March 2021

# Securities Enforcement and Litigation Update

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## INTRODUCTION

The beginning of 2021 brings a new presidential administration and leadership at the SEC. President Biden has nominated Gary Gensler as Chairman of the SEC to replace Jay Clayton, who stepped down in December and will be returning to S&C as Senior Policy Advisor and of counsel. Gary Gensler previously served as Chairman of the CFTC from May 2009 to January 2014. There will also soon be new leadership at the SEC's Enforcement Division, with Co-Director of the Enforcement Division, Steven Peikin, returning to S&C to lead the Firm's Securities & Commodities Investigations & Enforcement Practice. These changes in leadership may have significant ramifications for enforcement activity by the SEC in the upcoming months and years.

In 2020, there was a reduction in securities enforcement activity compared to recent years, likely due in large part to the ongoing COVID-19 pandemic. But in terms of both the amount of monetary remedies and whistleblower awards, 2020 was a historic year for the SEC. And the SEC might seek still greater authority in this area in 2021. Although the Supreme Court's recent decision in *Liu* v. *SEC* established important limitations on the SEC's disgorgement authority, the SEC may take the position that federal legislation enacted in January 2021 removes those limitations. The SEC continued to focus on protecting "Main Street" investors in 2020, as well as on actions against both corporate entities and individuals, returning money to investors, accelerating the pace of

investigations, and rewarding cooperation. In the digital assets space, the SEC is scrutinizing digital asset offerings and has initiated enforcement actions where it has concluded that offerings meet the definition of a security but lack registration or exemption.

Private securities litigation in 2020 saw a significant reduction in class action filings, both in federal and state courts. Claims under the Securities Act of 1933 ("1933 Act") reached their lowest level since the Supreme Court's 2018 decision in *Cyan, Inc.* v. *Beaver County Employees Retirement Fund*, with courts in California consistently upholding the enforceability of federal forum selection provisions in corporate governing documents. Meanwhile, the First Department issued its first post-*Cyan* appellate decisions, reviewing New York trial courts' considerations of motions to dismiss and a motion to vacate a stay in favor of a parallel federal action. As to claims under the Securities Exchange Act of 1934 ("1934 Act"), the Supreme Court will consider the standards to be applied by courts when defendants seek to rebut the "fraud-on-the-market" presumption of class-wide reliance established in *Basic Inc.* v. *Levinson*. Lower courts also continue to grapple with the reach of the "safe harbor" for "forward-looking" statements under the Private Securities Litigation Reform Act of 1995 ("PSLRA"), reaching divergent conclusions on the applicability of that provision to material omissions and "mixed" statements combining both forward-looking and non-forward-looking aspects. Shareholder suits related to environmental, social, and governance ("ESG") disclosures, as well as special purpose acquisition companies ("SPACs"), increased in 2020 and will likely continue to grow in 2021 as interest in ESG disclosures and SPACs surges.

The effects of the ongoing COVID-19 pandemic on SEC enforcement and private securities litigation persist. The SEC has issued a variety of guidance on COVID-related disclosures and has continued to bring enforcement actions against companies for allegedly making fraudulent COVID-related claims and for failing to fully disclose the impact of the pandemic on continuing operations. Similarly, private securities litigation has thus far predominantly involved companies' responses to COVID-19 and pandemic-related disclosures.

This update discusses recent developments in both SEC enforcement and private securities litigation. With respect to SEC enforcement, the update addresses: (i) recent numerical trends; (ii) the Enforcement Division's areas of focus; (iii) the legislative response to *Liu* and *Kokesh* v. *SEC*; (iv) the SEC whistleblower program; (v) digital asset offering cases; and (vi) COVID-related developments. From the perspective of private securities litigation, the update discusses: (i) recent numerical trends; (ii) the post-*Cyan* state court landscape; (iii) lower courts' application of the PSLRA's safe harbor; (iv) the Supreme Court's review of the Second Circuit's decision in *Goldman Sachs Group, Inc.* v. *Arkansas Teacher Retirement System* on the standards for rebutting the *Basic* presumption; (v) shareholder suits related to ESG disclosures; (vi) shareholder suits related to SPACs; and (vii) the effects of COVID-19 on securities litigation.

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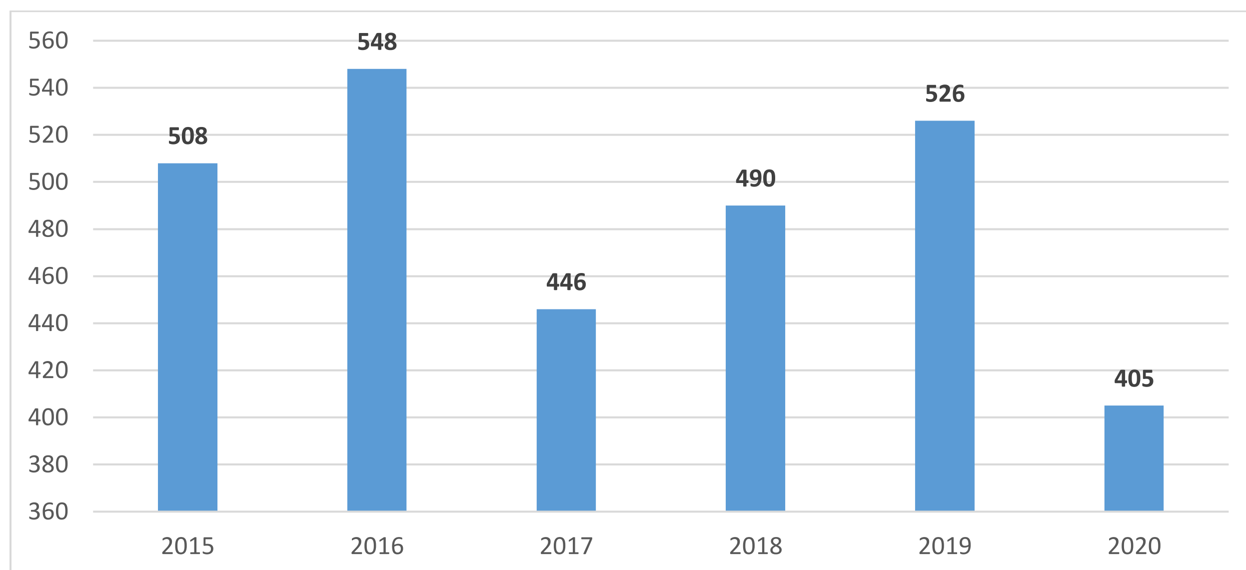
# I. PART 1 – SECURITIES ENFORCEMENT

## A. NUMERICAL TRENDS IN SEC ENFORCEMENT

Despite the ongoing challenges posed by COVID-19, the SEC continues to conduct investigations and bring enforcement actions at a strong pace. After increasing in each fiscal year from 2017 to 2019, the number of standalone enforcement actions decreased in fiscal year 2020 (which ended September 30, 2020).[1] In 2020, the SEC brought 405 standalone actions, down from 526 in 2019.[2] The decline in the number of actions is attributable largely to the disruptions resulting from COVID-19, as well as the fact that the prior year included numerous actions filed as part of the SEC's Share Class Selection Disclosure self-reporting initiative. In 2020, three enforcement areas drove the majority of the SEC's standalone cases: (i) securities offerings cases at 32%; (ii) investment advisors and investment company cases at 21%; and (iii) issuer reporting and audit and accounting cases at 15%.[3] The SEC also brought actions relating to broker-dealers (10%), insider trading (8%), market manipulation (5%), public finance (3%), and the Foreign Corrupt Practices Act (2%).[4] Across enforcement areas, the SEC continued to pursue charges against individuals; 72% of the SEC's standalone cases involved charges against one or more individuals.[5]

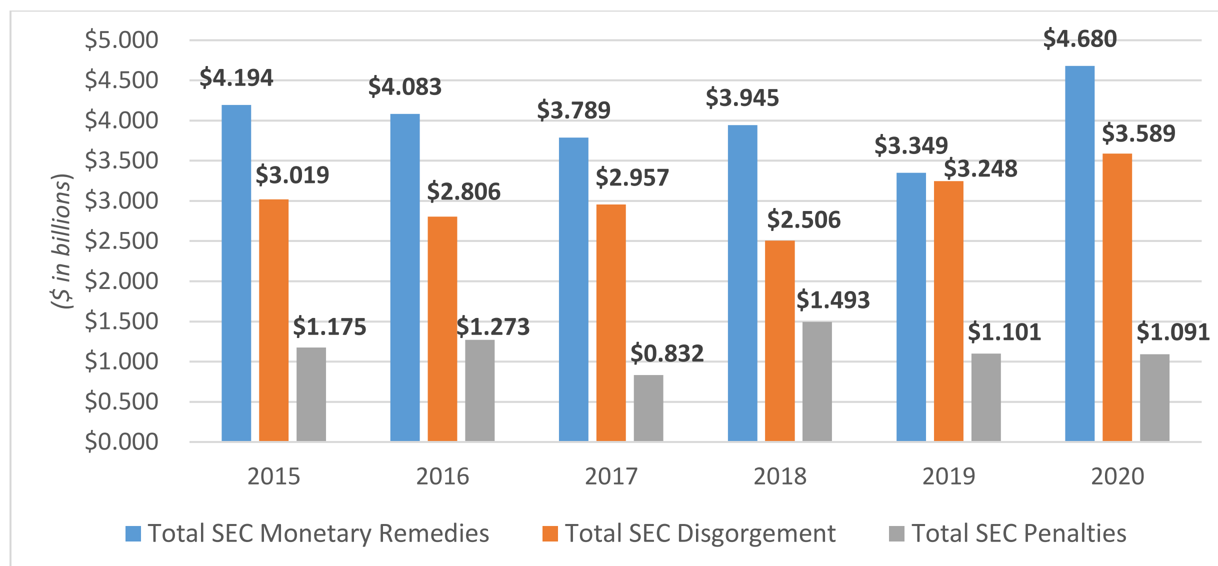
**Standalone SEC Enforcement Actions FY 2015 to 2020**




[1] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 16.
[2] *Id.*
[3] *Id.*
[4] *Id.*
[5] *Id.* at 21.

Notwithstanding the drop in the number of standalone enforcement actions, the SEC recovered the highest amount of monetary remedies on record.[6] In fiscal year 2020, the SEC obtained approximately $4.68 billion in disgorgement and penalties ($3.59 billion in disgorgement and $1.09 billion in penalties), up from approximately $4.35 billion ($3.25 billion in disgorgement and $1.1 billion in penalties) in fiscal year 2019.[7] The median amount recovered by the SEC per case in 2020 was $532,860, which was down slightly from the $554,033 median amount in 2019.[8]

**Total SEC Monetary Remedies, Disgorgement, and Penalties FY 2015 to 2020**




## B. FOCUS AREAS OF SEC ENFORCEMENT

The Enforcement Division's Annual Report provides insight into its areas of focus. In its 2020 Annual Report, the Enforcement Division highlighted a number of such areas of enforcement focus.

