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The Bulletin is a quarterly newsletter by Kessler Topaz Meltzer & Check to help institutional investors stay

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KESSLERTOPAZ MELTZERCHECK LLP

THE COVID-19 PANDEMIC DOES NOT SUSPEND OBLIGATIONS UNDER THE FEDERAL SECURITIES LAWS

Ryan T. Degnan, Esquire and Karissa J. Sauder, Esquire

Significant structural strains on equity markets often expose undisclosed risk lurking in investors' portfolios. The bursting of the dot-com and housing bubbles in the early and late 2000s, respectively, resulted in significant shareholder litigation under the federal securities laws. These actions sought compensation from corporate defendants for misleading investors about corporate performance and other investment risks. Like these prior events, the COVID-19 global pandemic has had a profound impact on the financial markets as uncertainty, economic disruption, and unemployment have generated significant investment losses. However, as was the case during the dot-com and housing bubbles, the COVID-19 pandemic does

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U.S. SUPREME COURT TO WEIGH IN ON REBUTTING THE FRAUD ON THE MARKET PRESUMPTION

Raphael Janove, Esquire

On December 11, 2020, the Supreme Court granted certiorari in *Goldman Sachs Group Inc. v. Arkansas Teacher Retirement System*, a recent decision from the Second Circuit on how defendants are permitted to oppose certification of securities class actions.[1] In *Goldman*, defendants argued that the false statements at issue had no impact on the stock price because the statements were too general for any reasonable investor to rely on. In other words, defendants challenged materiality — whether a false statement was material to investors — albeit couched in slightly different terms.

But past Supreme Court precedent makes it clear that materiality is not at issue during class certification. And by a 2-1 vote, the Second Circuit, like other courts before it, rejected defendants'

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[1] Appeal No. 20-222 (U.S. Dec. 11, 2020); *Arkansas Teacher Ret. Sys. v. Goldman Sachs Grp., Inc.*, 955 F.3d 254 (2d Cir. 2020).

"TRYING TIMES FOR TRIALS: DELAWARE CHANCERY COURT ADAPTS TO THE PANDEMIC"

Matt Benedict, Esquire

On Friday, March 13, 2020, attorneys from Kessler Topaz huddled with co-counsel in Wilmington, Delaware, making final preparations for a two-week trial against Tesla Motors founder Elon Musk in the Delaware Court of Chancery. After three-and-a-half years of litigation — during which plaintiffs in *In re Tesla Motors, Inc. Stockholder Litigation* survived motions to dismiss and for summary judgment, submitted six expert reports, and deposed more than twenty witnesses — a weekend was all that stood between the parties and the commencement of trial.

Or so they thought. That tumultuous week finally exposed the severity and extent of the public health threat caused by COVID-19. Schools began closing. The National Basketball Association put its season on hold. Ultimately, the federal government declared a national state of emergency, and the Delaware courts followed suit. On Friday the 13th, fittingly, the *Tesla* trial was taken off calendar indefinitely.

On Monday, March 16, instead of presiding over trial testimony by Tesla CEO Elon Musk concerning Tesla's expensive acquisition of Musk's sister company SolarCity, the Delaware Court of Chancery issued a standing order effectively prohibiting in-person courtroom activity for the next 30 days.

The Supreme Court renewed its declaration of judicial emergency on April 14 and May 14, 2020. These decisions were made in consultation with guidance from an infectious disease consultant hired by the court system, and followed Delaware Governor John Carney's direction that Delawareans stay at home unless engaged in essential business.

On June 5, the Supreme Court again extended the judicial emergency, but also introduced a four-stage plan for reopening courthouses to the public. Phase 2, beginning June 15, permitted non-jury civil trials for the first time since quarantine began. In order to protect against further spread of the coronavirus, the court system enacted numerous guidelines and restrictions. In addition to wearing masks at all times (except as expressly authorized by the judge), courthouse visitors and employees are screened for COVID-19 symptoms prior to building entry and required to remain in their designated, socially-distanced seats. No more than ten persons, excluding staff, are permitted in the courtroom at a time.

On June 15, 2020, Vice Chancellor Joseph Slights convened a telephonic status conference with counsel for the parties to discuss how to proceed with the *Tesla* trial. All parties were hopeful that by July 2020, the Delaware courts would move to Phase 3. While slightly less restrictive than Phase 2, even in Phase 3 no more than 14 persons would be permitted in the courtroom. Allowance for attendance by media and the public leaves each side's trial team (including witnesses) just four seats. The anterooms, where attorneys and clients customarily convene during breaks to discuss strategy, were limited to just two persons at a time. After consulting with the parties, the Vice Chancellor scheduled a "hybrid" trial — split approximately evenly between a week of live testimony and a week of remote proceedings via videoconferencing — beginning the last week of July.

All parties hoped that by July 2020, the worst would have passed. Unfortunately, by the summer of 2020, in Delaware as with the rest of the country, infection rates and hospitalizations got worse, not better. Across the nation, reluctance to impose and adhere to safeguards against the spread of COVID-19 allowed the virus to flourish rather than recede. Contrary to expectations, the Delaware courts did not enter Phase 3 in early July or, for that matter, any time last summer. Delaware transitioned to Phase 3 on October 5, 2020, but after COVID-19 cases and hospitalizations

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KTMC SECURES MAJOR LEGAL VICTORY IN CBS MERGER LITIGATION

Grant D. Goodhart, II, Esquire

On January 27, 2021, Vice Chancellor Joseph R. Slights III of the Delaware Court of Chancery issued an opinion in *In re CBS Corporation Stockholder Class Action and Derivative Litigation*, Consolidated C.A. No. 2020-0111-JRS, sustaining all but one of the claims asserted by Co-Lead Counsel KTMC on behalf of our client, Co-Lead Plaintiff Bucks County Employees Retirement Fund. In the 157-page opinion, which contains references to a wide array of Delaware case law and legal scholarship, as well as such diverse sources as *Rolling Stone* magazine, *Game of Thrones* author George R.R. Martin, and Greek mythology, Vice Chancellor Slights holds that the stockholder plaintiffs adequately pled their claims against CBS's (now known as ViacomCBS) Board Chair and controlling stockholder Shari Redstone, other members of the CBS board of directors, and former CBS President Joseph Ianniello challenging their conduct in connection with the December 2019 merger of CBS and Viacom, Inc., also controlled by Ms. Redstone.

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DELAWARE SUPREME COURT AFFIRMS STOCKHOLDERS' RIGHTS TO INVESTIGATE AMERISOURCEBERGEN'S OPIOID DISTRIBUTION PRACTICES

Justin O. Reliford, Esquire

On December 10, 2020, the Supreme Court of Delaware issued a landmark ruling affirming the rights of AmerisourceBergen Corp. stockholders to investigate possible wrongdoing in connection with the company's opioid distribution practices.[1] In the process, the Supreme Court also provided a clear signal to corporations that attempt to litigate the merits of potential claims of wrongdoing *before* turning over their corporate records.

The Supreme Court's ruling affirmed a post-trial judgment in favor of Kessler Topaz's client, Lebanon County Employees' Retirement Fund ("Lebanon County"). In the trial court's opinion, Vice Chancellor Travis J. Laster ruled that Lebanon County and another institutional stockholder were entitled to relatively broad ranging discovery into the opioid distribution practices at AmerisourceBergen, as well as its directors' oversight of those practices.

Opioid distributors, like AmerisourceBergen, have a responsibility to implement internal controls that help identify and report suspicious orders of opioids to appropriate state and federal authorities. According to allegations from numerous regulators and prosecutors, for over a decade, AmerisourceBergen did not comply with these and other legal requirements. These failures, in turn, have contributed to a nationwide opioid epidemic that kills over 100 Americans daily.

The opioid epidemic is readily apparent in Pennsylvania — the state Lebanon County, AmerisourceBergen, and Kessler Topaz all call home.[2] As Pennsylvania Secretary of Drug and Alcohol Programs Jenny Smith explained, "We're still losing 4,000 Pennsylvanians every year."[3] In Lebanon County, Pennsylvania, overdose deaths spiked in 2020, with the county recording 21 overdoses deaths by just August. This compares to 27 fatal overdoses in the county for the entire 2019 calendar year.[4]

Against the backdrop of a growing opioid epidemic, Lebanon County took action. In May 2019, Lebanon County served AmerisourceBergen with a demand under section 220 of the Delaware General Corporation Law ("Secton 220") to inspect the company's records related to opioid

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[1] *See AmerisourceBergen Corp. v. Lebanon County Employees' Retirement Fund, et al.*, ---A.3d---, 2020 WL 7266362 (Del. 2020).

