do not lend themselves to resolution as matters of objective fact."

7. In *Omnicare*, the Supreme Court rejected the argument that a defendant stating that "we believe we are following the law conveys that we in fact are following the law."

Second Circuit: Decentralized Crypto-Exchange Transactions Plausibly Alleged to Be Domestic Under *Morrison*

On March 8, 2024, the Second Circuit reversed and remanded a district court's dismissal of a putative securities fraud class action brought by plaintiff token purchasers alleging that an online crypto exchange–that denied that it had a physical headquarters in any geographic jurisdiction–violated federal and state securities laws by promoting, offering and selling tokens that were not registered as securities. *Williams v. Binance*, 96 F.4th 129 (2d Cir. 2024) (Nathan, J.). The Second Circuit held that plaintiffs plausibly alleged that the transactions were domestic transactions, under *Morrison v. National Australia Bank*, 561 U.S. 247 (2010), because they became irrevocable within the U.S. The court found that two transactional steps gave rise to an inference that irrevocable liability occurred in the U.S. First, the transactions were matched–and therefore became irrevocable–on U.S.-based servers. Second, plaintiffs transacted on the exchange from the U.S. and their buy orders became irrevocable when they were sent, pursuant to the exchange's Terms of Use.

The district court dismissed on the basis that plaintiffs' claims constituted an impermissible extraterritorial application of securities law under *Morrison*. On appeal, the Second Circuit held that "[p]laintiffs have adequately alleged that their claims involved domestic transactions because they became irrevocable within the United States and are therefore subject to our securities laws." Under *Morrison*, the Supreme Court interpreted the Exchange Act as applying only to "[1] securities listed on domestic exchanges, and [2] domestic transactions in other securities." The Second Circuit explained that "to sufficiently allege the existence of a domestic transaction in other securities, plaintiffs must allege facts

indicating that irrevocable liability was incurred or that title was transferred within the United States." The court continued that "[i]rrevocable liability attaches when parties become bound to effectuate the transaction or enter into a binding contract to purchase or sell securities." The court explained that "[t]o determine whether a transaction is domestic, courts must therefore consider both when and where the transaction became irrevocable." The court held "that irrevocable liability was incurred in the United States because Plaintiffs plausibly alleged facts allowing the inference that the transactions at issue were matched on U.S.-based servers." The court concluded it was appropriate to locate the matching of transactions where the exchange had its servers in the absence of an official locus of the exchange. Further, the court found that the fact that plaintiffs alleged that their purchase orders were submitted from U.S. locations rendered it more plausible that the trades at issue were matched over servers located in the U.S., as opposed to servers located elsewhere.

On January 13, 2025, the Supreme Court denied defendants' *certiorari* petition seeking to overturn the Second Circuit's decision. Defendants had asserted that the Second Circuit's approach was inconsistent with *Morrison* and was an improper revival of the "conduct and effects" test that the Court had rejected as inconsistent with the presumption against extraterritoriality.

Second Circuit: Reaffirms *Donoghue* Holding That Short-Swing Trading Inflicts Injury Sufficient for Constitutional Standing

On June 24, 2024, the Second Circuit reversed a district court's dismissal of a shareholder's Section 16(b)[8] derivative suit for lack of constitutional standing based on its determination that *TransUnion LLC v. Ramirez*, 594 U.S. 413 (2021) abrogated *Donoghue v. Bulldog Investors General Partnership*, 696 F.3d 170 (2d Cir. 2012). *Packer v. Raging Cap. Mgmt.*, 105 F.4th 46 (2d Cir. 2024) (Cabranes, J.). The Second Circuit concluded that the district court erred in dismissing and held that "nothing in *TransUnion* undermines *Donoghue*[.]"

This litigation arose when a retail company shareholder filed suit against an investment firm, its founder, and its investment manager alleging that they violated Section 16(b) by buying and selling the retailer's stock while they were 10% beneficial owners during a six-month period in 2014 and 2015. The district court dismissed concluding that the Supreme Court's 2021 decision in *TransUnion* (establishing that for an intangible injury[9] to be sufficiently concrete to confer constitutional standing, courts are to identify a "close historical or common-law analogue for the asserted injury"), abrogated the Second Circuit's 2012 *Donoghue* decision (holding that a violation of Section 16(b) inflicts an injury that confers constitutional standing). Finding that Section 16(b) merely protected against "speculative harm," the district court determined that the alleged violation did not confer standing in light of the *TransUnion* holding that "risk of harm" alone does not qualify as "concrete" harm.