***Actions Against Entities.*** In 2020, the Enforcement Division brought many enforcement actions against entities, including major financial institutions, automobile companies, telecommunications companies, and pharmaceutical companies.[9] For example, the SEC settled charges against General Electric Co. for violations of the antifraud, reporting, and disclosure and accounting controls provisions of the federal securities laws.[10] Specifically, the SEC alleged that General Electric misled investors by failing to disclose financial and operating information related to its power and insurance businesses.[11] As part of the

[6] *Id.* at 17.
[7] *Id.*
[8] *Id.* at 18.
[9] *Id.* at 3.
[10] Press Release, *General Electric Agrees to Pay $200 Million Penalty for Disclosure Violations*, SECURITIES AND EXCHANGE COMMISSION (Dec. 9, 2020), https://www.sec.gov/news/press-release/2020-312.
[11] *Id.*

settlement, without admitting or denying the SEC's findings, General Electric agreed to pay $200 million in penalties, report certain accounting and disclosure controls for its power and insurance businesses to the SEC for one year, and cease-and-desist from any further violations.[12]

***Actions Against Individuals***. The Enforcement Division has continued to focus on bringing enforcement actions against individuals, stating that "holding culpable individuals responsible for wrongdoing is essential to achieving [its] goals of general and specific deterrence and protecting investors."[13] In 2020, 72% of the SEC's standalone actions included charges against at least one individual.[14] Some of the individuals charged by the SEC include top corporate executives, including CEOs and CFOs, in addition to accountants and auditors.[15] For example, on July 31, 2020, the SEC announced that Bausch Health (formerly Valeant Pharmaceuticals) and three former executives—the CEO, CFO, and controller—agreed to pay penalties to settle charges of improper revenue recognition and misleading disclosures.[16] The SEC alleged that Bausch and its former executives misled investors by misstating Bausch's revenue transactions when announcing certain GAAP and non-GAAP financial measures.[17]

***"Main Street" Investors***. Both recently departed SEC Chairman Jay Clayton and the Enforcement Division have stated that protecting retail investors is a core principle of the SEC.[18] Protecting retail investors remained an important priority of the Enforcement Division in 2020.[19] Cases brought by the SEC in 2020 covered a broad range of conduct affecting different retail investor populations.[20] For example, the SEC settled charges against Wells Fargo for allegedly failing to reasonably supervise certain investment advisors who recommended complex, single-inverse exchange-traded-fund investments to retail investors and for allegedly lacking adequate compliance policies and procedures related to the recommendations.[21] As part of the settlement, Wells Fargo, without admitting or denying the SEC's findings, agreed to pay a penalty of $35 million, which the SEC will return to investors.[22]

The SEC and the Enforcement Division's Retail Strategy Task Force also continued their work to educate vulnerable retail investors about potential scams.[23] For example, in September 2020, the Retail Strategy Task Force developed a video to educate and protect the Deaf, Hard of Hearing, and Hearing Loss

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[12] *Id.*
[13] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 4-5.
[14] *Id.*
[15] *Id.*
[16] Press Release, *Pharmaceutical Company and Former Executives Charged With Misleading Financial Disclosures* (July 31, 2020), https://www.sec.gov/news/press-release/2020-169.
[17] *Id.*
[18] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 2, 10-11; Jay Clayton, SEC Chairman, *Remarks at the Economic Club of New York*, SECURITIES AND EXCHANGE COMMISSION (July 12, 2017), https://www.sec.gov/news/speech/remarks-economic-club-new-york.
[19] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 4.
[20] *Id.* at 12.
[21] *Id.* at 5; Press Release, *SEC Charges Wells Fargo In Connection With Investment Recommendation Practices*, SECURITIES AND EXCHANGE COMMISSION (Feb. 27, 2020), https://www.sec.gov/news/press-release/2020-43.
[22] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 5.
[23] *Id.* at 12.

communities from fraud.[24] This effort by the Retail Strategy Task Force was in response to the SEC's enforcement action against an individual who engaged in a fraudulent scheme harming thousands of retail investors, including hundreds from the Deaf, Hard of Hearing, and Hearing Loss communities.[25]

As a result of the SEC's focus on protecting retail investors, the operations, activities, and disclosures of investment managers, investment advisors, broker-dealers, auditors, issuers, and other public companies continue to remain under close scrutiny by the SEC.

***Returning Money to Investors***. The Enforcement Division created the Office of Bankruptcy, Collections, Distributions, and Receiverships to further the SEC's commitment to returning money to harmed investors. In fiscal year 2020, the SEC returned more than $600 million to harmed investors, comprising more than 800,000 payments to investors from 91 fair funds and court-appointed administrators.

***Accelerating the Pace of Investigations***. The SEC has continued to accelerate the pace of its investigations.[26] In 2020, the median amount of time between the SEC opening an investigation and filing an enforcement action was 21.6 months, which was the shortest length in five years.[27] For example, in September 2020, the SEC filed an enforcement action against the co-chair of the unsecured creditors committee in Neiman Marcus's Chapter 11 bankruptcy proceedings within five weeks of the alleged misconduct.[28] The SEC alleged that the co-chair abused his position on the committee to benefit a management firm that he founded and where he served as managing partner and portfolio manager.[29] The Enforcement Division also saw improvements in the pace of its financial fraud and issuer disclosure cases, reducing the average time it takes to complete an investigation from 37 months in 2019 to 34 months in 2020.[30]

***Rewarding Cooperation***. In 2020, the Enforcement Division continued to reward cooperation in an effort to accelerate its investigations.[31] The Enforcement Division also focused on providing greater transparency into its process for rewarding cooperation and weighing cooperation credit.[32] For example, in settling charges against BMW for disclosing inaccurate information about BMW's retail sales volume, the SEC reduced BMW's penalty as a result of BMW's cooperation.[33] Specifically, the Enforcement Division

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[24] *Id.*; *SEC Fireside Chat: A Video and Q&A About Red Flags of Investment Fraud Affecting the Deaf, Hard of Hearing and Hearing Loss Communities*, SECURITIES AND EXCHANGE COMMISSION (Sept. 29, 2020), https://www.sec.gov/news/sec-videos/protecting-hearing-loss-communities-fraud.

[25] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 12; Press Release, *SEC Charges Swedish National with Global Scheme Defrauding Retail Investors, Including Deaf Community Members*, SECURITIES AND EXCHANGE COMMISSION (Sept. 29, 2020), https://www.sec.gov/news/press-release/2020-232.

[26] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 6.

[27] *Id.*

[28] Press Release, *SEC Charges Fund Manager for Fraud in Securities Offering in Neiman Marcus Bankruptcy*, SECURITIES AND EXCHANGE COMMISSION (Sept. 3, 2020), https://www.sec.gov/news/press-release/2020-203.

[29] *Id.*

[30] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 6.

[31] *Id.*

[32] *Id.*

[33] *Id.*; Press Release, *SEC Charges BMW for Disclosing Inaccurate and Misleading Retail Sales Information to Bond Investors*, SECURITIES AND EXCHANGE COMMISSION (Sept. 24, 2020), https://www.sec.gov/news/press-release/2020-223.

emphasized that BMW, despite the challenges posed by COVID-19, collected and provided a large volume of information, data, and documents, as well as made available multiple current and former employees for interviews.[34] The SEC noted that BMW's cooperation allowed the SEC to finish its investigation in less than 12 months.[35] Additionally, in settling charges against Transamerica Asset Management for making misrepresentations regarding expenses charged by money market funds managed by Transamerica, the SEC declined to impose a penalty against Transamerica.[36] The Enforcement Division highlighted that Transamerica self-reported the conduct at issue, immediately worked to remediate it, and cooperated with the SEC's investigation.[37]

### C. THE *LIU/KOKESH* FIX LEGISLATION

Responding to the Supreme Court's recent decisions in *Kokesh* v. *SEC* and *Liu* v. *SEC*, on January 1, 2021, Congress passed legislation amending Section 21(d) of the 1934 Act to expand significantly the SEC's ability to obtain disgorgement and other remedies.[38]

The previous version of Section 21(d) authorized the SEC to obtain "any equitable relief . . . for the benefit of investors," but it did not expressly include disgorgement as a remedy.[39] Historically, "equitable relief" has been interpreted to exclude "punitive" remedies.[40]

In *Kokesh*, the Supreme Court held that disgorgement "bears all the hallmarks of a penalty," and is therefore subject to the five-year limitations period in 28 U.S.C. § 2462.[41] Notably, the Court expressly left open the question of "whether courts possess authority to order disgorgement in SEC enforcement proceedings" under the previous version of Section 21(d).[42] The impact of *Kokesh* on SEC disgorgement was nevertheless substantial. In 2019, the SEC estimated that, to that point, *Kokesh* had caused it to forgo seeking in the aggregate approximately $1.1 billion in disgorgement in its filed cases.[43]

In *Liu*, the Supreme Court answered the question left open by *Kokesh*, holding that disgorgement is a type of "equitable relief" that the SEC may obtain, but that such disgorgement awards may not exceed the wrongdoer's net profits or include proceeds held by another or that are not intended to be returned to victim investors.[44]

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[34] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 6.
[35] *Id.*
[36] *Id.* at 7; Press Release, *Denver Investment Adviser Settles Charges for Disclosure Failures*, SECURITIES AND EXCHANGE COMMISSION (Sept. 30, 2020), https://www.sec.gov/enforce/ia-5599-s.
[37] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 7.
[38] William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, H.R. 6395, 116th Cong. § 6501 (2021) (enacted).
[39] 15 U.S.C. § 78u(d)(5).
[40] *Kokesh* v. *SEC*, 137 S. Ct. 1635, 1644 (2017).
[41] *Id.*
[42] *Id.* at 1642 n.3.
[43] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2019 ANNUAL REPORT 21 (2019).
[44] *Liu* v. *SEC*, 140 S. Ct. 1936, 1940, 1946-50 (2020).

Congress amended Section 21(d) in three important ways in response to *Liu* and *Kokesh*. *First*, it amended Section 21(d) to expressly provide for disgorgement. The new language authorizes the SEC to seek, and federal courts to order, "disgorgement . . . of any unjust enrichment . . . as a result of [a] violation" of the federal securities laws.[45] Disgorgement therefore now has an independent statutory basis, not one derived solely from a court's authority to order equitable relief. *Second*, the amendments to Section 21(d) increase the statute-of-limitations periods for claims by the SEC seeking disgorgement and other equitable remedies. The new language allows the SEC to bring disgorgement claims within "5 years [of] the latest date of the violation" of any of the federal securities laws, and within "10 years [of] the latest date of the violation . . . if the violation involves conduct that violates" any scienter-based provisions of the securities laws.[46] *Third*, the new language provides that the SEC "may seek a claim for any equitable remedy, including for an injunction or for a bar, suspension, or cease and desist order" within "10 years [of] the latest date on which a violation . . . occurs."[47] These new amendments apply to "any [SEC] action or proceeding that is pending on, or commenced on or after," January 1, 2021.[48]

The new provisions of Section 21(d) will enhance the SEC's ability to recover remedies from violators of the federal securities laws and are likely to lead to higher-value resolutions in some SEC enforcement actions. Although it remains to be seen how the SEC and courts will interpret the scope of the new provisions, the SEC may take the position that the significant limitations on the scope of permissible disgorgement set forth in *Liu* may no longer apply. Additionally, the statute meaningfully enlarges the time period during which the SEC can reach back to seek disgorgement and other equitable remedies from violators of the federal securities laws.

## D. SEC WHISTLEBLOWER PROGRAM

The SEC's whistleblower program continued its strong growth through 2020—the 10-year anniversary of the creation of the program. The Commission reported that it was a "record-breaking" and "momentous" year for the program, with approximately $175 million in whistleblower awards made to 39 individuals—each of which was the largest amount in the program's history.[49] Also in 2020, the SEC issued the largest number of final orders resulting in whistleblower awards, processed the most whistleblower claims, and received the highest number of whistleblower tips in a single fiscal year in the program's history.[50]

[45] William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, H.R. 6395, 116th Cong. § 6501(a)(1) (2021) (enacted) ("Section 21(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(d)) is amended . . . [to include] . . . disgorgement . . . of any unjust enrichment by the person who received such unjust enrichment as a result of such violation.").

[46] *Id.* § 6501(a)(3) ("Section 21(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(d)) is amended [to include limitations periods in which] . . . [t]he Commission may bring a claim for disgorgement . . . not later than 5 years after the latest date of the violation that gives rise to the action or proceeding in which the Commission seeks the claim occurs; or . . . not later than 10 years after the latest date of the violation that gives rise to the action or proceeding in which the Commission seeks the claim if the violation involves conduct that violates . . . section 10(b); . . . section 17(a)(1) of the Securities Act of 1933 (15 U.S.C. 77q(a)(1)); . . . section 206(1) of the Investment Advisors Act of 1940 (15 U.S.C. 80b-6(1)); or . . . any other provision of the securities laws for which scienter must be established.").

[47] *Id.*

[48] *Id.* § 6501(b).

[49] SECURITIES AND EXCHANGE COMMISSION, 2020 ANNUAL REPORT TO CONGRESS: WHISTLEBLOWER PROGRAM, at 1-2 (2020).

[50] *Id.*

In addition to the continued growth, the SEC made revisions to the program's rules. On September 23, 2020, the SEC adopted amendments to "provide greater clarity to whistleblowers," "increase the program's efficiency and transparency," and ensure whistleblowers are properly incentivized.[51] The amendments went into effect on December 7, 2020.[52] Five changes are notable.