[2] Although it is a Delaware corporation, AmerisourceBergen's corporate headquarters are located in Chesterbrook Pennsylvania.

[3] *See* J. Falk, "Lebanon County native spearheading PA's fight against the opioid epidemic," July 23, 2020, available at https://lebtown.com/2020/07/23/lebanon-county-native-spearheading-pa-s-fight-against-the-opioid-epidemic/ (last visited January 27, 2021).

[4] *See* N. Shelly, "Lebanon officials raise alarm about increases in overdoses in 2020," August 13, 2020, available at https://www.ldnews.com/story/news/2020/08/13/lebanon-county-city-pa-opioid-overdose-deaths-fentanyl-coronavirus/3355097001/ (last visited January 27, 2021).

DELAWARE SUPREME COURT AFFIRMS STOCKHOLDERS' RIGHTS TO INVESTIGATE AMERISOURCEBERGEN'S OPIOID DISTRIBUTION PRACTICES *(continued from page 3)*

distribution and anti-diversion controls.[5] The demand specifically cited potential wrongdoing at AmerisourceBergen alleged by numerous government regulators and investigators. AmerisourceBergen refused the demand, claiming that Lebanon County lacked a proper purpose for its inspection. The trial and appeal followed.

In its unanimous opinion — issued 18 months after Lebanon County's demand — the Supreme Court easily dispatched with AmerisourceBergen's substantive arguments. The Court flatly rejected the company's primary contention that a stockholder must establish a credible basis to suspect "actionable wrongdoing" before stating a proper purpose. According to AmerisourceBergen, the Section 220 demand principally focused on investigating potential derivative claims — i.e., claims that directors and officers breached their fiduciary duties to the company. Thus, the company argued that stockholders had to prove their potential derivative claims could result in personal liability for the company's fiduciaries *before* it had to turn over records.

The Supreme Court made clear that "actionable wrongdoing" is not the standard applicable to Section 220, which asks only whether a stockholder has a proper purpose for the demand.[6] The Court reconciled (or otherwise overruled) a number of its prior precedents by noting that such arguments are appropriate where a stockholder's *only* purpose for inspection is the pursuit of derivative claims.[7] Lebanon County's Section 220 demand, however, stated several proper purposes that did not involve litigation at all. The Court likewise held that stockholders seeking to inspect corporate wrongdoing do not even need "to specify the ends to which it might use the books and records."[8] Thus, the opinion generally confirms that investigating wrongdoing and mismanagement will always be a proper purpose to seek corporate records, regardless of whether litigation ultimately follows.

The Supreme Court also rejected AmerisourceBergen's overall efforts to litigate the merits of the potential derivative claims that its stockholders might bring, after inspecting corporate records. Confirming that Section 220 trials are intended a summary actions, with low burdens of proof for stockholders, the Supreme Court issued a strong admonishment to Delaware corporations: "It has become evident that the interjection of merits-based defenses — defenses that turn on the quality of the wrongdoing to be investigated — interferes with [the 220] process."[9] Thus, the opinion directs Delaware judges to "defer the consideration" of merits-based defenses, absent the "rare case" where: (1) the stockholders' sole purpose is pursuing a derivative claim; and (2) that derivative claim is unquestionably "dead on arrival."[10]

At its core, the opinion represents a great success for Delaware stockholders willing to take a stand against corporate wrongdoing and mismanagement. As recognized by the Supreme Court's ruling, where there is a credible basis to suspect corporate wrongdoing, Section 220 should always be available to stockholders willing to take action to protect their interests and the companies they own.[11] ■

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[5] *See* 8 Del. C. §220.

[6] *Id.* at *13-14.

[7] *Id.*

[8] *Id.* at *7.

[9] *Id.* at *13.

[10] *Id.* at *14.

[11] Much like the opioid crisis itself, the battle over corporate accountability for that crisis continues. Kessler Topaz is also representing individual stockholders of Cardinal Health, Inc., one of the nation's other leading opioid distributors, in a federal derivative action in Ohio. *See In re Cardinal Health, Inc. Derivative Litig.*, Case No. 2:19-cv-2491-SDM (S.D. Ohio). That action alleges that the officers and directors of Cardinal Health failed to implement and monitor appropriate internal controls over its opioid distribution practices, in breach of their fiduciary duties under Ohio law. There, Kessler Topaz's clients likewise took advantage of Ohio's stockholder inspection laws to obtain confidential, board-level documents regarding Cardinal Health's opioid distribution and anti-diversion practices. On January 21, 2021, the Hon. Sarah D. Morrison heard argument on the Cardinal Health defendants' motion to dismiss the derivative action. While Judge Morrison has not ruled on the motion, at argument, she noted that the complaint, which was based on the company's books and records, identified 53 different potential "red flags" of unlawful conduct that the board potentially ignored.

REVISIONS TO CHINESE SECURITIES LAWS INCLUDE MORE ROBUST DISCLOSURE REQUIREMENTS AND A MECHANISM FOR REPRESENTATIVE OPT-OUT SHAREHOLDER LITIGATION

Emily N. Christiansen, Esquire

On March 1, 2020, China's revised Securities Law went into effect. The revised Securities Law is a major revision to comprehensive securities legislation that first went into effect in China on July 1, 1999 and has been modified only a handful of times since then. In this new revision, over 100 articles were modified to, *inter alia,* change the rules for initial public offerings from "Approval-based" to "Registration-based," add extraterritorial jurisdiction provisions that provide for liability under China's law when activity on an exchange or over the counter outside of China disrupts China's markets or damages legitimate rights of Chinese investors, enhances the securities trading mechanism, and increases the amount of regulator-issued fines for various violations of the law. Additionally, two new chapters regarding information disclosure and investor protection were added.

The newly added Chapter V of the Securities Law adds provisions designed to improve information disclosure and better protect the right of an investor to know pertinent information about the operations of a company. The most salient provisions of the new law: broaden the scope of required information disclosure; outline specific quality requirements (namely that information must be true, accurate, complete, concise, etc. and may not contain any false or misleading statements or material omissions); require that, where a stock trades both domestically and overseas, information disclosed overseas must be simultaneously disclosed in China; specify the content of information disclosure (including providing details on significant events that likely have a significant impact on the trading price of securities); and outline the obligations of board of directors, executives, and senior management in the disclosure process and grant them the right to object to the content of information in disclosures made by the company.

Chapter VI, the newly added chapter on investor protection, enhances protections for all investors but has a specific focus on enhancing protections for small and medium sized investors and draws a distinction between

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THE EASTERN DISTRICT OF VIRGINIA DENIES STATE FARM'S MOTION TO DISMISS BUSINESS INTERRUPTION CLAIMS RESULTING FROM ORDERS SHUTTING DOWN BUSINESSES DUE TO COVID-19

Jordan E. Jacobson, Esquire and Natalie Lesser, Esquire

Kessler Topaz recently achieved a rare success, overcoming efforts by State Farm[1] to dismiss a complaint filed on behalf of Virginia small businesses seeking coverage for business interruption losses resulting from social distancing and/or stay-at-home orders (the "Orders") in connection with the COVID-19 pandemic.

In March 2020, Virginia, like many other states, declared a state of emergency and the Governor of Virginia issued a series of Orders closing all recreational and entertainment businesses and ordering all individuals to remain at their place of residence, except when engaging in certain necessary activities. As a result of these Orders aimed at stemming the spread of COVID-19, Plaintiff Elegant Massage, LLC ("Plaintiff") and other Virginia businesses were forced to cease operations. Plaintiff and other small businesses that purchased "all risk" commercial property insurance from State Farm timely tendered insurance claims, seeking reimbursement for lost income as a result of closing their businesses in response to the Orders. These businesses paid substantial premiums to State Farm to cover

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[1] "State Farm" or "Defendants" include: State Farm Automobile Insurance Company and State Farm Fire and Casualty Company.