Reversing, the Second Circuit concluded that the "deprivation of [short-swing] profits inflicts an injury sufficiently concrete to confer constitutional standing." The Second Circuit pointed out that in *TransUnion*, the Supreme Court instructed that to determine whether an intangible injury is sufficiently concrete to confer constitutional standing, a court should identify a "close historical or common-law analogue for their asserted injury." The Second Circuit continued that "[i]n *Donoghue*, we had identified such an analogue for a Section 16(b) injury: breach of fiduciary duty." The Second Circuit explained

8. Under Section 16(b), owners of more than 10% of a company's stock are required to disgorge profits (so-called "short-swing profits") made by buying and selling that company's stock within a six-month window. *See* 15 U.S.C. § 78p(b).

9. Examples of intangible injury include reputational harms and disclosure of private information compared to tangible harms such as physical harms and monetary harms.

that, "[a]s *Donoghue* made clear, because Section 16(b) makes 10% beneficial owners into statutory fiduciaries, a close historical or common-law analogue to short-swing trading by a 10% beneficial owner is breach of fiduciary duty." The Second Circuit stated that plaintiff did not base his standing argument on a risk of harm and that the concrete injury that conferred standing was, "the breach by a statutory insider of a fiduciary duty owed to the issuer not to engage in and profit from any short-swing trading of its stock."

Seventh Circuit: Raises the Possibility of Sanctions Against Class Counsel Seeking Mootness Fees

On April 15, 2024, the Seventh Circuit issued a long-awaited opinion addressing a would-be intervenor's objection to mootness fees paid in connection with M&A strike suits brought challenging proxy disclosures in a public company merger transaction. [*Alcarez v. Akorn*, 99 F.4th 368 (7th Cir. 2024) (Easterbrook, J.)]. The Seventh Circuit vacated an order denying the shareholder's motion to intervene and remanded, instructing the district court to treat him as an intervenor. Notably, the Seventh Circuit raised the possibility of sanctions against plaintiffs' counsel pointing out that a district judge has discretion over the choice of sanction under Federal Rule of Civil Procedure 11(c)(4). The Seventh Circuit's decision is believed to be the first federal appellate court review of mootness fee payments to resolve M&A strike suits.

After learning that the company in which he was an investor had made some supplemental disclosures and paid $322,500 (so-called "mootness fees") to obtain the voluntary dismissal of six lawsuits claiming that the company's proxy statement failed to make certain disclosures in violation of Section 14(a) of the Securities Exchange Act, the stockholder sought to intervene and requested disgorgement of the mootness fees or an injunction blocking them in future cases. While some of the attorneys disclaimed the fees, attorneys in three of the suits continued to seek them. In these three cases, the district judge permitted the shareholder to participate as an *amicus curiae* and ordered counsel to return the fees to the company concluding that the complaints were frivolous and that the extra disclosures were worthless to investors. *House v. Akorn*, 385 F. Supp. 3d 616 (N.D. Ill. 2019). Two plaintiffs appealed, seeking an order that would allow two attorneys to retain the fees. The shareholder also appealed, seeking to intervene and additional relief.

The Seventh Circuit stated that it was inclined to agree with the district court's analysis concluding that plaintiffs' cases "should have been dismissed out of hand" based on its findings that the disclosures were worthless to shareholders; that the company paid the fees to avoid the nuisance of ultimately frivolous lawsuits; and that the settlements caused the company to lose money. The Seventh Circuit stated that the district court should have relied on §78u–4(c)(1) of the PSLRA and FRCP 11 rather than on its "inherent authority" to abrogate the settlement agreements and order plaintiffs' counsel to return the mootness fees. The PSLRA states that in any private action arising under the Securities Exchange Act, the court shall include in the record, upon final adjudication of the action, specific findings regarding

compliance by parties and their attorneys with each requirement of FRCP 11(b).[10] The Seventh Circuit then noted that the six suits invoked Section 14(a) of the Securities Exchange Act, the dismissal of each suit was a "final adjudication of the action" and then stated that the statute "obliges the judge to determine whether each suit was proper at the moment it was filed." The Seventh Circuit then observed that "because Rule 11(c)(4) gives the district judge discretion over the choice of sanction, the court would be entitled to direct counsel who should not have sued at all to surrender the money they extracted from [the company]. But selecting an appropriate remedy (if any) should await resolution of the proceedings under §78u–4(c)(1) and, derivatively, Rule 11."