*First*, the amended rules create procedures to presumptively award the statutory maximum amount of 30% of monetary sanctions collected to meritorious claimants when the maximum award is $5 million or less—which represents the substantial majority of all whistleblower awards to date.[53] *Second*, the amended rules authorize awards for whistleblower information leading to a deferred or non-prosecution agreement entered into by the Department of Justice or a settlement by the SEC outside of a judicial or administrative proceeding to address federal securities laws violations.[54] *Third*, the amended rules require whistleblowers to submit written reports to the SEC for all aspects of Section 21F of the 1934 Act, including award program eligibility, heightened confidentiality protections, and anti-retaliation protections.[55] Under Section 21F of the 1934 Act, an employer may not "discharge, demote, suspend, threaten, harass, directly or indirectly, or in any other manner discriminate against, a whistleblower in the terms and conditions of employment because of any lawful act done by the whistleblower" related to providing information to the SEC.[56] *Fourth*, the amended rules create procedures that allow the SEC to permanently bar individuals from submitting frivolous or false award applications and to prevent whistleblowers from receiving an award from the SEC if the SEC determines that a whistleblower will also receive an award from another whistleblower award program (*e.g.*, the CFTC's whistleblower program).[57] *Fifth*, the amended rules clarify the meaning of "independent analysis" as the term is defined in Rule 21F-4 of the 1934 Act, which requires a whistleblower to submit "original information" derived from "independent knowledge" or "independent analysis."[58] The new language requires a whistleblower to provide the SEC with evaluation, assessment, or insight beyond what would be reasonably apparent from publicly available information.[59]

The amended rule requiring whistleblowers to submit written reports to the SEC for award program eligibility is a response to the Supreme Court's decision in *Digital Realty Trust, Inc.* v. *Sommers.*[60] In *Digital Realty*, the Court unanimously held that the anti-retaliation protections for whistleblowers afforded by the Dodd-Frank Act apply only to individuals who report alleged misconduct to the SEC.[61] The Court noted that the Dodd-Frank Act "delineates a more circumscribed class" of individuals eligible for whistleblower protections

[51] *Id.* at 33.
[52] *Id.*
[53] *Id.*
[54] *Id.*
[55] *Id.* at 34.
[56] 15 U.S.C. § 78u-6(h)(1)(A).
[57] SECURITIES AND EXCHANGE COMMISSION, 2020 ANNUAL REPORT TO CONGRESS: WHISTLEBLOWER PROGRAM, at 35.
[58] 17 C.F.R. § 240.21F-4(h)(1).
[59] SECURITIES AND EXCHANGE COMMISSION, 2020 ANNUAL REPORT TO CONGRESS: WHISTLEBLOWER PROGRAM, at 37.
[60] *Id.* at 34.
[61] *Digital Realty Trust, Inc.* v. *Sommers*, 138 S. Ct. 767, 777 (2018).

than the Sarbanes-Oxley Act, which affords whistleblower protections to employees who report violations to the SEC, other federal agencies, Congress, or internal supervisors.[62]

### E. DIGITAL ASSET OFFERING CASES

The SEC continues to closely scrutinize digital asset offerings and distributions of digital tokens to determine whether they are securities that require registration or exemption. As recently departed SEC Chairman Jay Clayton stated, "I believe every [digital asset offering] I have ever seen is a security. . . . [digital asset offerings] should be regulated like securities offerings. End of story."[63] Similarly, recently departed SEC Director of Corporation Finance Bill Hinman stated that "calling the transaction [a digital asset offering] or a sale of a 'token,' will not take it out of the purview of the U.S. securities laws."[64] As a result, the SEC has continued to bring enforcement actions and prosecute cases related to digital asset offerings and distributions of digital tokens without registration or exemption. Three recent actions are noteworthy.

On June 26, 2020, a federal court entered a final judgment against Telegram Group Inc. and its wholly owned subsidiary, TON Issuer Inc., following a settlement agreement with the SEC, requiring Telegram to return $1.2 billion in disgorgement to investors and pay an $18.5 million penalty for violations of federal securities laws related to Telegram's public sale of digital tokens.[65] The judgment also permanently restrains and enjoins Telegram from violating Section 5 of the 1933 Act and requires Telegram to notify the SEC before Telegram issues, offers, sells, or transfers digital assets similar to cryptocurrencies, coins, or tokens, or which are issued or transferred using distributed ledger technology for a period of three years.[66] In 2018, Telegram offered and sold digital tokens called "Grams" for the TON blockchain to 175 sophisticated investors in exchange for $1.7 billion.[67] On October 11, 2019, the SEC filed a complaint alleging that the digital tokens were securities that Telegram offered and sold without registration or exemption in violation of Section 5 of the 1933 Act.[68] In a previously issued decision granting the SEC's motion for preliminary injunction, the court concluded that the SEC had shown a "substantial likelihood of success," and that the unregistered distribution of Grams constituted a securities offering that did not comply with Section 5 of the 1933 Act.[69] Specifically, the court found that the elements of the *SEC* v. *W.J. Howey Co.* test were likely satisfied because Telegram's digital tokens involved an investment of money, Telegram established a common enterprise in which investor profits depended on the TON blockchain, and

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[62] *Id.* at 772.
[63] Jay Clayton, *Testimony on Virtual Currencies: The Oversight Role of the U.S. Securities and Exchange Commission and the U.S. Commodity Futures Trading Commission*, U.S. SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS (Feb. 6, 2018), https://www.banking.senate.gov/hearings/virtual-currencies-the-oversight-role-of-the-us-securities-and-exchange-commission-and-the-us-commodity-futures-trading-commission.
[64] Bill Hinman, *Digital Asset Transactions: When Howey Met Gary (Plastic)*, SECURITIES AND EXCHANGE COMMISSION (June 14, 2018), https://www.sec.gov/news/speech/speech-hinman-061418.
[65] *SEC* v. *Telegram Group Inc. & TON Issuer Inc.*, No. 19-cv-09439, Dkt. No. 242, at 3–4 (S.D.N.Y. June 26, 2020).
[66] *Id.* at 1–3.
[67] *See SEC* v. *Telegram Group Inc.*, 448 F. Supp. 3d 352, 358 (S.D.N.Y. 2020).
[68] *SEC* v. *Telegram Group Inc. & TON Issuer Inc.*, No. 19-cv-09439, Dkt. No. 1, ¶¶ 1–2 (S.D.N.Y. Oct. 11, 2019).
[69] *Telegram*, 448 F. Supp. 3d at 381.

Telegram's promotion of the digital tokens established an expectation of profits based on the efforts of others.[70] The court further determined that Telegram's unregistered offering and distribution of Grams was "a disguised public distribution" that rendered exemptions under Section 4(a)(2) of the 1933 Act and Rule 506(c) of Regulation D inapplicable.[71] A few months after the injunction was issued, Telegram settled with the SEC without admitting or denying the complaint's allegations.[72]

On October 21, 2020, a federal court entered a final judgment against Kik Interactive Inc., following a settlement agreement with the SEC, requiring Kik to pay a $5 million penalty for violations of federal securities laws related to Kik's unregistered public sale of digital tokens in 2017.[73] The judgment also permanently restrains and enjoins Kik from violating Section 5 of the 1933 Act and requires Kik to notify the SEC before Kik issues, offers, sells, or transfers digital assets similar to cryptocurrencies, coins, or tokens, or which are issued or transferred using distributed ledger technology for a period of three years.[74] Between June and September 2017, Kik offered and sold digital tokens called "Kin" for in-app purchases on its blockchain network to accredited investors.[75] On June 4, 2019, the SEC filed a complaint alleging that Kik offered and sold its digital tokens without registration or exemption in violation of Section 5 of the 1933 Act.[76] In its decision granting the SEC's motion for summary judgment, the court concluded that Kik's sale of digital tokens to the public was a sale of a security requiring either registration or exemption.[77] Specifically, the court found that the elements of the *Howey* test were satisfied because Kik's digital token public distribution involved an investment of money, Kik established a common enterprise in which investors realized profits through the digital tokens' increased value, and Kik's public statements promoting the digital tokens established an expectation of profits based on the efforts of others.[78] The court further determined that the private pre-sale of the digital tokens integrated with the public distribution, thus rendering inapplicable an exemption under Rule 506(b) of Regulation D.[79]

On December 22, 2020, the SEC filed a complaint alleging that Ripple Labs, Inc. and two of its executives sold unregistered digital asset securities for $1.38 billion.[80] The SEC's complaint seeks injunctive relief, disgorgement, and civil penalties.[81] According to the complaint, Ripple began raising funds in 2013 to finance the company's business through the sale of digital assets called "XRP" to investors.[82] After Ripple and its executives allegedly ignored legal advice that XRP could be considered a security under federal

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[70] *Id.* at 368–80 (citing *SEC* v. *W.J. Howey Co.*, 328 U.S. 293 (1946)).
[71] *Id.* at 380.
[72] Press Release, *Telegram to Return $1.2 Billion to Investors and Pay $18.5 Million Penalty to Settle SEC Charges*, SECURITIES AND EXCHANGE COMMISSION (June 26, 2020), https://www.sec.gov/news/press-release/2020-146.
[73] *SEC* v. *Kik Interactive Inc.*, No. 19-cv-05244, Dkt. No. 90, at 3 (S.D.N.Y. Oct. 21, 2020).
[74] *Id.* at 1–3.
[75] *SEC* v. *Kik Interactive Inc.*, No. 19-cv-05244, Dkt. No. 88, at 2–5 (S.D.N.Y. Sept. 30, 2020).
[76] *Id.* at 7.
[77] *Id.* at 9.
[78] *Id.* at 9–14.
[79] *Id.* at 14–17.
[80] *SEC* v. *Ripple Labs, Inc.*, No. 20-cv-10832, Dkt. No. 4, ¶¶ 1–2 (S.D.N.Y. Dec. 22, 2020).
[81] *Id.* at 70.
[82] *Id.* ¶¶ 1–2.

securities laws, they allegedly initiated a distribution of XRP to investors without filing a registration statement.[83] Ripple's CEO and the chairman of Ripple's board of directors also allegedly personally profited approximately $600 million from the unregistered sale of XRP in the absence of a registration statement at the time of the complaint's filing.[84] On January 29, 2021, Ripple filed its answer to the SEC's complaint, asserting that XRP is a virtual currency that is not subject to securities regulation, which securities regulators in the United Kingdom, Japan, and Singapore have also concluded.[85]

These cases suggest that the SEC will continue to scrutinize whether digital asset offerings meet the definition of a security, which requires filing a registration statement or applying an exemption. Further, the SEC will likely continue to initiate enforcement actions where it concludes that offerings meet the definition of a security and lack registration or exemption.

### F. COVID-19 RELATED DEVELOPMENTS

The COVID-19 pandemic continues to have a significant impact on the SEC's enforcement priorities. In March 2020, the SEC formed a Coronavirus Steering Committee to coordinate the SEC's investigations related to an array of potential coronavirus-related wrongdoing.[86] Composed of leaders from the Enforcement Division, the Committee is tasked with identifying and monitoring areas of misconduct, ensuring appropriate allocation of SEC resources, coordinating the SEC's responses with those of other state and federal agencies, and ensuring consistency in the SEC's investigations and enforcements in coronavirus-related matters.[87]

As a result of the Committee's work, the SEC suspended trading in the securities of over 30 issuers due to concerns about the adequacy and accuracy of the issuers' coronavirus-related statements.[88] For example, the SEC has suspended trading when issuers have made questionable claims about potential COVID-19 treatments, personal protection equipment, and disaster-response capabilities.[89] The SEC has stated that although a trading suspension is not an enforcement action or a finding of wrongdoing, further investigation into potential wrongdoing may lead to an enforcement action in some cases.[90] For example, after suspending trading in the securities of Praxsyn Corporation in March 2020, the SEC filed fraud charges against Praxsyn and its CEO a month later for allegedly making false claims that the company could supply large quantities of N95 or comparable masks.[91] On August 21, 2020, Praxsyn and its CEO jointly agreed

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[83] *Id.* ¶¶ 3–4.
[84] *Id.* ¶¶ 6–8.
[85] *SEC* v. *Ripple Labs, Inc.*, No. 20-cv-10832, Dkt. No. 43, ¶¶ 1–3 (S.D.N.Y. Jan. 29, 2021).
[86] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 2.
[87] Steven Peikin, *Keynote Address: Securities Enforcement Forum West 2020*, SECURITIES AND EXCHANGE COMMISSION (May 12, 2020), https://www.sec.gov/news/speech/keynote-securities-enforcement-forum-west-2020.
[88] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 2.
[89] *Id.*
[90] *Information Regarding Trading Suspensions and COVID-19*, SECURITIES AND EXCHANGE COMMISSION, https://www.sec.gov/files/information-regarding-trading-suspensions-covid-19_1.pdf.
[91] SECURITIES AND EXCHANGE COMMISSION DIVISION OF ENFORCEMENT, 2020 ANNUAL REPORT, at 2, 26.