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not suspend the obligation of public companies and their executive officers to communicate truthfully with investors, and securities litigation continues to provide a useful tool for investors to recover damages caused by materially misleading statements.

In recent months, investors have filed numerous securities fraud class actions under the federal securities laws in response to instances where companies and their executive officers have caused investment losses by misleading the market regarding their responses to COVID-19, the effects of COVID-19 on their businesses, and more. Indeed, since March 2020, when many states began to implement stay-at-home orders and the pandemic began to dramatically affect most industries, more than twenty companies have been sued under the federal securities laws in connection with misrepresentations directly relating to the pandemic and its effect on the companies. Similarly, the United States Securities and Exchange Commission (the "SEC") has initiated enforcement actions against a growing number of companies regarding misrepresentations about COVID-19. The SEC's enforcement actions illustrates that regulators are not allowing corporations to point to the sudden and unforeseen onset of the pandemic as a basis to avoid proper disclosure. Notably, the SEC is widely expected to become more active in its scrutiny and regulation of companies under President Biden's nominee for SEC Chair, Gary Gensler, who is known for his aggressive regulatory work while Chair of the Commodity Futures Trading Commission during the Obama administration.

As discussed below, these class action lawsuits and enforcement actions involve a variety of industries and types of misrepresentations, demonstrating that investors should be vigilant for companies who may use the pandemic as a basis to misrepresent their business operations. While all of the private actions are still in their infancy — with none yet receiving a ruling on a motion to dismiss — they, coupled with the government's interest, demonstrate the wide-ranging misconduct that has occurred as companies have attempted to minimize risks and/or capitalize on business opportunities presented by the COVID-19 pandemic.

Pharmaceuticals and Medical Manufacturing

Perhaps unsurprisingly, many of the securities class actions filed during the COVID-19 pandemic have alleged misrepresentations about pharmaceuticals and other medical products intended to diagnose, treat, or otherwise respond directly to COVID-19.

In the first such action, filed on March 12, 2020, the plaintiffs alleged that Inovio Pharmaceuticals, Inc. ("Inovio") and its Chief Executive Officer falsely stated that Inovio had successfully developed a COVID-19 vaccine in just three hours and would soon be conducting vaccine trials.[1] According to the plaintiffs, the truth began to emerge when a short seller publicly called for an SEC investigation into Inovio's "ludicrous and dangerous claim that they designed a vaccine in 3 hours," and stated that Inovio "has been a serial stock promotion for years." The amended complaint, filed in September 2020, further alleged that the defendants also made false statements about Inovio's selection for the federal government's Operation Warp Speed vaccine funding program and Inovio's ability to produce certain doses of its purported vaccine, and that the defendants timed certain at-the-market stock offerings in order to raise critical cash while the stock price was inflated due to their false statements about Inovio's vaccine.

Other cases have similarly alleged that pharmaceutical companies have misled investors regarding sources of funding for COVID-related products, such as Operation Warp Speed and large purchase orders. For example, investors have sued SCWorx Corp. ("SCWorx") and its Chief Executive Officer, who announced in April 2020 that SCWorx had received a committed purchase order of two million COVID-19 rapid testing kits, with provision for additional weekly orders of 2 million units for twenty-three weeks.[2] According to the plaintiffs, this announcement

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[1] *McDermid v. Inovio Pharm., Inc.*, No. 2:20-cv-01402 (E.D. Pa. filed Mar. 12, 2020).

[2] *Yannes v. SCWorx Corp.*, No. 1:20-cv-03349 (S.D.N.Y. filed Apr. 29, 2020).

was revealed to be false just a few days later, when a short seller issued a report that labeled the deal "completely bogus." Similarly, investors have sued Vaxart, Inc. ("Vaxart") and certain of its executive officers and directors, alleging that Vaxart falsely suggested that it would be receiving significant financial support from Operation Warp Speed and that the defendants, which include a major Vaxart shareholder, engineered substantial insider trading while the stock price was inflated as a result of these misrepresentations.[3] Investors have also alleged that Eastman Kodak Company ("Kodak") officers engaged in insider trading following public statements about funding for COVID-related efforts.[4] Specifically, according to the plaintiffs, Kodak insiders improperly leaked news that Kodak would be receiving a $765 million loan under the Defense Production Act to produce ingredients for COVID-19 drugs — then profited from transactions timed to take advantage of the resulting risk in Kodak's stock price. Revelation of this misconduct has delayed the disbursement of the loan funds to Kodak.

Other pandemic-related securities actions have alleged that companies overstated the accuracy of the COVID-19 diagnostic tests they had developed. For example, investors have alleged that both Co-Diagnostics, Inc.[5] and Chembio Diagnostics, Inc.[6] falsely claimed that their respective COVID-19 tests were 100% accurate. And, recently, investors sued Decision Diagnostics Corp. ("Decision Diagnostics") for falsely stating that the company had developed a finger-prick blood test that could detect COVID-19 in less than one minute.[7]

Travel, Facilities, and Technology

COVID-related securities actions have also alleged that companies have made false representations regarding their readiness and ability to respond to pandemics, generally, and COVID-19, specifically. For example, a series of cases against cruise lines have claimed that cruise companies misrepresented their commitment to health and safety and failed to implement appropriate safety protocols in light of COVID-19. First, on March 12, 2020, investors sued Norwegian Cruise Lines ("Norwegian") and certain of its executive officers, alleging that Norwegian falsely claimed that the safety of its guests and crew was of the utmost importance.[8] As the plaintiffs alleged, the defendants' misrepresentations were revealed when whistleblowers leaked internal emails directing sales staff to lie about the risks of COVID-19 in order to protect the company's bookings. Sales staff were instructed to falsely assure potential customers that, among other things, "[t]he Coronavirus can only survive in cold temperatures, so the Caribbean is a fantastic choice for your next cruise." Two months later, investors — represented by Kessler Topaz — similarly sued Carnival Corporation ("Carnival") for concealing the existence of COVID-19 outbreaks on Carnival ships and for falsely representing that health and safety were a top priority while Carnival ships were failing to follow necessary health and safety protocols.[9] According to the plaintiffs, the truth began to emerge when media outlets reported that Carnival had, for example, continued to launch ships even after the company received specific warnings about COVID-19, failed to report known COVID-19 cases on Carnival ships to the necessary authorities, and allowed passengers to continue circulating as usual for days after COVID-19 cases were confirmed on their ships. More recently, in October 2020, investors similarly alleged that Royal Caribbean Cruises Ltd. had downplayed the significance of COVID-19 and failed to implement rigorous safety protocols aboard its ships.[10]

The GEO Group, Inc. ("GEO Group") — which operates facilities such as halfway houses and U.S. Immigration and Customs Enforcement processing centers — faces similar allegations regarding misrepresented capabilities. Specifically, plaintiffs have alleged that GEO Group and its officers' statements regarding GEO Group's commitment to mitigating COVID-related risks and implementing thorough safety protocols were false, as revealed by media reports disclosing significant and unmitigated COVID-19 outbreaks at GEO Group facilities.[11] According to *The Intercept*, for example, one GEO Group halfway house kept its residents in overcrowded conditions even as positive diagnoses continued to increase at the facility.

Several other securities class actions have involved technology companies that have seen a staggering increase in demand due to the pandemic. For

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[3] *Himmelberg v. Vaxart, Inc.*, No. 3:20-cv-05949 (N.D. Cal. filed Aug. 24, 2020).

[4] *Tang v. Eastman Kodak Co.*, No. 3:20-cv-10462 (D.N.J. filed Aug. 13, 2020); *McAdams v. Eastman Kodak Co.*, No. 1:20-cv-06861 (S.D.N.Y. filed Aug. 26, 2020).

[5] *Gelt Trading v. Co-Diagnostics, Inc.*, No. 2:20-cv-00368 (D. Utah filed June 15, 2020).

[6] *Chernysh v. Chembio Diagnostics, Inc.*, No. 2:20-cv-02706 (E.D.N.Y. filed June 18, 2020).

[7] *Sanchez v. Decision Diagnostics Corp.*, No. 2:21-cv-00418 (C.D. Cal. Jan. 15, 2021).