Ninth Circuit: Writing and Disseminating Favorable Articles Is Solicitation Within the Meaning of a Securities Purchase Agreement

On April 5, 2024, the Ninth Circuit largely reversed the dismissal of a putative securities fraud class action alleging that a company misled investors when it represented in a securities purchase agreement ("SPA") that it had not compensated any entity to solicit its securities, when, in fact, it had retained a stock promoter to write and disseminate favorable articles about it. [*In re Genius Brands Int'l*, 97 F.4th 1171 (9th Cir. 2024) (Mendoza, J.)](). Relying on the plain meaning of solicit and *Pino v. Cardone Capital*, 55 F.4th 1253 (9th Cir. 2022), which defined "solicitation" broadly, the Ninth Circuit concluded that writing and disseminating favorable articles amounted to solicitation within the meaning of the SPA.

After the company experienced a stock drop, plaintiff stockholders sued alleging that the company had concealed its relationship with a stock promoter it retained in violation of Section 10(b) and Rule 10b-5(b), because the company later stated in an SPA that the company "has not . . . paid or agreed to pay any Person any compensation for soliciting another to purchase" its securities. The district court dismissed finding that plaintiffs "did not allege that anything in the [stock promoter's] articles themselves was false or misleading and because [the stock promoter] had no duty to disclose [the company] as the source of its funding."

On appeal, the Ninth Circuit stated that the dispositive question was whether the company, by representing in its SPA that it did not hire anyone to solicit its securities, had made a misleading statement when it compensated the stock promoter to publish favorable articles about it. The Ninth Circuit explained that "[t]o determine whether a statement or omission is misleading, our central inquiry is whether a reasonable investor would have been misled" and that the court must assess "whether an investor who had been reasonably diligent in reviewing the statement or omission at issue would have been misled."

Examining the plain meaning of "solicit," the Ninth Circuit concluded that "a person solicits the sale of a security where she petitions, entices, lures or urges another to purchase a security." In *Pino v. Cardone Capital*, in the course of determining whether a company alleged to have made misleading statements on social media to encourage people to invest in its equity funds, was a statutory seller within the meaning of Section 12(a)(2) of the Securities Act, the Ninth Circuit considered the definition of solicitation. Choosing to define solicitation broadly, the Ninth Circuit concluded that "a person can solicit a purchase, within the meaning of the Securities Act, by promoting the sale of a security in a mass communication." Drawing on the plain meaning of solicit and *Pino*, in this case, Ninth Circuit concluded that the stock promoter solicited the purchase of the company's securities because plaintiff alleged that the company retained the stock promoter "to publish and disseminate favorable information about [the company's] shares." Further, the court stated that the articles solicited the purchase of the securities because "they urged or lured readers into purchasing [the company's] stock." The court reasoned that it "plausibly follows" that the company misled investors when it represented in the SPA that it "had not paid or agreed to pay to any Person any compensation for soliciting another to purchase any other securities of the Company." The court

10. Generally, FRCP 11(b) provides that by presenting a document to the court, an attorney certifies that it is not being presented for any improper purpose (such as needlessly increasing the cost of litigation); that the claims, defenses, and other legal contentions are warranted by existing law; that the factual contentions have or will have evidentiary support; and that the denials of factual contentions are warranted.

concluded that reasonable investor would have taken the company's statements to mean that it had not retained any person or any entity to promote its securities, when the company had, in fact, done so.

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

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*, 97 F.4th 634 (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."

In May 2020, the company announced its development of a COVID-19 antibody. While the company's stock price increased following the initial announcement, the company experienced a stock drop after questions arose concerning the importance of the development. Plaintiff filed suit alleging that the company falsely claimed to have developed a COVID-19 cure, misleading investors in violation of Section 10(b) and Rule 10b-5. The district court dismissed finding that the assertion, "We want to emphasize there is a cure. There is a solution that works 100 percent," was "a statement of corporate optimism" that "cannot state an actionable material misstatement of fact under federal securities law." The district court concluded plaintiff failed to sufficiently plead the existence of false or misleading statements when the court reviewed the statements within the context of each entire article.

On appeal, the Ninth Circuit affirmed concluding that while defendants' "enthusiasm . . . might have been overblown, in context, their statements were not materially misleading." The court further 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 further took 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 and 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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