to pay $65,000 in penalties to the SEC to settle the fraud charges.[92] The SEC has further stated that it will not hesitate to recommend similar actions against other market actors that make fraudulent coronavirus-related claims.[93]

On March 25, 2020, the SEC's Division of Corporation Finance issued guidance to companies on disclosures during the COVID-19 pandemic.[94] The guidance explained that the SEC is "monitoring how companies are reporting the effects and risks of COVID-19 on their businesses" and provided a series of questions related to the impact of COVID-19 on a company's finances and operations to consider when making disclosures.[95] The guidance also addressed reporting earnings and other financial results, including noting that "[t]o the extent a company presents a non-GAAP financial measure or performance metric to adjust for or explain the impact of COVID-19, it would be appropriate to highlight why management finds the measure or metric useful and how it helps investors assess the impact of COVID-19 on the company's financial position and results of operations."[96] Shortly thereafter, then-Chairman Clayton and then-Director of Corporation Finance Bill Hinman underscored the importance of COVID-related disclosures in a public statement urging companies to provide as much information as is practicable regarding their current financial and operating status, as well as their future operational and financial planning.[97] They further stressed the importance of framing disclosures as forward-looking and providing investors with forward-looking information.[98] The Coronavirus Steering Committee has developed a systematic process for reviewing the public filings of companies in highly impacted industries to identify disclosures "significantly out of step" with others in the same industry, as well as disclosures attempting to disguise undisclosed problems as COVID-related.[99]

On July 23, 2020, the Division of Corporation Finance issued additional guidance urging companies to make "disclosures that allow investors to evaluate the current and expected impact of COVID-19 through the eyes of management and to proactively revise and update disclosures as facts and circumstances change."[100] Similar to its initial guidance, the Division of Corporation Finance provided questions related to the impact of COVID-19 to consider when making disclosures.[101] The SEC has since reaffirmed that it will

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[92] Plaintiff's Unopposed Motion for Entry of Final Judgments Against Defendants Prasxyn Corporation and Frank J. Brady at 1, *SEC v. Praxsyn Corp.*, No. 20-cv-80706, Dkt. No. 9 (S.D. Fla. Aug. 21, 2020).

[93] *Information Regarding Trading Suspensions and COVID-19*, SECURITIES AND EXCHANGE COMMISSION, https://www.sec.gov/file/information-regarding-trading-suspensions-and-covid-19.

[94] Division of Corporation Finance, *Coronavirus (COVID-19)*, SECURITIES AND EXCHANGE COMMISSION (Mar. 25, 2020), https://www.sec.gov/corpfin/coronavirus-covid-19.

[95] *Id.*

[96] *Id.*

[97] Jay Clayton & William Hinman, *The Importance of Disclosure – For Investors, Markets and Our Fight Against COVID-19*, SECURITIES AND EXCHANGE COMMISSION (Apr. 8, 2020), https://www.sec.gov/news/public-statement/statement-clayton-hinman.

[98] *Id.*

[99] Steven Peikin, *Keynote Address: Securities Enforcement Forum West 2020*, SECURITIES AND EXCHANGE COMMISSION (May 12, 2020), https://www.sec.gov/news/speech/keynote-securities-enforcement-forum-west-2020.

[100] Division of Corporation Finance, *Coronavirus (COVID-19) – Disclosure Considerations Regarding Operations, Liquidity, and Capital Resource*, SECURITIES AND EXCHANGE COMMISSION (June 23, 2020), https://www.sec.gov/corpfin/covid-19-disclosure-considerations.

[101] *Id.*

closely monitor companies' coronavirus-related disclosures and recommend actions against companies that make inadequate or misleading disclosures.[102]

For example, on December 4, 2020, the SEC announced that it had settled charges against The Cheesecake Factory for making misleading disclosures about the impact of COVID-19 on the company's finances and operations.[103] The SEC alleged that The Cheesecake Factory, in its March and April 2020 SEC filings, falsely claimed that the company's restaurants were "operating sustainably" during the COVID-19 pandemic.[104] The company's internal documents, however, suggested that the company was losing approximately $6 million per week.[105] Although the company had not disclosed its financial hardships in its SEC filings, the company did share the information with potential private equity investors when seeking additional liquidity and also informed its landlords that the company would not pay rent in April.[106] Without admitting the findings in the SEC's order alleging that The Cheesecake Factory violated the reporting provisions of the federal securities laws, The Cheesecake Factory agreed to pay a $125,000 penalty and to cease-and-desist from further violations of the reporting provisions of the federal securities laws.[107] This case further reflects that the SEC is proactively monitoring disclosures regarding the impact of COVID-19 on issuers' finances and operations.

## II. PART 2 – PRIVATE SECURITIES LITIGATION

### A. NUMERICAL TRENDS IN PRIVATE SECURITIES LITIGATION

Amid the COVID-19 pandemic, securities class action filings experienced a significant reduction in 2020, reaching the lowest level since 2016. In 2020, the total number of such filings in federal and state courts dropped to 334, a notable decline from the record-setting 427 filings in 2019.[108] "Core" filings (*i.e.*, excluding M&A-related litigation) declined to 234 in 2020, compared with 267 in 2019, 238 in 2018, and 214 in 2017.[109] Despite those year-over-year reductions, securities class action filings in 2020 were still 49% higher than the average between 1997 and 2019.[110] Core federal filings by sector did not change substantially from the previous year, with relative decreases in activity against consumer (67 filings in 2020 compared with 87 in 2019), communications (19 filings in 2020 compared with 37 in 2019), and industrial (13 filings in 2020 compared with 20 in 2019) firms.[111] Reflecting their increasing role in recent years, securities filings

[102] Press Release, *SEC Charges The Cheesecake Factory For Misleading COVID-19 Disclosures*, SECURITIES AND EXCHANGE COMMISSION (Dec. 4, 2020), https://www.sec.gov/news/press-release/2020-306.
[103] *Id.*
[104] *Id.*
[105] *Id.*
[106] *Id.*
[107] *Id.*
[108] Cornerstone Research, *Securities Class Action Filings: 2020 Year in Review*, at 5, available at https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2020-Year-in-Review.
[109] *Id.* at 38.
[110] *Id.*
[111] *Id.* at 32.

involving SPACs remained at a historically high level, with five filings in 2020, compared with six in 2019, and two or fewer filings in the previous three years.[112]

Disrupting the growth trend since the Supreme Court's 2018 decision in *Cyan, Inc.* v. *Beaver County Employees Retirement Fund*,[113] state court filings of 1933 Act claims declined by 68% in 2020, down from 52 filings in 2019 to 18 in 2020.[114] Counting both state-only and parallel filings in 2020, 12 actions were filed in New York, while four were filed in California.[115] Outside of New York and California, state filing activity reached its lowest level since 2015, with just one filing each in Massachusetts and Ohio.[116] Apart from the slowdown in private securities litigation during the COVID-19 pandemic, this reduction in state court actions may be driven by the Delaware Supreme Court's decision in *Salzberg* v. *Sciabacucchi* in March 2020, which upheld the enforceability of a federal forum provision encompassing private securities litigation in a company's certificate of incorporation.[117] Prior to the *Sciabacucchi* decision, 43% of 1933 Act filings were in state court only, a proportion that declined to 29% following the decision, with federal-only filings increasing to 58% of 1933 Act filings.[118] Since September 2020, a series of decisions in California state courts have similarly enforced such federal forum provisions in corporate governing documents. If courts in other states follow suit, state filings may continue to decline as more companies adopt federal forum provisions.

In addition, securities class actions against foreign companies listed on U.S. exchanges reached the highest figure to date, with 74 core federal filings against non-U.S. issuers in 2020, reflecting a significant increase from 56 filings in 2019.[119] In 2020, 33% of total core federal filings were against non-U.S. issuers, the second highest proportion of filings to date and the highest since 2011.[120] Consistent with previous years, core filings in 2020 against Asia-based defendants were highest at 31, including 24 Chinese firms, followed by 18 filings against European firms and 12 against Canadian firms.[121] These filings include recent litigation commenced against overseas software companies,[122] a Chinese automotive company,[123] and foreign biomedical companies.[124]

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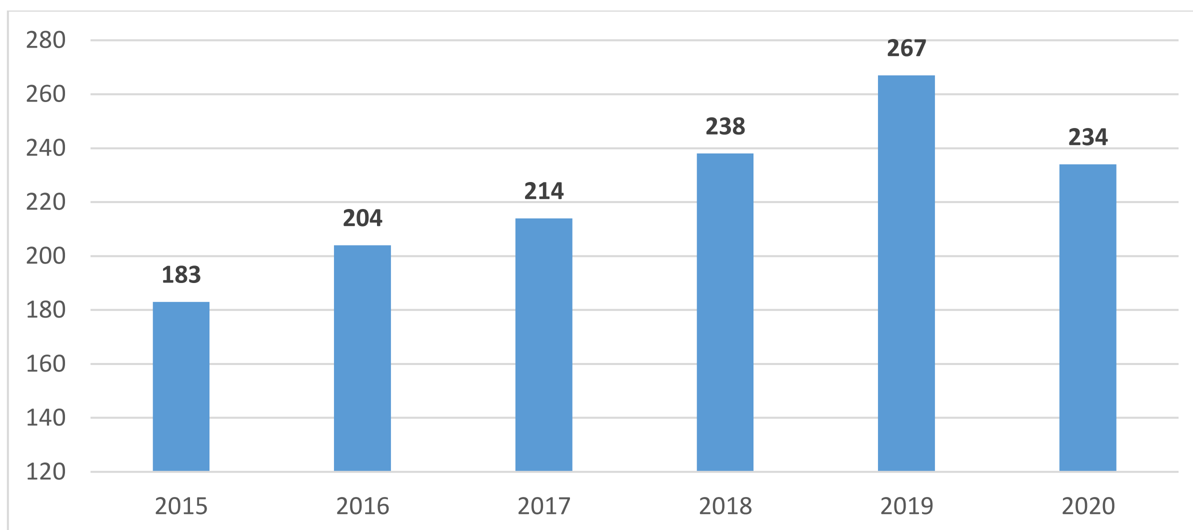
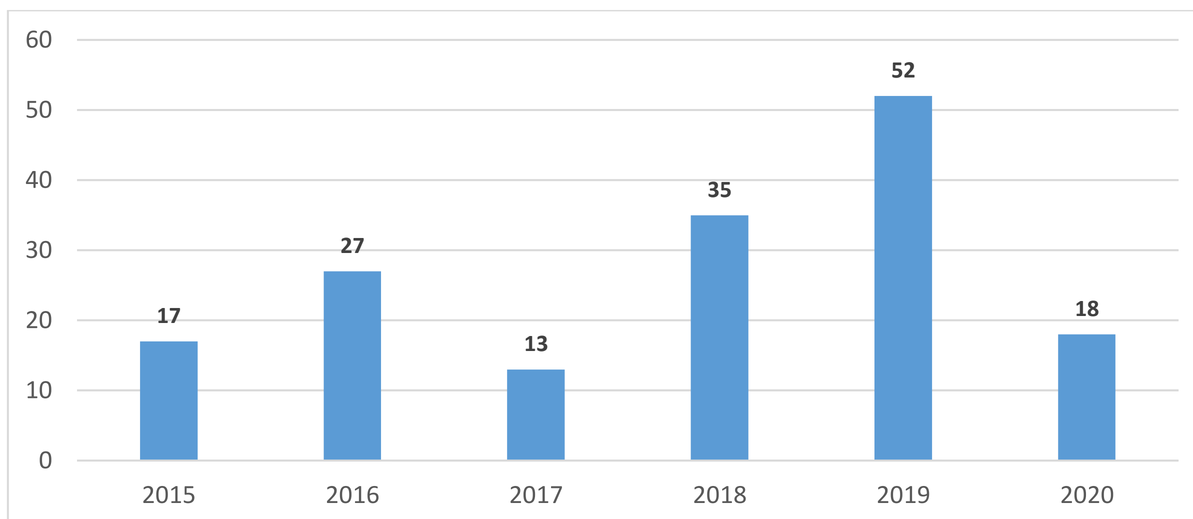
[112] *Id.* at 7.
[113] 138 S. Ct. 1061 (2018).
[114] Cornerstone Research, *Securities Class Action Filings: 2020 Year in Review*, at 19.
[115] *Id.* at 4, 19.
[116] *Id.* at 19.
[117] *Id. See Salzberg* v. *Sciabacucchi*, 227 A.3d 102 (Del. 2020).
[118] Cornerstone Research, *Securities Class Action Filings: 2020 Year in Review*, at 21.
[119] *Id.* at 28.
[120] *Id.*
[121] *Id.* at 29.
[122] *Alagappan* v. *Baidu, Inc.*, No. 20-cv-03794, Dkt. No. 1 (E.D.N.Y. Aug. 19, 2020); *Ciccarello* v. *Alibaba Grp. Holding Ltd.*, No. 20-cv-09568, Dkt. No. 1 (S.D.N.Y. Nov. 13, 2020); *Hershewe* v. *Joyy Inc.*, No. 20-cv-10611, Dkt. No. 1 (C.D. Cal. Nov. 20, 2020); *ODS Capital LLC* v. *Changyou.com Ltd.*, No. 20-cv-05973, Dkt. No. 1 (E.D.N.Y. Dec. 8, 2020); *Trampe* v. *CD Project S.A.*, No. 20-cv-11627, Dkt. No. 1 (C.D. Cal. Dec. 24, 2020); *Gutman* v. *Lizhi Inc.*, No. 21-cv-00317, Dkt. No. 1 (E.D.N.Y. Jan. 20, 2021); *Holland* v. *9F Inc.*, No. 21-cv-00948, Dkt. No. 1 (D.N.J. Jan. 20, 2021).
[123] *Valdes* v. *Kandi Tech. Grp., Inc.*, No. 20-cv-06042, Dkt. No. 1 (E.D.N.Y. Dec. 11, 2020).
[124] *See*, *e.g.*, *Alperstein* v. *Sona Nanotech Inc.*, No. 20-cv-11405, Dkt. No. 1 (C.D. Cal. Dec. 17, 2020).