[8] *Douglas v. Norwegian Cruise Lines*, No. 1:20-cv-21107 (S.D. Fla. Mar. 12, 2020).

[9] *Service Lamp Corp. Profit Sharing Plan v. Carnival Corp.*, No. 1:20-cv-22202 (S.D. Fla. filed May 27, 2020).

[10] *City of Riviera Beach Gen. Emps. Ret. Sys. v. Royal Caribbean Cruises LTD*, No. 1:20-cv-24111 (S.D. Fla. filed Oct. 7, 2020).

[11] *Hartel v. The GEO Group, Inc.*, No. 9:20-cv-81063 (S.D. Fla. filed July 7, 2020).

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example, investors have alleged that Zoom Video Communications, Inc. made false representations regarding its technological security, as discovered after demand for the company's services rocketed as a result of stay-at-home orders and the company became far more scrutinized.[12] Likewise, K12, Inc. — which offers online schooling programs — faces allegations that its officers falsely claimed that the company was prepared to handle a surge in demand as schools flocked to its services (which, in several high-profile instances, failed).[13]

Finance and Manufacturing

While the cases against pharmaceutical, travel, facilities, and technology companies have largely involved the companies' ability to *directly respond to* COVID-19, securities actions have also alleged that companies in other industries misrepresented the broader *effects of* COVID-19 on their businesses.

For example, cases involving exchange-traded funds that purportedly track the price of crude oil and crude oil futures contracts — United States Oil Fund[14] and ProShares Ultra Bloomberg Crude Oil,[15] respectively — have alleged that the defendants concealed the effects of oil market volatility resulting from the pandemic. Similarly, investors have alleged that Lexinfintech Holdings Limited ("Lexinfintech") — an online consumer finance platform — concealed the extent of borrower delinquency rates resulting from COVID-19.[16] According to the plaintiffs, a short seller report revealed that Lexinfintech had secretly been extending the maturity of delinquent loans — which had greatly increased in number as a result of COVID-19 — in order to make its finances appear healthier than they were. Likewise, investors have also sued Elanco Animal Health Incorporated and certain of its executive officers, alleging that they concealed the extent to which COVID-19 was impacting the company's distributors and forcing the company to reduce its channel inventory.[17]

SEC Enforcement Actions

In addition to securities class actions filed by investors, a growing number of companies are facing enforcement actions by the SEC relating to their misrepresentations about COVID-19.

In April and May 2020, during the initial stages of the pandemic, the SEC filed several enforcement actions, including actions against Praxsyn Corp. for false statements about the company's ability to supply N95 face masks, Applied Biosciences Corp. for misleading statements regarding the company's plan to develop a COVID-19 home testing kit, and Turbo Global Partners, Inc. for false statements about an agreement to sell equipment that could identify people with elevated temperatures in crowds. Several months later, in September 2020, the SEC filed an enforcement action against the President of Arrayit Corporation alleging false statements about the development of the company's COVID-19 test. The SEC also announced several actions in December 2020, including an enforcement action against Decision Diagnostics and its Chief Executive Officer — who, as discussed above, allegedly misled investors by claiming that the Company had developed a finger-prick COVID-19 test. The SEC also recently settled charges against The Cheesecake Factory which, according to the SEC, misled investors by representing in March and April 2020 that it was "operating sustainably," when in fact the company had informed its landlords it would not be paying rent in April, drew down the last $90 million available under a line of credit, and disclosed to potential lenders that the company was losing $6 million per week and had only a few months of cash remaining.

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[12] *Drieu v. Zoom Video Communications, Inc.*, No. 3:20-cv-02353 (N.D. Cal. filed Apr. 7, 2020).

[13] *Lee v. K12, Inc.*, No. 1:20-cv-01419 (E.D. Va. filed Nov. 19, 2020).

[14] *In re: United States Oil Fund, LP Sec. Litig.*, No. 1:20-cv-04740 (S.D.N.Y. filed June 19, 2020).

[15] *Di Scala v. ProShares Ultra Bloomberg Crude Oil*, No. 1:20-cv-05865 (S.D.N.Y. filed July 28, 2020).

[16] *In re LexinFintech Holdings Ltd. Sec. Litig.*, No. 3:20-cv-01562 (D. Or. filed Sep. 9, 2020).

[17] *Hunter v. Elanco Animal Health Inc.*, No. 1:20-cv-1460 (S.D. Ind. May 20, 2020).

Conclusion

These class actions and enforcement actions involve a broad-spectrum of industries and cover various types of misrepresentations. Some of the cases arise directly from companies' affirmative or purported efforts to capitalize on the pandemic, as in the cases involving pharmaceuticals and other medical products, while other cases concern the failure of certain companies to respond appropriately to the risks presented by the pandemic, as in the cases involving cruise ships, detention facilities, and communications technology. Still other cases concern companies' misrepresentations about the pandemic's general impact on various market forces. The lawsuits may ultimately provide valuable avenues for investors to recover some of the losses they have sustained as a result of various misconduct during the pandemic. As such, investors should continue to explore opportunities to file or take leading roles in these and future actions, including future actions that may arise in connection with businesses' purported abilities to recover and adapt in a post-vaccine economic recovery. ■

KTMC SECURES MAJOR LEGAL VICTORY IN CBS MERGER LITIGATION

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Plaintiffs alleged that the merger of CBS and Viacom (referred to as the "Merger") was the culmination of a years-long effort by Shari Redstone to combine the two companies in order to save the floundering Viacom, despite the lack of economic merit of the Merger and the opposition of CBS directors and stockholders alike. Plaintiffs alleged that Shari Redstone wrested control of NAI (the holding company that controls CBS and Viacom) from her ailing father Sumner Redstone, and twice previously attempted to merge CBS and Viacom and failed. The first time she was rebuked by the CBS board of directors, after which she publicly proclaimed that "the merger would get done even if [she had] to use a different process."

Two years later, Ms. Redstone was back at it, attempting to force a CBS-Viacom merger. This time the CBS board was so concerned that Ms. Redstone would force a merger over their objections, that they took the "extraordinary" measure of attempting to dilute Ms. Redstone's control of CBS to protect CBS and its stockholders from her influence. After hard-fought, expedited litigation, a settlement was reached that resulted in the CBS board turning over, and the addition of six new directors hand-picked by Ms. Redstone. Importantly, Ms. Redstone and NAI also agreed that they would not propose that CBS and Viacom merge for a period of two years following the settlement.

In spite of the settlement's prohibitions, Plaintiffs allege that Ms. Redstone and NAI pushed forward. Only four months after the settlement Shari Redstone caused the new CBS board — whom she had largely hand-picked — to form a committee to evaluate a merger with one primary target: Viacom. Ms. Redstone sidelined carry-over directors who opposed her, enticed CBS's acting CEO Joseph Ianniello (who previously opposed the Merger) to support her with hefty compensation packages, and worked to impose her views on an ultimate tie up through Ianniello's newfound support. As controlling stockholders of CBS, NAI and Ms. Redstone decided not to give CBS's minority stockholders any say on the Merger — such as by permitting them to vote — and instead pushed the Merger through on deal terms that benefitted NAI and Viacom to the detriment of CBS and its stockholders in violation of their fiduciary duties.

In the end, Plaintiffs allege that the Merger forced the poorly performing Viacom on CBS and destroyed value for CBS and its stockholders for NAI's benefit. Plaintiffs brought both direct class and stockholder derivative claims in the Delaware Court of Chancery in the Spring of 2020, and alleged that the current ViacomCBS board was conflicted and, therefore, not able to entertain a stockholder demand to initiate litigation against the board and NAI. In its opinion, the Court credited nearly all of Plaintiffs' allegations and held that the transaction was a "conflicted controller transaction" where Shari Redstone "engineered the Merger to bail out Viacom for the benefit of NAI, and thereby extracted a non-ratable benefit from the transaction." Vice Chancellor Slights noted in response to Defendants' arguments that "A sinking ship remains a sinking ship, regardless of its proximity (spatial or temporal) from rock-bottom; and Plaintiffs have satisfactorily pled Ms. Redstone believed Viacom needed to be rescued at the time of the Merger."

With respect to Plaintiffs' class claims, the Court ruled that sufficient to survive were Plaintiffs' claims that "Ms. Redstone coerced Ianniello and the CBS Board into playing roles in the dramedy that culminated in the Merger, where CBS ostensibly played the role of acquirer" despite that what "really happened" was that "Ms. Redstone, desperate to combine Viacom and CBS, and viewing Viacom as the entity that would emerge from the Merger as superior, caused CBS to be subjugated by Viacom's Board and management in a combined company that would henceforth be known as ViacomCBS."

The case will now proceed to discovery, with a trial expected to be set for some time in mid- to late-2022. ■

"TRYING TIMES FOR TRIALS: DELAWARE CHANCERY COURT ADAPTS TO THE PANDEMIC"

(continued from page 2)

more than tripled levels from June, the Supreme Court issued an administrative order on November 16, 2020 reverting back to Phase 2.

Interstate travel restrictions announced by numerous governors in June and July mandated that witnesses and attorneys residing in New York, California, and other states quarantine for more than a week before and/or after visiting a Delaware courthouse. Wary of compelling witnesses to appear in court at substantial risk to their own and others' health, the Vice Chancellor continued the trial yet again. The Tesla trial is currently set to proceed in July of 2021. Hopefully a live trial will be able to go forward on that date.

Other cases besides the *Tesla* trial are moving forward, as litigants have increasingly opted to move ahead with fully remote trials.

During the past year, out of necessity legal professionals gained considerable experience and comfort in using video conferencing platforms to take part in depositions and oral arguments and other traditionally in-person court activity. Platform capabilities are evolving rapidly. Even when located an ocean away from one another, an examining attorney and deponent can see and hear each other clearly and produce a clean record in real time. The attorney can share an exhibit electronically as quickly as she can slide a paper across the table, and during breaks can consult team members in a private chat room as though they were meeting behind the closed doors of a conference room down the hall.

In *Forescout Techs., Inc. v. Ferrari Grp. Hldgs., L.P.,* 2020 WL 3971012 (Del. Ch. July 14, 2020), Delaware Vice Chancellor Glasscock denied defendants' request to adjourn an expedited trial when doing so would render the equitable relief sought by the plaintiff practically unattainable. The Court determined that the unwillingness of plaintiff's key witness to travel from California to Delaware in the midst of a pandemic was reasonable, and that "justice would best be served with a remote presentation of [the witness'] cross-examination." The Court agreed to submit for interlocutory review the question of whether requiring a "Zoom" cross-examination of the witness, with the Vice Chancellor presiding virtually via computer, is consistent with defendants' due process rights and within the trial court's discretion. Ultimately, the Delaware Supreme Court did not need to answer the question because the parties agreed to settle their litigation on the following day.

Aside from one-day corporate "books and records" trials that the Court of Chancery resumed hearing at the beginning of Phase 2 in June, the first "Zoom" trial held by the Court occurred in late August in the matter of *AB Stable VIII v. Maps Hotels and Resorts One LLC,* 2020 WL 7024929, at *4 (Del. Ch. Nov. 30, 2020). Conducting the trial by "Zoom" in this instance was a necessity: the controversy concerned a transaction featuring a September 2020 drop-dead closing date, such that postponement was out of the question, and the principal litigants were based in China and Korea and thus restricted from traveling to Delaware no matter what health risks they may have been willing to assume. The trial lasted five days and ran smoothly given the immensity of the undertaking.

Thus far, a "hybrid" trial such as that contemplated by the *Tesla* parties has yet to occur in the Delaware Court of Chancery. Chief Justice Seitz has authorized the state's courts to conduct proceedings remotely "to the greatest extent possible" while the judicial emergency continues. *See* Administrative Order No. 15, In re: COVID-19 Precautionary Measures (Del. Dec. 30, 2020), at 3. Following this directive, the Court of Chancery has consistently adapted to the current moment by seeking the best available balance between the public health and litigants' interest in obtaining timely resolution of their disputes. In certain instances, "Zoom" trials are the closest the Court can come to achieving that balance.

But while attorneys and judges have demonstrated the means to conduct trials by videoconference, "Zoom" trials are by no means ideal. Apart from the technical difficulty interruptions that IT professionals (and amateurs) work hard to make less inevitable, courtroom trials have very real advantages. The gravitas of the courtroom is more keenly felt without the filter of a videoconference interface. Credibility determinations can be made more confidently regarding testimony made in person. A rapport with a trial witness, or opposing counsel, can be developed more naturally when a handshake is within reach. Demonstrative exhibits can be more persuasive in the courtroom, rather than re-sized to fit on a segment of each user's computer screen. And perhaps most importantly, communication among litigation team members occurs much more efficiently when the team can physically huddle together to share ideas and reach consensus — especially in the context of complex litigation requiring more than a dozen attorneys, numerous paralegals, and multiple expert witnesses to quickly understand one another and what's transpiring in a trial that is already inherently compressed for time.

In his opinion denying the *Ferrari* defendants' request for an adjournment, Vice Chancellor Glasscock observed, "The trial date was imposed on May 28, 2020. At that point, I was hopeful that viral conditions would abate by July 20. Manifestly, that hope has proved misplaced." Even now, and even with multiple vaccines in distribution, the scope and duration of the impact of the pandemic, both globally and in Delaware, remain impossible to predict with any precision. Identifying and improving appropriate procedural solutions in response to changing public health considerations is a project that courts and litigants will likely be tackling for years. ■

U.S. SUPREME COURT TO WEIGH IN ON REBUTTING THE FRAUD ON THE MARKET PRESUMPTION *(continued from page 1)*

attempts to smuggle materiality into class certification. While defendants can defeat class certification by showing that the statements did not affect the stock price, defendants cannot challenge the lack of price impact by arguing the statements were immaterial.

The highly-watched certiorari petition (the "Petition") arising out of *Goldman* presents the Supreme Court with the opportunity to address the tension between defendants' right to challenge price impact at class certification with the prohibition on challenging materiality at this stage of the litigation. The Petition also asks the Court to impose a greater burden on plaintiffs at class certification, arguing that plaintiffs carry the burden of persuasion on price impact. While we do not know how the Supreme Court will ultimately rule, the decision in this case has at least the potential to affect the evidence that can be considered at class certification. As a result, it is being closely watched by the securities bar.

The Basic Presumption and the Price Maintenance Theory

The Petition implicates four leading Supreme Court decisions on securities class actions. In 1988, the Court in *Basic*[2] established a rebuttal presumption of class-wide reliance in securities cases. Under what is commonly referred to as the "fraud on the market" presumption of reliance, a plaintiff at class certification needs to show that a company's stock trades in an efficient market — meaning that the stock price incorporates all publicly available, material information. If the market is efficient, courts presume that those who invested in the company's stock "d[id] so in reliance on the integrity of that price."[3] The *Basic* presumption is a bedrock principle upon which securities class actions are based as it dispenses with individualized proof of each class members' reliance on a company's false statements, which if necessary would likely preclude class-wide adjudication of claims.

At the same time, *Basic* also held that the presumption of reliance may be rebutted with "[a]ny showing that severs the link between the alleged misrepresentation and either the price received (or paid) by the plaintiff, or his decision to trade at a fair market price."[4] However, in the years since *Basic* has been decided, courts have struggled with which types of evidence can be used to "sever[]" this link. This thorny issue arises particularly where evidence on price impact overlaps with issues that, post-*Basic*, the Supreme Court has held cannot be raised during class certification.

In 2011, the Supreme Court in *Halliburton I* held that loss causation (that the defendant's fraud caused the plaintiff's losses) need not be proved at class certification.[5] In 2013 in *Amgen*, it held that materiality was also not at issue at class certification.[6] Then in 2014 in *Halliburton II*, while the Court clarified that defendants can use both "direct as well as indirect price impact evidence" to rebut the presumption, it affirmed *Amgen*'s holding that defendants cannot attack materiality in opposing class certification.[7] To wit, *Halliburton II* reasoned that because "materiality is a discrete issue that can be resolved in isolation from the other prerequisites, it can be wholly confined to the merits stage."[8]

To understand *Goldman*, it is also helpful to have familiarity with the "price maintenance" or "inflation-maintenance" theory that is at issue in many securities class actions. This theory, which courts have widely embraced, is based on the factual and economic predicate that false information can falsely affirm market expectations about a company's prospects and thus maintain its stock price.[9] In such cases,

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[2] *Basic v. Levinson*, 485 U.S. 224 (1988).