**Core Securities Filings 2015 to 2020**




**State Court 1933 Act Filings 2015 to 2020**




## B. STATE COURT PROCEEDINGS FOLLOWING *CYAN INC.* v. *BEAVER COUNTY EMPLOYEES RETIREMENT FUND*

New developments in state court 1933 Act litigation in the past six months include three decisions by the New York Appellate Division, which are the first post-*Cyan* appellate considerations of rulings on a motion to dismiss and a ruling to vacate a stay of a parallel action in New York state court. In addition, in four rulings, trial courts in California have consistently upheld the enforceability of federal forum provisions governing private securities litigation contained in corporate governing documents.

***Dismissal and Stay of Cases in New York State Court.*** Since August, New York state courts have issued only a handful of decisions in securities actions under the 1933 Act. Notably, on December 3, 2020,

the First Department issued the first post-*Cyan* appellate decision in a 1933 Act action in New York. In *Lyu* v. *Ruhnn Holdings Ltd.*, the plaintiffs brought claims for violations of Sections 11, 12(a)(2), and 15 of the 1933 Act based on allegations that Ruhnn, an e-commerce company, and its underwriters made a material omission regarding certain online store closures in Ruhnn's IPO materials.[125] The trial court granted defendants' motion to dismiss as to the Section 12(a)(2) claim, but allowed the other claims to proceed after holding that the plaintiffs had adequately pleaded that the alleged omission was material.[126] The First Department unanimously reversed as to the claims under Sections 11 and 15 and upheld the dismissal of the Section 12(a)(2) claim.[127] In its relatively short opinion, the First Department reasoned that the plaintiffs had adopted a "myopic" focus on the number of online stores operated by Ruhnn since this metric "was not closely related" to the company's full-service segment from which it derived most of its revenues, and the disclosure of this metric "would not have given a more accurate picture of the status of the business."[128] In reaching its decision, the First Department cited Second Circuit precedent for financial disclosures standards for an IPO,[129] suggesting that New York courts will continue to look to prevailing federal court precedents for guidance with respect to the federal securities laws.

On February 2, 2021, in *In re Dentsply Sirona, Inc. Shareholders Litigation*, the First Department modified a trial court's dismissal of 1933 Act claims to make the dismissal with prejudice, on the basis that the claims were time-barred.[130] In this case, the trial court dismissed the plaintiffs' Section 11, 12(a)(2), and 15 claims without prejudice, finding, among other things, that the company's alleged misstatements about its competitiveness and market conditions were inactionable puffery.[131] Although the defendants argued that the claims were time-barred, the trial court declined to dismiss the complaint on statute-of-limitations grounds due to the "early stage of the litigation and because the inquiry is fact-intensive."[132] The First Department disagreed, ruling that plaintiffs' claims "should have been dismissed as time-barred" and noting that plaintiffs could have brought their claims earlier because neither Section 11 nor Section 12 requires a plaintiff to plead damages.[133] In granting dismissal with prejudice, the First Department's decision will likely strengthen the position of defendants seeking to defeat state court 1933 Act claims on statute-of-limitations grounds.

Another key issue for state court 1933 Act claims is when cases should be stayed in favor of parallel proceedings in federal court. In determining whether to stay state court 1933 Act actions, the New York courts look to general comity factors, including: (i) whether the federal action was commenced first and the stage of litigation; (ii) whether there is substantial overlap between the parties, issues, and relief requested; (iii) where a more complete disposition of issues may be obtained; (iv) whether a stay will avoid duplication

[125] 2020 WL 1939668, at *1-2 (N.Y. Sup. Ct., N.Y. Cty. Apr. 22, 2020).
[126] *Id.* at *3-5.
[127] *Lyu* v. *Ruhnn Holdings Ltd.*, 189 A.D.3d 441 (1st Dep't 2020).
[128] *Id.* at 441–42.
[129] *Id.* at 441 (citing *Stadnick* v. *Vivint Solar, Inc.*, 861 F.3d 31, 38 (2d Cir. 2017)).
[130] 2021 WL 329443, at *1 (1st Dep't Feb. 2, 2021).
[131] *In re Dentsply Sirona, Inc. S'holders Litig.*, 2019 WL 4695724, at *5 (N.Y. Sup. Ct., N.Y. Cty. Sept. 26, 2019).
[132] *Id.* at *3.
[133] *Dentsply Sirona*, 2021 WL 329443, at *1.

of effort, waste of judicial resources, and the risk of inconsistent rulings; (v) whether plaintiffs have demonstrated how they would be prejudiced by a stay; and (vi) which court has greater familiarity with the trial of such issues.[134]

As recent decisions in the New York courts have emphasized, the interaction of the first three factors is particularly significant to the stay analysis. Although the fact that a federal action was filed first is a crucial consideration, New York courts have refused to stay 1933 Act claims where there was not complete overlap between the parallel actions and the federal proceeding could not dispose of all issues raised in state court. For instance, in *Convery* v. *Jumia Technologies AG*, the New York Supreme Court refused to stay 1933 Act claims in favor of first-filed federal litigation.[135] In this case, in which S&C represented defendant Jumia Technologies and its officers, the federal complaint alleged violations of Sections 10(b) and 20(a) of the 1934 Act, while the state complaint asserted claims under Sections 11 and 15 of the 1933 Act. The federal plaintiffs later amended their complaint to add similar claims under the 1933 Act, and the state plaintiff added a claim under Section 12(a)(2) of the 1933 Act to his complaint. Although the federal action was filed first, and despite the "substantial overlap between the claims," the New York Supreme Court ruled that "neither action will completely dispose of all of the issues" since only the state action included "a claim under section 12(a)(2) of the 1933 Act for which rescission is available" and a claim against an auditor defendant.[136] The court declined to stay the action and held that the fact that "the federal action was technically filed first . . . is not dispositive."[137]

Similarly, the First Department signaled in *In re Qudian Securities Litigation* that, in assessing whether to grant a stay in favor of parallel federal litigation, New York courts will carefully scrutinize the nature of any overlap between the parallel actions.[138] In this case, the First Department reversed the trial court's decision not to vacate a stay of a 1933 Act claim, reasoning that the concurrent federal proceedings "will not determine all of the questions in this action."[139] Several putative class actions were first filed in federal court, and following the dismissal of most of the federal claims, the plaintiffs sought to lift a previously imposed stay of their 1933 Act claims in state court.[140] The lower court determined that continuation of the stay was warranted even where "the underlying conduct relied upon may be different,"[141] an approach consistent with other securities cases staying state court 1933 Act claims in favor of parallel federal proceedings despite a divergence of legal theories or claims in the federal and state actions.[142] The First Department reversed, finding that a stay was inappropriate because the plaintiffs' claim differed from the

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[134] *See*, *e.g.*, *Labourers' Pension Fund of Cent. & E. Can.* v. *CVS Health Corp.*, 2020 WL 2857654, at *3 (N.Y. Sup. Ct., N.Y. Cty. June 1, 2020) (citing *Asher* v. *Abbott Labs.*, 307 A.D.2d 211, 212 (1st Dep't 2003).
[135] 2020 WL 4586301, at *3 (N.Y. Sup. Ct., N.Y. Cty. Aug. 7, 2020).
[136] *Id.* at *2.
[137] *Id.* at *3 (citing *Labourer's Pension Fund*, 2020 WL 2857654, at *7).
[138] 189 A.D.3d 449 (1st Dep't 2020).
[139] *Id.* at 449.
[140] *See In re Qudian Sec. Litig.*, 2020 WL 2106837, at *1 (N.Y. Sup. Ct., N.Y. Cty. Apr. 28, 2020).
[141] *Id.*
[142] *See*, *e.g.*, *In re Nio Inc. Sec. Litig.*, 2020 WL 4932073, at *1 (N.Y. Sup. Ct., N.Y. Cty. Aug. 21, 2020); *Mahar* v. *Gen. Elec. Co.*, 112 N.Y.S. 3d 879, 888 (N.Y. Sup. Ct., N.Y. Cty. 2019).

claims dismissed in the federal action, such that "the finding in the federal action would not pose a risk of inconsistent rulings."[143] Further, the First Department emphasized that the plaintiffs in the two actions were different, and that there was no evidence that either the federal or state plaintiffs "are mere tools or puppets" of counsel, who had represented plaintiffs in both actions.[144] Thus, the ruling suggests that defendants may continue to face the risk of parallel actions where different plaintiffs have chosen to advance different claims in each action.

***Federal Forum Selection Provisions***. In a positive development for issuers, a series of California state court decisions have ruled that federal forum provisions ("FFPs") in a corporate charter or bylaws providing that all 1933 Act claims against the company must be brought in federal court are generally enforceable and preclude litigation of securities claims in state court. These decisions follow the Delaware Supreme Court's holding in *Salzberg* v. *Sciabacucchi* that FFPs are facially valid under the Delaware General Corporate Law and do not violate public policy.[145] Although adopting different reasoning from the Delaware Supreme Court, these California courts have uniformly affirmed the enforceability of FFPs under California law, absent a showing by the plaintiff that the provisions are unconscionable, unreasonable, or otherwise unenforceable.

The September 1, 2020 decision of a California trial court in *Wong* v. *Restoration Robotics* was the first in the state to dismiss claims brought under the 1933 Act because the issuer's corporate charter contained a federal forum provision.[146] Unlike in *Sciabacucchi*, the court reasoned that an FFP is not analogous to a release in a settlement clause or an arbitration clause for the purposes of enforceability, but "is most akin to a contractual forum selection clause" because it does not remove the rights of the parties to litigate in court, to a jury trial, or to appeal, nor does it create any additional expense or inconvenience.[147] Under this reasoning, the court held that the FFP was enforceable under California law, absent any demonstration by the plaintiff that it was otherwise "unenforceable, unconscionable, unjust or unreasonable."[148]

In a second decision, rendered on November 16, 2020, another California trial court upheld the enforceability of an FFP in Uber's charter, providing for exclusive jurisdiction in federal district courts to resolve 1933 Act claims.[149] The court held that "federal securities claims brought by a shareholder" did not fall within the internal affairs doctrine and that California law, as opposed to the law of the state of incorporation, therefore applied to the question of whether the FFP was valid and enforceable.[150] Applying California law, the court concluded that the FFP was not unconscionable because "it does not eliminate the

[143] *In re Qudian Sec. Litig.*, 189 A.D.3d at 450.
[144] *Id.*
[145] 227 A.3d 102, 109 (Del. 2020).
[146] 2020 Cal. Super. LEXIS 227 (Cal. Super. Ct. Sept. 1, 2020).
[147] *Id.* at *37–38.
[148] *Id.* at *57.
[149] *In re Uber Technologies, Inc. Sec. Litig.*, No. CGC-19-579544, slip op. at 3 (Cal. Super. Ct. Nov. 16, 2020).
[150] *Id.* at 6.

substantive protections provided by the Securities Act itself."[151] The court thus granted the defendants' motion to dismiss in its entirety.