[3] *Id.* at 247.

[4] *Id.* at 248.

[5] *Erica P. John Fund, Inc. v. Halliburton Co.*, 563 U.S. 804 (2011).

[6] *Amgen Inc. v. Connecticut Ret. Plans & Tr. Funds*, 568 U.S. 455, 467 (2013).

[7] *Halliburton Co. v. Erica P. John Fund, Inc.*, 573 U.S. 258, 283 (2014).

[8] *Id.* at 282-283.

[9] *See, e.g., In re Advance Auto Parts, Inc., Sec. Litig.*, 2020 WL 6544637, at *4 (D. Del. Nov. 6, 2020) (collecting cases); *In re Vivendi, S.A. Sec. Litig.*, 838 F.3d 223, 259 (2d Cir. 2016); *Glickenhaus & Co. v. Household Intern., Inc.*, 787 F.3d 408, 418 (7th Cir. 2015); *FindWhat Investor Grp. v. FindWhat.com*, 658 F.3d 1282, 1316 (11th Cir. 2011); *In re CenturyLink Sales Practices & Sec. Litig.*, --- F.R.D.---, 2020 WL 5517483, at *10 (D. Minn. Sept. 14, 2020); *Plymouth Cty. Ret. Sys. v. Patterson Cos., Inc.*, 2020 WL 5757695, at *11 (D. Minn. Sept. 28, 2020).

defendants cannot establish a lack of price impact simply by showing that the false statements did not inflate the price of the stock when they were made. Rather, the defendant must establish that there was no "back-end impact" when the relevant truth was revealed to the market. Courts use this back-end impact as a proxy for the amount of artificial inflation (*i.e.*, price impact) resulting from a false statement. In short, the amount the stock price dropped once the relevant truth was revealed demonstrates how much the price was artificially inflated (whether by maintenance of otherwise) as a result of the earlier false statements.

The Second Circuit's Decision

Against this legal backdrop comes the Second Circuit's 2-1 decision in *Goldman.* There the Court of Appeals was presented with the application of the price maintenance theory where: 1) there was a lack of front-end price impact when the false statements were made; and 2) defendants argued that the statements lacked price impact because, in effect, they were immaterial.

Goldman arose out of Goldman's packaging of subprime mortgages into complex investment vehicles called collateralized debt obligations ("CDO"s), which Goldman offered to its clients. Between 2006 and 2010, Goldman made statements that assured the public that it took the necessary steps to prevent conflicts of interest. For example, it stated:

- "We have extensive procedures and controls that are designed to identify and address conflicts of interest";
- "Integrity and honesty are at the heart of our business"; and
- "We are dedicated to complying fully with the letter and spirit of the laws, rules and ethical principles that govern us."[10]

Unbeknownst to investors, Goldman had allowed a hedge fund to select the mortgages included in certain CDOs with a goal of causing the CDOs to fail, and that hedge fund ultimately made some $1 billion when those CDOs inevitably plummeted in value. The SEC announced its investigation into these conflicted transactions, and Goldman's stock dropped 13%. Goldman then paid the SEC a $550 million fine and plaintiffs, Goldman's shareholders, brought a securities fraud lawsuit against Goldman and several of its directors. Plaintiffs alleged that Goldman's statements about being conflict-free artificially maintained the stock price and the revelations of these conflicts were "corrective disclosures" that devalued the stock.

The district court initially certified the class, refusing to consider Goldman's argument that the stock price had not declined when numerous articles had previously disclosed Goldman's practices on the ground that it pertained to materiality. On appeal, the Second Circuit vacated and remanded. It instructed the district court to apply the burden of persuasion (the preponderance of the evidence) standard to defendants' evidence. The Circuit also told the court to consider the additional "price-impact evidence Goldman had sought to introduce" — that the stock price did not decline when the thirty-six news articles allegedly disclosed these conflicts of interest.[11]

On remand, the district court once again certified the class. While Goldman pointed to the release of these news articles and lack of contemporaneous price declines, the court found this evidence did not establish a lack of price impact. The articles did not describe "the nature and extent of Goldman's client conflicts," unlike what was disclosed by the SEC enforcement action.[12]

This time on appeal, the Second Circuit affirmed in a 2-1 vote. The Majority first held that the district court did not abuse its discretion in applying the price maintenance theory, under which the court found that "the inflation maintained by Goldman's statements equaled the price drop caused by the corrective disclosures."[13]

It then rejected Goldman's attempt to shoehorn into class certification the argument that the alleged statements were immaterial as a matter of law. It reasoned that "while securities class action defendants have numerous avenues for challenging materiality," such as at motions to dismiss or summary judgment, "Rule 23 is not one of them."[14]

The Majority then held that the district court "reasonably concluded by a preponderance of the evidence that the corrective disclosures revealed new and material information to the market" and therefore "moved the market in a way that the news reports did not."[15] As it reasoned, "It is difficult to imagine that Goldman's shareholders would have been indifferent had Goldman disclosed its alleged failure to prevent employees from illegally advising clients to buy into CDOs that were built to fail by a hedge fund secretly shorting the investors' positions."[16] Had this information been disclosed to the market, Goldman would have lost business and revenue,

(continued on page 14)

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[10] *Goldman*, 955 F.3d at 258.

[11] *Id.* at 262 (citing *Arkansas Teachers Ret. Sys. v. Goldman Sachs Grp., Inc.*, 879 F.3d 474 (2d Cir. 2018)).

[12] *Id.* at 263 (quoting *In re Goldman Sachs Grp., Inc. Sec. Litig.*, 2018 WL 3854757, at *4 (S.D.N.Y. Aug. 14, 2018)).

[13] *Id.* at 266.

[14] *Id.* at 270.

[15] *Id.*

[16] *Id.* at 272.

U.S. SUPREME COURT TO WEIGH IN ON REBUTTING THE FRAUD ON THE MARKET PRESUMPTION *(continued from page 13)*

and those "adverse consequences have nothing to do with the threat of enforcement actions, and everything to do with how Goldman managed its conflicts of interest."[17]

The dissenter, Judge Sullivan, would have reversed the district court's decision and decertified the class. He criticized the majority for "strain[ing] to avoid looking at the statements themselves for fear that such a review amounts to 'smuggling materiality into Rule 23.'" As he explained, "Candidly, I don't see how a reviewing court can ignore the alleged misrepresentations when assessing price impact."[18]

In Judge Sullivan's view, "[o]nce a defendant has challenged the *Basic* presumption and put forth evidence demonstrating that the misrepresentation did not affect share price, a reviewing court is free to consider the alleged misrepresentations in order to assess their impact on price."[19] Here, "the generic quality of Goldman's alleged misstatements, coupled with lack of price movement 'on any of the 36 dates on which the falsity of the alleged misstatements was revealed to the public,' . . . clearly compels the conclusion that the stock drop following the corrective disclosures was attributable to something other than the misstatements alleged in the complaint."[20]

The Petition for a Writ of Certiorari and the Arguments before the Supreme Court

Goldman's Petition largely embraces Judge Sullivan's dissent. The Petition contends that the Second Circuit's decision provides a "cheap ticket" and "automatic path for securities plaintiffs to obtain class certification," and presents two issues for review.[21] *First*, it asks whether defendants may rebut the *Basic* presumption "by pointing to the generic nature of the alleged misstatements in showing that the statements had no impact on the price of the security, even though that evidence is also relevant to the substantive element of materiality."[22]

The Petition urges the Supreme Court to follow the "framework" purportedly established by *Allstate*, a recent Seventh Circuit decision in which Justice Amy Coney Barrett, then serving as a circuit judge, joined.[23] Goldman contends this case "shows how a court should navigate between the holdings of *Halliburton II*, on one side, and *Amgen* and *Halliburton I*, on the other."[24] Under this framework, while a court must "avoid deciding materiality or loss causation"[25] at class certification, it can consider evidence about the lack of price impact even if that "same evidence is likely to have obvious implications for the off-limits merits issues of materiality and loss causation." Thus, according to Goldman, the Second Circuit erred in failing to consider that the "generic and aspirational statements" at issue were "too general to cause a reasonable investor to rely upon them."[26]

Second, the Petition asks whether a defendant, in rebutting the *Basic* presumption, "has only a burden of production or also the ultimate burden of persuasion."[27] The Second Circuit, like it has in other cases, held that defendants must satisfy the burden of persuasion. Goldman urges the Supreme Court to instead hold that only the burden of production applies to defendants, following the Eighth Circuit's decision in *Best Buy*, and Rule 301 of the Federal Rules of Evidence, which is the default evidentiary rule governing rebutting presumptions.[28]

Although Goldman acknowledges that many courts have rejected this interpretation of *Best Buy* — construing *Best Buy's* language on

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[17] *Id.*

[18] *Id.* at 278 (Sullivan, J. dissenting)

[19] *Id.*

[20] *Id.* at 278-79.