Consistent with this reasoning, another California trial court upheld the enforceability of FFPs in two subsequent cases. In the *Dropbox* securities litigation, the court granted the defendants' motion to dismiss in full, after finding that an FFP included in Dropbox's bylaws was not unconscionable given the "legitimate business need" of avoiding unnecessary costs and the burden of defending multiple cases simultaneously in state and federal courts.[152] The court followed its reasoning in *Dropbox* in a securities class action against Sonim Technologies, a Delaware corporation incorporating a FFP in its corporate charter.[153]

Collectively, these decisions reflect a trend by California courts to permit the enforcement of FFPs, subject to the doctrine of unconscionability and other doctrines restricting the application of contractual forum selection clauses. Since *Cyan*, California has been one of the two states (along with New York) with the most state court 1933 Act claims. These decisions may portend a drop in state court 1933 Act filings in California. It remains to be seen, however, how courts in other states will treat the enforceability of FFPs. If other states, especially New York, enforce FFPs, they will continue to grow in significance for curbing the rise of state court 1933 Act claims.

### C. APPLICATION OF THE PSLRA'S SAFE HARBOR

The Private Securities Litigation Reform Act of 1995 ("PSLRA") establishes a "safe harbor" for "forward-looking" statements. Under this provision, a defendant "shall not be liable with respect to any forward-looking statement, whether written or oral," if (i) the statement is accompanied by meaningful cautionary language, (ii) the statement is immaterial, or (iii) the plaintiff fails to show that the statement was made with actual knowledge that it was false or misleading.[154] Two recent circuit court decisions demonstrate the sometimes conflicting conclusions of courts on the reach of that provision. In August 2020, the Fifth Circuit affirmed in *Heinze* v. *Tesco Corp.* that projections included in a merger proxy statement may be protected by the safe harbor, while departing from the Eleventh Circuit in concluding material omissions fall outside the safe harbor provision.[155] In January 2021, in *Wochos* v. *Tesla*, the Ninth Circuit clarified the application of the safe harbor to "mixed" statements combining both forward-looking and non-forward-looking aspects.[156]

In *Tesco*, the Fifth Circuit applied the PSLRA's safe harbor to a merger proxy statement to affirm the dismissal of a claim under Section 14(a) of the 1934 Act. There, the plaintiff alleged that defendants made material misstatements and omissions about projections for revenue and earnings before interest, taxes, depreciation, and amortization (EBITDA), claiming that these "left Tesco shareholders with an unduly

[151] *Id.* at 14.
[152] *In re Dropbox, Inc. Sec. Litig.*, No. 19-civ-05089, slip op. at 14 (Cal. Super. Ct. Dec. 4, 2020).
[153] *In re Sonim Tech., Inc. Sec. Litig.*, No. 19-civ-05564, slip op. at 2 (Cal. Super. Ct. Dec. 4, 2020).
[154] 15 U.S.C. § 78u-5(c).
[155] 971 F.3d 475 (5th Cir. 2020).
[156] 2021 WL 246210, at *5 (9th Cir. Jan. 26, 2021).

pessimistic view of Tesco's future growth potential."[157] Notably, although the Court of Appeals affirmed that the safe harbor applied to the defendant's "forecasts" and "projections," it agreed with the plaintiff that "the text of the safe harbor covers only forward-looking *statements*, not *omissions*."[158]

The Fifth Circuit's determination that the safe harbor provision does not apply to material omissions is also significant because it creates a split on this issue with the Eleventh Circuit. According to the Eleventh Circuit, "there is no question under the [PSLRA] that a material and misleading omission can fall within the forward-looking safe harbor."[159] District courts in the Seventh and Ninth Circuits have also followed that reasoning.[160] In contrast, in addition to the Fifth Circuit in *Tesco*, district courts in the Second, Third, Fourth, and Tenth Circuits have ruled that "[t]he safe harbor does not apply to material omissions."[161] Accordingly, although we are likely to see further development on this issue at the circuit level, issuers should be aware that at least some courts may view alleged omissions, unlike alleged misstatements, as categorically outside the scope of the safe harbor.

As the *Tesco* decision demonstrates, the PSLRA's safe harbor can offer protection against merger-related actions for defendants that have disclosed projections accompanied by meaningful cautionary language. Often, however, the challenged statements may qualify as "mixed statements," which have both forward-looking and non-forward-looking aspects. There continues to be significant divergence regarding the scope of the safe harbor as applied to such mixed statements. Courts have split on this question, with some finding that the entire statement may be shielded,[162] while others apply the protection only to the forward-looking aspects of the mixed statement.[163]

Most recently, the Ninth Circuit offered further guidance on this issue, determining in *Tesla* that the forward-looking statements may be "separable" from the non-forward-looking statements.[164] Prior to *Tesla*, the Ninth Circuit had held in *In re Quality Systems, Inc. Securities Litigation* that "a defendant may not transform non-forward-looking statements" into statements protected by the safe harbor simply by "combining non-forward-looking statements about past or current facts with forward-looking statements about projected revenues and earnings."[165] In a restrictive interpretation of the safe harbor, the *Quality Systems* court indicated that for its protections to apply to a mixed statement, there must be cautionary language that "accurately convey[s] appropriate, meaningful information about not only the forward-looking statement but

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[157] *Tesco*, 971 F.3d at 481.
[158] *Id.* at 483–84.
[159] *Harris* v. *Ivax Corp.*, 182 F.3d 799, 806 (11th Cir. 1999); *Ehlert* v. *Singer*, 245 F.3d 1313, 1317 (11th Cir. 2001).
[160] *See*, *e.g.*, *Kuebler* v. *Vectren Corp.*, 412 F. Supp. 3d 1000, 1007 n.2 (S.D. Ind. 2019); *W. Pa. Elec. Emps. Pension Fund* v. *Mentor Graphics Corp.*, 2017 WL 3668957, at *20 (D. Or. June 2, 2017).
[161] *See*, *e.g.*, *City of Providence* v. *Aeropostale, Inc.*, 2013 WL 1197755, at *12 (S.D.N.Y. Mar. 25, 2013); *In re Salix Pharms., Ltd.*, 2016 WL 1629341, at *9 (S.D.N.Y. Apr. 22, 2016); *In re MobileMedia Sec. Litig.*, 28 F. Supp. 2d 901, 930 (D.N.J. 1998); *AES Corp.* v. *Dow Chem. Co.*, 2001 WL 34367296, at *4 (D. Del. Jan. 19, 2001); *In re Constellation Energy Grp., Inc. Sec. Litig.*, 738 F. Supp. 2d 614, 625 (D. Md. 2010); *Voulgaris* v. *Array Biopharma Inc.*, 2020 WL 8367829, at *20 (D. Colo. Nov. 24, 2020).
[162] *See*, *e.g.*, *Harris*, 182 F.3d at 806; *Miller* v. *Champion Enters. Inc.*, 346 F.3d 660, 677 (6th Cir. 2003).
[163] *See*, *e.g.*, *In re Stone & Webster, Inc., Sec. Litig.*, 414 F.3d 187, 213 (1st Cir. 2005); *In re Vivendi, S.A. Sec. Litig.*, 838 F.3d 223, 246 (2d Cir. 2016); *Institutional Inv'rs Grp.* v. *Avaya, Inc.*, 564 F.3d 242, 255 (3d Cir. 2009); *Spitzberg* v. *Houston Am. Energy Corp.*, 758 F.3d 676, 691 (5th Cir. 2014); *Makor Issues & Rights, Ltd.* v. *Tellabs Inc.*, 513 F.3d 702, 705 (7th Cir. 2008).
[164] 2021 WL 246210, at *5 (9th Cir. Jan. 26, 2021).
[165] 865 F.3d 1130, 1141, 1148 (9th Cir. 2017).

also the non-forward-looking statement," such as the possibility that the statements "are, or may be, untrue."[166]

In *Tesla*, however, the court clarified its earlier approach and explained that "the PSLRA's safe harbor does not apply in an all-or-nothing fashion."[167] There, the plaintiffs filed a putative class action alleging that Tesla and two of its officers misled investors in announcing Tesla's 2017 production goals for its Model 3 vehicles, including by stating that preparations at production facilities were "on track" to support production of 5,000 vehicles per week.[168] The Ninth Circuit affirmed the district court's dismissal of the action, finding that with one exception, the challenged statements about Tesla's preparations at its production facilities were forward-looking statements of "plans and objectives" or "assumptions underlying or relating to" those plans and objectives, and, hence covered by the safe harbor.[169] The court stated that in the context of mixed statements, "only the forward-looking aspects could be immunized from liability."[170] To avoid the safe harbor, "a plaintiff must plead facts that show that the statement goes *beyond* the articulation of 'plans,' 'objectives,' and 'assumptions' and instead contains an express or implied 'concrete' assertion concerning a specific 'current or past fact[ ].'"[171]

Courts' attempts at distinguishing between forward- and non-forward-looking aspects of a statement are particularly salient in the merger context, where companies frequently disclose both earnings projections and valuation figures. Here, the subtle distinctions courts sometimes draw in applying the safe harbor are illustrated by two cases in the past few months, in which plaintiffs alleged that statements or omissions in proxy materials misleadingly undervalued the defendant company. In *In re Mindbody Securities Litigation*, the court ruled that the defendants' revenue projections were forward-looking statements within the safe harbor, but that misstatements about the "premium" gained by an acquisition offer calculated on the basis of those projections were actionable.[172] Likewise, in *Karri* v. *Oclaro, Inc.*, the court distinguished between internal financial projections, which were deemed to be forward-looking, and "valuation figures in the proxy statement," which the court held fell outside the safe harbor.[173] Although there may be a fine line between a projection and a valuation, these decisions suggest that at least in some cases courts are treating the latter as a non-forward-looking statement, even where the valuation is calculated on the basis of forward-looking projections.

### D. SUPREME COURT TO CONSIDER REBUTTAL OF THE *BASIC* "FRAUD-ON-THE-MARKET" PRESUMPTION

In one of the most closely watched securities class actions in recent years, on December 11, 2020, the Supreme Court granted a certiorari petition by Goldman Sachs and its former senior officers, represented

[166] *Id.* at 1148.
[167] *Tesla*, 2021 WL 246210, at *5.
[168] *Id.* at *2.
[169] *Id.* at *7.
[170] *Id.* at *5.
[171] *Id.* at *7 (quoting *Quality Sys.*, 865 F.3d at 1142, 1144).
[172] 2020 WL 5751173, at *8 (S.D.N.Y. Sept. 25, 2020).
[173] 2020 WL 5982097, at *5, *12 (N.D. Cal. Oct. 8, 2020).

by S&C, seeking review of a Second Circuit decision affirming class certification. In *Goldman Sachs Group, Inc.* v. *Arkansas Teacher Retirement System*,[174] the Supreme Court will consider the standards to be applied by courts when defendants seek to rebut the "fraud-on-the-market" presumption of class-wide reliance established in *Basic Inc.* v. *Levinson*.[175] Commentators have stated that the appeal "could redefine the ability of shareholders to pursue class actions against public companies whose stock prices fall."[176]

The case stems from the highly publicized lawsuit the SEC filed in 2010 alleging that Goldman Sachs and an employee misrepresented conflicts in a collateralized debt obligation called ABACUS. The plaintiffs alleged that the conduct revealed by the SEC's lawsuit and subsequent rumors of additional enforcement actions rendered false Goldman Sachs' statements about its Business Principles and conflicts controls. The case twice reached the Second Circuit on Federal Rule of Civil Procedure 23(f) appeals from class certification prior to the grant of certiorari by the Supreme Court.

Goldman Sachs' petition raised two issues: (i) whether a defendant in a securities class action may rebut the *Basic* presumption of class-wide reliance by pointing to the generic nature of the alleged misstatements in showing that the statements had no price impact, even though that evidence is also relevant to the substantive element of materiality; and (ii) whether a defendant seeking to rebut the *Basic* presumption has only a burden of production or also the ultimate burden of persuasion.