[21] Petition for a Writ of Certiorari at 25, Appeal No. 20-222 (U.S. Aug. 21, 2020) ("Pet.").

[22] Pet. at (I).

[23] *In re Allstate Corp. Securities Litigation*, 966 F.3d 595 (2020).

[24] Pet. at 20.

[25] *Id.* (quoting *Allstate*, 966 F.3d at 608).

[26] *Id.* at 21.

[27] Pet. at (I).

[28] *Id.* at 22 (citing *IBEW Local 98 Pension Fund v. Best Buy Co.*, 818 F.3d 775 (2016)).

burdens as mere dicta — it nonetheless contends *Best Buy* "unambiguously concluded" that defendants need only satisfy the lower of burden of production to show a lack of price impact. According to Goldman, under *Best Buy* and Rule 301, once a defendant "come[s] forward with evidence showing a lack of price impact," it satisfies the burden of production. Plaintiffs must then provide evidence of price impact to carry their burden of persuasion.[29]

In this case, Goldman contends "there can be no doubt that [plaintiffs'] effort to certify the class would have failed if they had borne the ultimate burden of persuasion."[30] Goldman argues that plaintiffs "offered no hard evidence, expert or otherwise," and "made no serious attempt to refute" Goldman's evidence of lack of price impact.[31] According to Goldman, plaintiffs' mere criticisms of defendants' evidence would not have carried the burden of persuasion, and the district court would not have certified the class.

Finally, while the Petition itself does not directly challenge the validity of the "inflation-maintenance theory," it notes it is "a theory that this Court has never even recognized."[32] Goldman contends that the Second Circuit's decision "only encourages reliance" on the price-maintenance theory, which incentivizes "the troubling practice of event-driven securities litigation."[33] Noting that defendants cannot establish a lack of price impact in a price maintenance case by showing that the misrepresentations did not cause an increased price on the front end, Goldman contends that the Second Circuit's decision also "strip[s] defendants of any meaningful 'back end' defense that 'the 'correction' of the alleged misrepresentation did not cause a price decrease." *Id.* at 26.[34] Thus, according to Goldman, defendants should be entitled to "point[] to the generic nature of the alleged misstatements" to show that a price drop on the back end had no connection to such statements.

Plaintiffs, in opposing the certiorari petition, assert that the Second Circuit correctly rejected Goldman's impermissible attempts to argue materiality at class certification. Plaintiffs emphasize that the district court did not disregard any of Goldman's *actual evidence* on price impact out of some fear that it overlapped with evidence on materiality. Instead, "the only 'evidence' the district court refused to consider was Goldman's *legal* assertion that its statements did not satisfy the Second Circuit's standards for materiality."[35] And a "legal argument that a statement is immaterial is not the kind of 'evidence' regarding price impact that *Halliburton II* permits."[36]

Regarding the burden of production and persuasion, Plaintiffs argue that the Eighth Circuit in *Best Buy* did not actually hold that the burden of production applied, as language to that affect was merely dicta. They further contend that *Halliburton II* squarely places the burden of persuasion on defendants.[37] In any event, Plaintiffs posit that the burden issue is insignificant because "the distinction between the burden of proof and production rarely matters in the end" and "is unimportant unless the case is close."[38]

On January 25, 2021, Goldman filed its opening brief, which raises the same issues and largely echoes the argument in its Petition. Goldman posits that at class certification, "a court must consider *all* evidence offered by the defense showing that the alleged misrepresentations did not actually affect the stock price," even if the evidence also bears on materiality or loss causation.[39] Goldman also repeats its argument that the burden of production — not persuasion — applies to defendants in rebutting the *Basic* presumption. Under the burden of production, Goldman asserts that a defendant need only "produce evidence that the alleged misrepresentation did not affect the stock's price"; it does not need to "establish the absence of price impact."[40] Goldman also attacks the price-maintenance theory for "mak[ing] it virtually impossible to rebut the supposedly rebuttable *Basic* presumption."[41]

Conclusion

This will be the fourth time in the past decade the Supreme Court weighs in on certifying securities class actions. While the outcome is uncertain and hard to predict, if the petitioners succeed in the arguments below, the decision could affect how parties litigate class certification in securities cases. ■

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[29] *Id.* at 22-23.

[30] *Id.* at 24.

[31] *Id.* at 23-24.

[32] *Id.* at 26.

[33] *Id.*

[34] *Id.*; Goldman's Reply in support of its Petition further warns that "many securities class actions settle following class certification on the basis of generic and aspirational statements like the ones at issue here." Reply Brief of Petitioners at 8, Appeal No. 20-222 (U.S. Nov. 17, 2020).

[35] Respondents' Brief in Opposition at 18, Appeal No. 20-222 (U.S. Oct. 21, 2020).

[36] *Id.*

[37] *Id.* at 30.

[38] *Id.* at 31.

[39] Petitioners' Opening Brief at 31, Appeal No. 20-222 (U.S. Jan. 25, 2021).

[40] *Id.* at 38.

[41] *Id.* at 34.

THE EASTERN DISTRICT OF VIRGINIA DENIES STATE FARM'S MOTION TO DISMISS BUSINESS INTERRUPTION CLAIMS RESULTING FROM ORDERS SHUTTING DOWN BUSINESSES DUE TO COVID-19 *(continued from page 5)*

fortuitous losses under the "all risk" policies (the "Policies") to protect themselves against losses stemming from unexpected interruptions to business. However, State Farm swiftly and uniformly denied claims. In fact, despite issuing policies and collecting premiums to cover *all risks*, State Farm summarily denied these claims without engaging in any good faith investigation. Thereafter, in May 2020, Kessler Topaz filed breach of contract, breach of the covenant of good faith and fair dealing and declaratory judgment claims (the "Claims") on behalf of Plaintiff and other similarly situated small businesses.

Although State Farm accepted all risks of fortuitous losses not expressly excluded under the Policies, Defendants moved to dismiss Plaintiff's Claims arguing that: (1) although their policy covers "direct physical loss to property," such coverage does not include the loss of use of property but rather requires structural damage; and (2) the Virus Exclusion — an exclusion regarding "growth, proliferation, spread, or presence" of a virus — precluded coverage because the cause of loss was COVID-19. Neither of these arguments was successful.

While no one could have contemplated state and local government orders requiring social distancing, customers staying at home, and/or business closures, State Farm assumed that risk under its *all-risk* Policies. Kessler Topaz, on behalf of the Plaintiff and other small businesses, therefore argued to the Court that State Farm — after millions of small businesses were forced to suspend operations as a result of the Orders — could not rewrite the language of its Policies to both narrow its coverage and broaden exclusions to limit its financial exposure.

With respect to the "direct physical loss to property," State Farm essentially asked the Court to re-write their policy such that coverage would be limited to structural damage to property. But, as Kessler Topaz argued on behalf of Plaintiff, Virginia law is clear that Plaintiff's inability to use its property for its intended use is a direct physical loss. Because Plaintiff was required to shut down its business in compliance with the Orders, Plaintiff suffered a direct physical loss triggering coverage under its Policy.

Kessler Topaz also countered State Farm's application of the Virus Exclusion, arguing that the plain language of the exclusion only barred losses resulting from the growth, spread or proliferation of a virus on Plaintiff's property, and/or the resulting decontamination of Plaintiff's property — none of which occurred here. Indeed, Plaintiff's business closure was unrelated to virus contamination on its property. Rather, the Orders ordered Virginia businesses closed in an attempt to stop the spread of COVID-19.