Goldman Sachs was supported by multiple amici, including the U.S. Chamber of Commerce, Securities and Financial Markets Association, Bank Policy Institute, American Bankers Association, Society for Corporate Governance, Retail Litigation Center, and Washington Legal Foundation, as well as financial economists, former SEC officials, and law professors.

The oral argument before the Supreme Court is scheduled for March 29, 2021.

### E. SHAREHOLDER SUITS RELATED TO ESG DISCLOSURES

The past several years have witnessed the rise of environmental, social and governance factors in corporate disclosures, as U.S. public companies seek to respond to increasing stakeholder interest in these issues and choose to adopt broader disclosure of their ESG practices, impacts, and risks.[177] The Government Accountability Office estimated that in 2019, 5% of companies in the S&P 1500 received one or more shareholder proposals related to increasing ESG disclosures.[178] Common topics of ESG disclosures include sustainability, climate change, human rights, diversity and inclusion, and occupational

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[174] (No. 20-222), 2020 WL 7296815 (U.S. Dec. 11, 2020).
[175] 485 U.S. 224 (1988).
[176] Jonathan Stempel, *U.S. Supreme Court Takes up Goldman Securities Class Action Appeal*, REUTERS (Dec. 11, 2020), https://www.reuters.com/article/usa-court-goldmanUsachs/-u-s-supreme-court-takes-up-goldman-securities-class-action-appeal-idUKLUN2E301G.
[177] *See*, *e.g.*, Jennifer S. Fan, *Woke Capital: The Role of Corporations in Social Movements*, 9 HARV. BUS. L. REV. 441 (2019).
[178] U.S. GOV'T ACCOUNTABILITY OFF., GAO-20-530, PUBLIC COMPANIES: DISCLOSURE OF ENVIRONMENTAL, SOCIAL AND GOVERNANCE FACTORS AND OPTIONS TO ENHANCE THEM 14 (2020).

health and safety risks.[179] For instance, in the 2020 proxy season, climate change, other environmental issues, and workplace diversity were leading themes of shareholder proposals.[180]

As corporate efforts to engage with ESG issues have increased, the risk of litigation related to such disclosures has also become more pervasive. Similar to other types of public disclosures, ESG-related disclosures in SEC filings, other than those subject to the PSLRA's safe harbor, may be challenged by plaintiffs as materially inaccurate or misleading under the U.S. federal securities laws. The risks associated with ESG disclosures are accentuated with the ongoing trend of "event-driven" securities litigation, in which plaintiffs seek to attribute an event causing a share price drop to earlier public statements made by the defendant, which are often general and aspirational in nature.

In 2020, a number of shareholder derivative actions and securities fraud suits stemming from ESG-related commitments and disclosures were filed against a wide array of companies. In a series of derivative suits filed in California federal courts, shareholders alleged that directors and officers of companies ranging from a cybersecurity firm to a clothing retailer had breached their fiduciary duties and violated Section 14(a) of the 1934 Act by failing to uphold corporate commitments to leadership diversity.[181] These suits contend that the defendants made false statements regarding the companies' efforts to promote and achieve diversity, as well as corporate policies regarding hiring and promotion, and seek damages and injunctions directing the defendants to take all necessary actions to improve corporate governance and internal procedures.

Companies may also face a risk of litigation arising from disclosures about their safety and environmental sustainability standards, policies, and practices. For example, in May 2020, a court in the Eastern District of New York denied Brazilian mining company Vale S.A.'s motion to dismiss, in a securities fraud case alleging that the collapse of a dam disclosed the falsity of the company's statements about its risk management and sustainability policies and practices.[182] Although it acknowledged that Section 10(b) of the 1934 Act is not intended to make corporate mismanagement actionable, and that "Vale's statements about safety and sustainability may be generic," the court nevertheless allowed claims based on such statements to proceed, noting that Vale had "repeatedly emphasized its commitment to such priorities."[183] In another case involving public statements about a corporate miner safety program, the court dismissed the claims for lack of particularity and failure to adequately plead falsity.[184]

A number of decisions this past year demonstrate the increasing scrutiny of companies' public statements about corporate culture and employee codes of conduct, with varying outcomes. In January 2020, a court

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[179] *Id.* at 20.
[180] *See* Sullivan & Cromwell LLP, *2020 Proxy Season Review: Part 1: Rule 14a-8 Shareholder Proposals* (July 15, 2020), https://www.sullcrom.com/files/upload/SC-Publication-2020-Proxy-Season-Review-Part-1-Rule-14a-8.pdf.
[181] *See*, *e.g.*, *Esa* v. *NortonLifeLock Inc.*, No. 20-cv-05410, Dkt. No. 1, at 6–12 (N.D. Cal. Aug. 5, 2020); *Lee* v. *Fisher*, No. 20-cv-06163, Dkt. No. 1, at 2–11 (N.D. Cal. Sept. 1, 2020); *Falat* v. *Sacks*, No. 20-cv-01782, Dkt. No. 1, at 4–16 (C.D. Cal. Sept. 18, 2020); *City of Pontiac Gen. Emps.' Ret. Sys.* v. *Bush*, No. 20-cv-06651, Dkt. No. 1, at 1–2 (N.D. Cal. Sept. 23, 2020).
[182] *In re Vale S.A. Sec. Litig.*, 2020 WL 2610979, at *9 (E.D.N.Y. May 20, 2020).
[183] *Id.* at *12, *14–15.
[184] *In re Sibanye Gold Ltd. Sec. Litig.*, 2020 WL 6582326, at *14–15 (E.D.N.Y. Nov. 10, 2020).

in the Southern District of New York granted in part a motion to dismiss in a securities fraud case filed against CBS Corporation and its directors and officers, which focused on statements including that CBS "*believes* in an environment that is free from workplace bullying" and "has a '*zero tolerance*' *policy* for sexual harassment."[185] The plaintiffs claimed that these statements were rendered false by then-CEO Leslie Moonves' concealment of his sexual misconduct. The court held that the statements were "far too general and aspirational to invite reasonable reliance."[186] However, it found that the plaintiffs "adequately—though barely—allege[d]" that Moonves' statement that "[t]here's a lot we didn't know [about #MeToo]" may be materially misleading, finding that the plaintiffs' allegations raised a strong inference that Moonves knew "his statement and its implications were not truthful."[187] With the exception of Moonves, the court dismissed all claims against CBS's directors and officers, one of whom was represented by S&C. In other recent cases, courts have held similarly broad statements of corporate culture—such as Papa John's Pizza's pledge "to conduct its business lawfully, responsibly and with the highest moral and ethical standards"[188] and a telemedicine company's "commitment to the highest level of ethical conduct" by its officers[189]—to be inactionable puffery.

In contrast, in July 2020, a district court approved a $240 million settlement by a jewelry retailer, in a shareholder fraud case alleging that the company's statements concerning gender parity and sexual harassment policies were misleading.[190] The settlement followed an earlier ruling in which the court found that the retailer's code of conduct and ethics, including statements that it was "committed to a workplace that is free from sexual, racial, or other unlawful harassment" and does not tolerate "[a]busive, harassing, or other offensive conduct," did not qualify as inactionable puffery.[191] There, the court reasoned that, despite their generality, the challenged statements were "directly contravened by allegations in the [complaint] that the company conditioned employment decisions on whether female employees acceded to sexual demands and retaliated against women who attempted to anonymously report sexual harassment."[192] Meanwhile, in two securities fraud class actions against different manufacturing companies, both represented by S&C, courts in the Eastern District of New York reached divergent conclusions on whether the same anti-bribery statement—that the defendant company "will not condone, under any circumstances, the offering or receiving of bribes"—amounted to inactionable puffery[193] or a potentially material misstatement.[194] In the former case, the plaintiffs chose not to appeal the dismissal of the action, while a motion for reconsideration by defendants is currently pending in the latter.

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[185] *Constr. Laborers Pension Tr. for S. Cal.* v. *CBS Corp.*, 433 F. Supp. 3d 515, 533 (S.D.N.Y. 2020).
[186] *Id.* at 533.
[187] *Id.* at 539.
[188] *Okla. L. Enf't Ret. Sys.* v. *Papa John's Int'l, Inc.*, 444 F. Supp. 3d 550, 555 (S.D.N.Y. 2020).
[189] *Reiner* v. *Teladoc Health, Inc.*, 2020 WL 6343217, at *5 (S.D.N.Y. Sept. 4, 2020), *aff'd*, 2020 WL 7028638 (S.D.N.Y. Nov. 30, 2020).
[190] *In re Signet Jewelers Ltd. Sec. Litig.*, 2020 WL 4196468, at *1 (S.D.N.Y. July 21, 2020).
[191] *In re Signet Jewelers Ltd. Sec. Litig.*, 389 F. Supp. 3d 221, 226 (S.D.N.Y. 2019).
[192] *Id.* at 227.
[193] *Ulbricht* v. *Ternium S.A.*, 2020 WL 5517313, at *9 (E.D.N.Y. Sept. 14, 2020).
[194] *In re Tenaris S.A. Sec. Litig.*, 2020 WL 6018919, at *7 (E.D.N.Y. Oct. 9, 2020).

As these cases highlight, courts vary in their assessments of whether ESG-related statements are inactionable puffery, even in cases involving similarly worded statements. The uncertainty in how a particular court will rule on a particular ESG disclosure carries significant implications for potential liability arising from such disclosures. Recently, the rise of ESG disclosures has led some investors to call for the adoption of a standardized framework for such disclosures, which would facilitate comparison of ESG practices and risks.[195] With a May 2020 recommendation by its Investor Advisory Committee to address ESG disclosures,[196] and the appointment in February 2021 of the first-ever Senior Policy Advisor for Climate and ESG,[197] the SEC is giving increased attention to the regulatory regime for ESG disclosures. On February 24, 2021, Acting Chair of the SEC Allison Herren Lee announced that she was "directing the Division of Corporation Finance to enhance its focus on climate-related disclosure in public company filings."[198] The Corporation Finance Division's staff will review the extent to which companies address the topics identified in its earlier 2010 guidance regarding disclosure on climate change matters, as well as examine how the market is currently managing climate risks, in order "to begin updating the 2010 guidance to take into account developments in the last decade."[199] Recently, Acting Chair Lee has also stated that the SEC aims to implement a "global" framework for climate disclosures providing for "relevant, standardized, comparable and reliable disclosure of business risks and opportunities," in line with the new administration's focus on climate risks.[200]

Beyond the prospect of liability under the federal securities laws, companies should also be aware of applicable consumer protection and anti-fraud state and federal laws, which plaintiffs may attempt to invoke as further bases to challenge ESG disclosures.

### F. SHAREHOLDER SUITS RELATED TO SPECIAL PURPOSE ACQUISITION COMPANIES

As special purpose acquisition companies have emerged as a fundamental tool for capital formation and deployment in current market conditions, SPAC-driven IPOs have dramatically increased in the past year. In 2020, there were 248 SPAC IPOs, a more than four-fold increase compared with the previous highs of 59 in 2019 and 46 in 2018.[201] As of the time of writing, there were 204 SPAC IPOs this year, positioning 2021 to be the busiest year ever for SPAC transactions.[202]

In turn, the widespread embrace of SPACs may drive an increase in securities filings in this area. While the period between 2016 and 2018 witnessed one to two securities class actions involving SPACs per year,

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[195] *See* Sullivan & Cromwell LLP, *The Rise of Standardized ESG Disclosure Frameworks in the United States* (June 8, 2020), https://www.sullcrom.com/files/upload/SC-Publication-Rise-Standardized-ESG-Disclosure-Frameworks.pdf.
[196] SEC Investor Advisory Committee, *Recommendation of the SEC Investor Advisory Committee Relating to ESG Disclosure* (May 21, 2020), https://www.sec.gov/spotlight/investor-advisory-committee-2012/esg-disclosure.pdf.
[197] Press Release, *Satyam Khanna Named Senior Policy Advisor for Climate and ESG*, SECURITIES AND EXCHANGE COMMISSION (Feb. 1, 2021), https://www.sec.gov/news/press-release/2021-20.
[198] Public Statement, *Statement on the Review of Climate-Related Disclosure*, SECURITIES AND EXCHANGE COMMISSION (Feb. 24, 2021), https://www.sec.gov/news/public-statement/lee-statement-review-climate-related-disclosure.
[199] *Id.*
[200] Al Barbino, *SEC Working Toward 'Global' Climate Disclosure Framework*, Law360 (Mar. 1, 2021), https://www.law360.com/environmental/articles/1360178.
[201] Cornerstone Research, *Securities Class Actions Filings: Year in Review 2020*, at 23.
[202] *SPAC IPO Transactions Statistics*, SPACINSIDER, https://spacinsider.com/stats/ (last visited Mar. 2, 2021).