On December 9, 2020,[2] Judge Raymond Jackson of the Eastern District of Virginia rejected State Farm's bid for dismissal and instead accepted Kessler Topaz's arguments that the plain language of State Farm's Policy provides coverage for business interruption losses stemming from the Orders.

Judge Jackson found that the insurance policy issued by State Farm "covers loss or damage to the covered commercial property resulting from all risks other than those expressly excluded."[3] In considering State Farm's argument that "direct physical loss" requires structural damage to property, the Court set forth a well-reasoned and thorough analysis finding that "if Defendants wanted to limit liability of 'direct physical loss' to strictly require structural damage to property, then Defendants, as the drafters of the policy, were required to do so explicitly."[4]

Judge Jackson continued: "[s]ince Defendants did not explicitly include 'structural damage' in the language, the Policy may be construed in favor of more coverage based on plausible interpretations."[5] Accordingly, the Court rejected State Farm's attempt to retroactively limit its coverage in the wake of the unprecedented business closures precipitated by the spread of COVID-19 throughout Virginia and the United States, finding "it is plausible that Plaintiff [] experienced a direct physical loss when the

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[2] *Elegant Massage, LLC v. State Farm Mut. Auto. Ins. Co.*, 2020 WL 7249624 (E.D.Va. Dec. 9, 2020).

[3] *Id.* at *1.

[4] *Id.* at *9.

[5] *Id.*

property was deemed uninhabitable, inaccessible, and dangerous to use by the Executive Orders because of its high risk for spreading COVID-19, an invisible but highly lethal virus."[6]

The Court further rejected State Farm's efforts to invoke various exclusions in the Policy. Specifically, the Court rejected State Farm's argument that an exclusion regarding "growth, proliferation, spread, or presence" of a virus excluded coverage for losses incurred due to the Orders issued in connection with COVID-19. The Court found that, based on the plain language of the Virus Exclusion, the exclusion "applies where a virus has spread throughout the property[]"[7] and therefore "in applying the Virus Exclusion there must be a direct connection between the exclusion and the claimed loss and not, as the Defendants argue, a tenuous connection anywhere in the chain of causation."[8] Accordingly, because Plaintiff did not allege that a virus was present on its property or that a virus caused direct physical loss to its property, the Court found that State Farm "failed to meet its burden to show that the Virus Exclusion applies to Plaintiff's claim."[9]

Regarding State Farm's additional arguments, the Court similarly rejected attempts to shoehorn Plaintiff's claim into circumstances where coverage is excluded due to the *enforcement* of laws or ordinances regulating the use of property. The Court found that the Orders "which were temporary restrictions that impacted the Plaintiff's business, were not ordinances or laws such as safety regulations or laws passed by a legislative body regulating the construction, use, repair, removal of debris, or physical aspects of the property[]"[10] and therefore the policy's ordinance or law exclusion was inapplicable. Finally, the Court declined to enforce an "acts or decisions" policy exclusion, which State Farm attempted to apply in order to deny coverage any time anyone makes any act or decision, finding that such an application would "leave the insurance policy practically worthless."[11]

Judge Jackson's opinion is one of a handful of opinions finding in favor of insureds nationwide. After overcoming this initial roadblock and successfully defeating State Farm's improper attempt to re-write its Policy in order to deny coverage under the unprecedented circumstances caused by COVID-19, Kessler Topaz will continue to work to bring relief to these small businesses. In the coming months, Kessler Topaz will engage in discovery, seek to certify a class of businesses insured under State Farm's "all risk" policies, and work to obtain recoveries.

This crucial litigation is necessary to make Plaintiff and other businesses whole after they were forced to suspend operations as a result of the Orders, and have faced significant financial hardship due to the COVID-19 pandemic and State Farm's wrongfully denial of insurance coverage. ■

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[6] *Id.* at *10.

[7] *Id.* at *12.

[8] *Id.*

[9] *Id.* at *13.

[10] *Id.*

[11] *Id.*

REVISIONS TO CHINESE SECURITIES LAWS INCLUDE MORE ROBUST DISCLOSURE REQUIREMENTS AND A MECHANISM FOR REPRESENTATIVE OPT-OUT SHAREHOLDER LITIGATION *(continued from page 5)*

"ordinary investors" and "professional investors." For example, in a dispute between a company and an "ordinary investor," the burden of proof is shifted to the company. Additionally, where an "ordinary investor" submits a request for settlement, the company may not refuse such a request.

Chapter VI also contains provisions that both create new and improve existing mechanisms for investors to seek compensation for losses they suffer due to fraudulent issuances, fraudulent misrepresentations, or other illegal acts. A newly added mechanism for distributing compensation allows the controlling shareholder, actual controller of the issuer, or the relevant company to entrust an investor protection institution (which is an institution established in accordance with the laws and administrative regulations of the securities regulators) to enter into an agreement for compensation with investors who suffer losses and make that compensation to investors in advance. When the company makes advance compensation, it may then seek recourse against other parties that may be held jointly liable under the law.

Improvements made to the securities litigation mechanisms now allow for representative opt-out class actions. There appear to be two types of representative actions that are envisioned in the new law. First, when there is an allegation of fraudulent misrepresentations, insider trading, or market manipulation and there are multiple plaintiff investors who have claims against a company for losses stemming from the same subject matter, the investors may elect a representative to proceed with litigation against the company or wrongdoer. During the course of those proceedings, the court may issue a notice with details of the litigation to those investors who may also be affected but who have not yet joined in the litigation and invite them to register their claims with the court within a set period of time. The decision will bind all investors who participated in the action.

The law also provides for "special representative litigation" that includes a role for investor protection organizations (which, as noted above, are established in accordance with Chinese law and regulations). Under this mechanism, an investor protection institutions may participate in litigation as the representative of investors and, provided they reach at least 50 investors, to register all affected investors with the court once the investors' information has been verified by the securities registration and clearing institutions.

This new special representative litigation process is envisioned as an "opt-out" process. Both the representative litigation process and the special representative litigation process were further clarified by regulations issued by the Shanghai Financial Court on March 24, 2020, the *Regulations of the Shanghai Financial Court on the Securities Dispute Litigation Mechanism (Trial)* ("Financial Court Regulations") and by the Chinese Supreme Court on July 23, 2020, the *Regulations of the Supreme People's Court on Several Issues about Securities Dispute Representative Litigation* ("The Supreme Court Regulations). In representative litigation, the Financial Court Regulations specify processes for case registration, representative appointment, rights of the representative, the trial, court judgment and enforcement.The Financial Court Regulations also provided clarity on the requirements for special representative litigation and outlined methods for collecting the names of affected investors and the "opt-out" procedures to be used. The Supreme Court Regulations further provide the pre-conditions for starting a case, how to determine the plaintiffs and the representative, case procedures, and the allocation of litigation cost. The Supreme Court Regulations also provide that plaintiffs in special representative litigation do not need to pay court fees upfront, allow courts to waive the requirement for a security deposit from the plaintiffs (if requested by the investor protection organization to do so),and clarify how the court will deal with situations where an investor protection institution does not reach 50 investors or if there are multiple investor protection organizations involved.

While the representative litigation mechanisms have now been in place for almost a year, it does not appear that any significant shareholder litigation has yet been filed. It may, however, only be a matter of time and it will be interesting to watch and see what develops in China. ■

WHAT'S TO COME

MARCH 2021

Council of Institutional Investors (CII) 2021 Spring Conference

March 8 – March 10
(Virtual)

MAY 2021

State Association of County Retirement Systems (SACRS) Spring Conference

May 11 – May 14
Long Beach, CA

Texas Association of Public Employee Retirement Systems (TEXPERS) Annual Conference

May 23 – May 26
Austin Marriott Downtown ■ Austin, TX

Pennsylvania Association of Public Employee Retirement Systems (PAPERS) Spring Forum

May 25 – May 26
(Virtual)

JUNE 2021

Florida Public Pensions Trustees Association (FPPTA) 37th Annual Conference

June 27 – June 30
Renaissance Orlando at SeaWorld ■ Orlando, FL

National Association of Public Pension Attorneys (NAPPA) Legal Education Conference

June 22 – June 25
Hilton Denver City Center ■ Denver, CO

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