SPAC filings reached an all-time high in the past two years, with six filings in 2019 and five filings in 2020.[203] In the context of SPAC IPOs, plaintiffs have filed suits against the SPAC and/or the target company, based on alleged misstatements or omissions prior to, or after, the de-SPAC transaction. In a recent filing, for instance, the plaintiffs alleged that a SPAC and its directors violated Sections 14(a) and 20(a) of the 1934 Act by making misleading statements in the SPAC's registration statement about potential conflicts of interest of the SPAC's financial advisors and the background of its proposed acquisition of an electric vehicle company.[204] In another case, the plaintiffs alleged that a target company and its CEO violated Sections 10(b) and 20(a) of the 1934 Act by making misstatements, following its reverse merger with a SPAC, related to the company's development of battery technology.[205] Based on these observed trends, it is likely that SPAC-related litigation will continue to grow in prominence.

## G. EFFECTS OF COVID-19 ON SECURITIES LITIGATION

***U.S. Chamber of Commerce Petition for SEC Rulemaking on COVID-19 Liability***. On October 30, 2020, the U.S. Chamber of Commerce submitted a petition for rulemaking to the SEC, requesting that the Commission exercise its authority "to expand the PSLRA's statutory safe harbors and create additional exemptions from liability where appropriate."[206] In its petition, the Chamber pointed to "a strong likelihood" of pandemic-related securities litigation and urged action to respond to the possibility that "securities class actions can be abused to bring unjustified lawsuits."[207] Specifically, the Chamber proposed that the Commission (i) use its authority under the PSLRA "to bar liability for statements about a company's plans or prospects for getting back to business, resuming sales or profitability, or other statements about the impacts of COVID-19, whether forward-looking or not—as long as suitable warnings were attached"; (ii) alternatively, "consider limiting liability for all such statements to circumstances in which the plaintiff can prove that the speaker had actual (subjective) knowledge of its falsity"; and (iii) require that financial statements include a statement reminding users that certain elements of financial statements "are determined on the basis of projections of future business or market conditions or by applying 'mark to market' standards" and emphasizing "the tremendous uncertainties flowing from the pandemic," as well as "bar liability for claims based on statements that satisfy these warnings, or alternatively, treat them as the equivalent of opinions that require proof of subjective knowledge of falsity in order to be actionable."[208]

The petition is supported by TechNet[209] and a coalition of 14 trade associations and business groups.[210] No action has yet been taken on the petition for rulemaking.

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[203] Cornerstone Research, *Securities Class Actions Filings: Year in Review 2020*, at 7.
[204] *Ryan* v. *GigCapital3, Inc.*, No. 21-cv-00969, Dkt. No. 1, at 1–3 (N.D. Cal. Feb. 8, 2021).
[205] *Malriat* v. *QuantumScape Corp.*, No. 21-cv-00058, Dkt. No. 1, at 1–2 (N.D. Cal. Jan. 5, 2021).
[206] U.S. Chamber of Commerce, *Request to Limit Unjustified COVID-19 Lawsuits*, at 2 (Oct. 30, 2020), https://www.sec.gov/rules/petitions/2020/petn4-766.pdf.
[207] *Id.* at 1, 5.
[208] *Id.* at 9–10.
[209] TechNet, *Comment Letter: Request to Limit Unjustified COVID-19 Lawsuits* (Dec. 18, 2020), https://www.sec.gov/comments/4-766/4766-8163226-226946.pdf.
[210] U.S. Chamber Center for Capital Markets Competitiveness, et al., *Re: Support for Petition for Rulemaking on COVID-19 Related Litigation – File 4-766* (Feb. 3, 2021), https://www.sec.gov/rules/petitions/2020/petn4-766.pdf.

***Event-Driven Securities Litigation During the Pandemic***. In the latter half of 2020 and early months of 2021, filings of COVID-related securities suits have been notable but relatively modest. Although disclosures in the biomedical and healthcare industries have been the focus of most COVID-related litigation to date, the phenomenon of "event-driven" litigation has expanded to target companies in other industries for disclosures relating to specific challenges and opportunities presented by the pandemic.

On January 25, 2021, the District Court for the Central District of California issued the first decision dismissing a COVID-related securities action in *Berg* v. *Velocity Financial, Inc.*, rejecting the plaintiff's COVID-related claims as an attempt to plead fraud by hindsight.[211] In this case, the plaintiff alleged that the defendant, a real estate finance company, had violated Sections 11 and 15 of the 1933 Act by making misleading statements in its IPO offering materials filed in January 2020, including by failing to disclose the risks that the pandemic posed to the real estate market.[212] In granting the defendants' motion to dismiss in full, the district court found that the plaintiff failed to adequately allege "how Defendants would have known about the coronavirus risks at the time of the IPO" and ruled that "Defendants did not need to include more specific disclosures about the coronavirus pandemic."[213] In emphasizing the need to plead the defendant's knowledge of coronavirus risks at the time of the allegedly misleading statements, the ruling provides some assurance to defendants faced with COVID-related allegations.

Following a trend identified in the previous iteration of our Securities Enforcement and Litigation Update, securities class actions continue to be filed against biomedical and healthcare companies in late 2020 and early 2021 for statements related to COVID-19 treatments and testing. Between August and December 2020, at least three class action complaints were filed against biomedical companies, alleging misleading statements or omissions in relation to the development of an oral COVID-19 vaccine candidate[214] and diagnostic tests for COVID-19.[215] In early 2021, the filing of a number of securities class actions in this area continued. On January 15, 2021, a shareholder fraud class action was filed against Decision Diagnostics, alleging misstatements by the company about its development of a COVID-19 test.[216] Likewise, on January 26, 2021, a class action was initiated against drug-maker AstraZeneca, alleging that it made material misstatements and omissions in relation to clinical trials for its vaccine candidate.[217]

Beyond the biomedical industry, several new suits focus on statements that companies in other sectors have made in response to challenges and opportunities presented by the pandemic. In August 2020, shareholders filed a class action complaint against Eastman Kodak, alleging that the company and its CEO and CFO engaged in a fraudulent scheme to inflate Kodak's stock price.[218] The plaintiffs allege that Kodak's

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[211] 2021 WL 268250, at *10 (C.D. Cal. Jan. 25, 2021).
[212] *Id.* at *5, *10.
[213] *Id.* at *10.
[214] *Himmelberg* v. *Vaxart, Inc.*, No. 20-cv-05949, Dkt. No. 1, at ¶ 2 (N.D. Cal. Aug. 24, 2020).
[215] *Special Situations Fund III QP, L.P.* v. *Chembio Diagnostics, Inc.*, No. 20-cv-03753, Dkt. No. 1, at 3 (E.D.N.Y. Aug. 17, 2020); *Alperstein* v. *Sona Nanotech Inc.*, No. 20-cv-11405, Dkt. No. 1, at 4–5 (C.D. Cal. Dec. 17, 2020).
[216] *Sanchez* v. *Decision Diagnostics Corp.*, No. 21-cv-00418, Dkt. No. 1, at 2 (C.D. Cal. Jan. 15, 2021).
[217] *Monroe Cnty. Emps.' Ret. Sys.* v. *AstraZeneca plc*, No. 21-cv-00722, Dkt. No. 1, at 3–16 (S.D.N.Y. Jan. 26, 2021).
[218] *Tang* v. *Eastman Kodak Co.*, No. 20-cv-10462, Dkt. No. 1, at 1 (D.N.J. Aug. 13, 2020).

announcement, in July 2020, of a $765 million loan by the U.S. International Finance Corporation to produce pharmaceutical materials, including ingredients for COVID-19 drugs, coincided with undisclosed stock option grants to Kodak's executives.[219] Other notable examples include putative class actions initiated against Royal Caribbean Cruises for allegedly misleading statements about booking slowdowns and safety protocols onboard its ships,[220] an education company for allegedly misleading statements in connection with its capacity to support increased demand for virtual learning during the pandemic and adequate protections against cyberattack,[221] and a meat producer for allegedly misleading disclosures in relation to coronavirus safety protocols.[222]

[219] *Id.* at 2.
[220] *City of Riviera Beach Gen. Emps. Ret. Sys.* v. *Royal Caribbean Cruises Ltd.*, No. 20-cv-24111, Dkt. No. 1, at 3–4 (S.D. Fla. Oct. 7, 2020).
[221] *Lee* v. *K12 Inc.*, No. 20-cv-01419, Dkt. No. 1, at 2–3 (E.D. Va. Nov. 19, 2020).
[222] *Guo* v. *Tyson Foods, Inc.*, No. 21-cv-00552, Dkt. No. 1, at 4–10 (E.D.N.Y. Feb. 2, 2021).

## MEET THE EDITORS

**Jeffrey T. Scott** is a partner in S&C's Litigation Group and co-lead of the Firm's Securities Litigation Practice. A versatile and accomplished litigator, Mr. Scott has secured significant successes for clients in a wide range of areas, including securities, antitrust, and commercial civil litigation and regulatory and criminal investigations, as well as in other bet-the-company actions. In 2019, Jeff was recognized as a Litigation Trailblazer and Winning Litigator by *The National Law Journal*, and has been recognized by *Chambers USA*, *New York Super Lawyers*, *The Legal 500* and *Benchmark Litigation* for his work in antitrust, appellate, financial services, securities litigation, and other areas. Jeff also has been recognized as a Law360 MVP in securities law and featured multiple times in *The American Lawyer*'s Litigator-of-the-Week series. He frequently speaks and writes about litigation issues.

**Steven R. Peikin** leads S&C's Securities & Commodities Investigations & Enforcement Practice. Mr. Peikin brings decades of experience at the most senior levels of government and in private practice to his representation of clients in a wide range of regulatory enforcement investigations, white-collar criminal matters, and internal investigations. He has particular expertise in matters involving the federal securities and commodities laws. From 2017 to 2020, Mr. Peikin served as Co-Director of the U.S. Securities and Exchange Commission's Division of Enforcement. During his prior tenure at the Firm, Mr. Peikin led S&C's Criminal Defense & Investigations Group, advising clients in nearly every major enforcement initiative brought over the course of more than a decade. Before joining S&C, Mr. Peikin served for eight years as a prosecutor in the U.S. Attorney's Office for the Southern District of New York, including as Chief of the Securities and Commodities Fraud Task Force. Mr. Peikin has tried more than 20 criminal jury cases in federal court and argued numerous appeals before the U.S. Court of Appeals for the Second Circuit.



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**Julia A. Malkina** is a partner in S&C's Litigation Group and co-lead of the Firm's Securities Litigation Practice. She joined the Firm in 2015 after serving as a law clerk to Justices Sandra Day O'Connor (Ret.) and Stephen G. Breyer of the U.S. Supreme Court, a Bristow Fellow in the Office of the Solicitor General at the U.S. Department of Justice, and a law clerk to then-Judge Brett M. Kavanaugh of the U.S. Court of Appeals for the D.C. Circuit. Ms. Malkina's practice comprises appellate court litigation, trial court litigation, and regulatory proceedings in a number of areas, including securities, commodities, and criminal law. She was named a 2020 Rising Star by the *New York Law Journal* for her representations in precedent-setting cases across those areas. Ms. Malkina also represents clients pro bono in criminal matters both at the trial court level and on appeal. She is a member of S&C's Women's Initiative Committee, which seeks to recruit, retain, and advance the Firm's women lawyers.



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S&C provides superior legal representation to U.S. and non-U.S. corporations, financial institutions, and individuals in their most complex, high-value securities matters. Our lawyers have played a fundamental role in the evolution of U.S. banking and securities law and are well respected by courts, regulators, and adversaries. The Firm is regularly ranked as one of the top firms for defending securities litigation.

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S&C's Securities & Commodities Investigations & Enforcement Practice lawyers have a deep understanding of markets and complex trading and financial products. The Group regularly represents clients in investigations and enforcement actions by the SEC, the CFTC, FINRA, the National Futures Association, and other federal, state, and non-U.S. regulators and self-regulatory organizations. Clients facing securities and commodities investigations turn to S&C for our record of obtaining favorable outcomes in high-stakes matters.

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