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2020 Directors and Officers Case Law Update

Annual summary and review of Directors and Officers (D&O) Case Law

Special Section on COVID-19 for 2020

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2020 Directors and Officers Case Law Update
By Aaron M. Simon[1]

1) Basic Corporate Structure Overview

Directors and Officers run a company so it is helpful to start an analysis of Directors and Officers Case Law with review of basic corporate structure.

What is a corporation?

A corporation is a legal entity that is separate and distinct from its owners. Corporations enjoy most of the rights and responsibilities that individuals possess: they can enter contracts, loan and borrow money, sue and be sued, hire employees, own assets, and pay taxes.

How is a corporation managed and run?

A corporation is managed and run by its directors and officers.

Officers are usually appointed by the corporation's board.

Common corporate officers include:

Chief Executive Officer (CEO) or President. The CEO has the ultimate responsibility for the corporation's activities, and signs off on contracts and other legally-binding action on behalf of the corporation. The CEO reports to the corporation's board of directors.

Chief Operating Officer (COO). Charged with managing the corporation's day-to-day affairs, the COO typically reports directly to the CEO.

Chief Financial Officer (CFO) or Treasurer. The CFO is responsible for a corporation's financial matters.

Secretary. The corporation's Secretary is in charge of maintaining and keeping a corporation's records, documents, and minutes from shareholder meetings.

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Shareholders. A corporation's shareholders have an ownership interest in the company by having money invested in the corporation. A "share" is an apportioned ownership interest in the corporation.

Corporations typically hold annual shareholder meetings. At these annual shareholder meetings the shareholders will elect the corporation's directors. Special shareholder meetings may also be held.

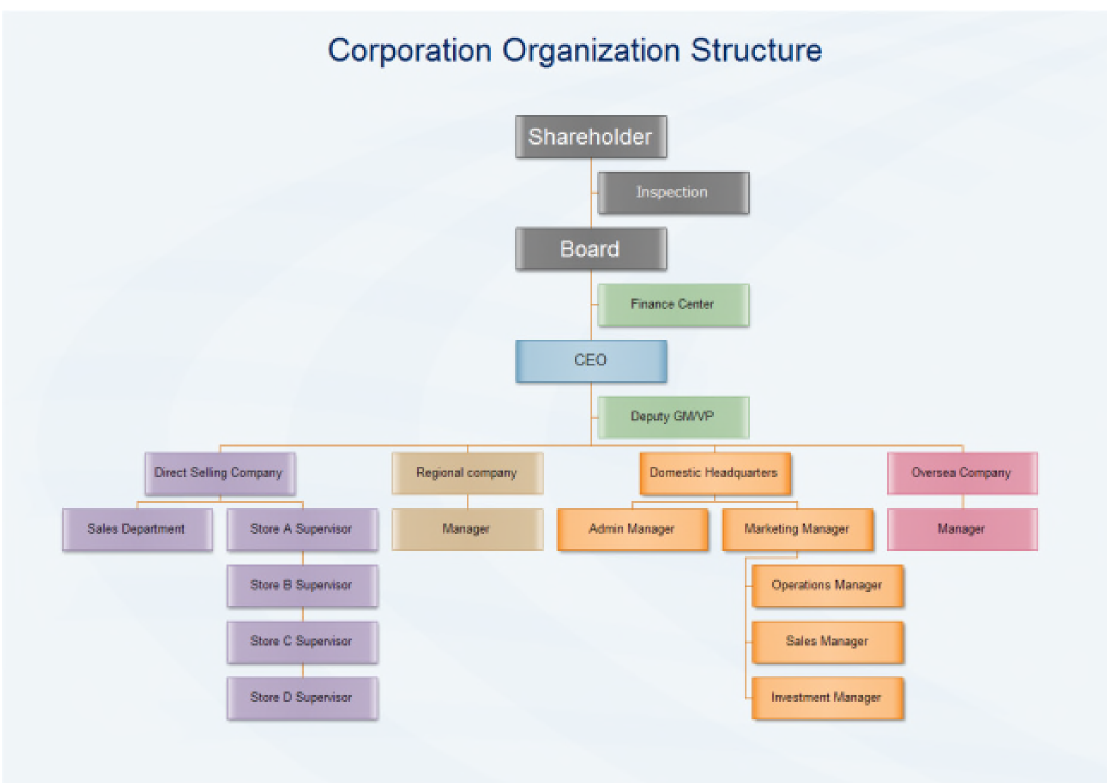
A corporation's articles of incorporation (combined with certain laws addressing shareholder rights) set forth shareholder voting rights and procedures.

Board of Directors. The Board of Directors is the entity that ultimately controls and governs a corporation on behalf of the shareholders. The Board of Directors of a corporation manages the corporation's business and has the authority to exercise all of the corporation's powers.

Generally, the board of directors is responsible for making major business and policy decisions and the officers are responsible for carrying out the board's policies and for making the day-to-day decisions.

The number of directors a corporation will have, or a minimum and maximum number of directors that the corporation may have, are set forth in the articles of incorporation or bylaws of the corporation.

Typical Corporation Organizational Chart:



Credit: https://www.edrawsoft.com/template-corporation-organization-structure.php

2) Directors' and Offices Standard of Care - In General

Typical state statutes governing the standard of care of directors (and officers) usually state something to the effect that a director is generally not liable for any action taken as a director, or any failure to take any action, if the director performed the duties of his or her office in compliance with the statutory standard of conduct or in compliance with his or her fiduciary duties.

See for example Minn. Stat. Ann. § 302A.251, the Minnesota Statute governing the standard of care for directors:

> Subdivision 1. Standard; liability. A director shall discharge the duties of the position of director in good faith, in a manner the director reasonably believes to be in the best interests of the corporation, and with the care an ordinarily prudent person in a like position would exercise under similar circumstances. A person who so performs those duties is not liable by reason of being or having been a director of the corporation.
>
> Subd. 2. Reliance. (a) A director is entitled to rely on information, opinions, reports, or statements, including financial statements and other financial data, in each case prepared or presented by:
>
> > (1) one or more officers or employees of the corporation whom the director reasonably believes to be reliable and competent in the matters presented;
> >
> > (2) counsel, public accountants, or other persons as to matters that the director reasonably believes are within the person's professional or expert competence; or
> >
> > (3) a committee of the board upon which the director does not serve, duly established in accordance with section 302A.241, as to matters within its designated authority, if the director reasonably believes the committee to merit confidence.
> >
> > (b) Paragraph (a) does not apply to a director who has knowledge concerning the matter in question that makes the reliance otherwise permitted by paragraph (a) unwarranted.
>
> Subd. 3. Presumption of assent; dissent. A director who is present at a meeting of the board when an action is approved by the affirmative vote of a majority of the directors present is presumed to have assented to the action approved, unless the director:
>
> > (a) objects at the beginning of the meeting to the transaction of business because the meeting is not lawfully called or convened and does not participate thereafter in the meeting, in which case the director shall not be considered to be present at the meeting for any purpose of this chapter;
> >
> > (b) votes against the action at the meeting; or

> (c) is prohibited by section 302A.255 from voting on the action.

Subd. 4. Elimination or limitation of liability. A director's personal liability to the corporation or its shareholders for monetary damages for breach of fiduciary duty as a director may be eliminated or limited in the articles. The articles shall not eliminate or limit the liability of a director:

> (a) for any breach of the director's duty of loyalty to the corporation or its shareholders;
>
> (b) for acts or omissions not in good faith or that involve intentional misconduct or a knowing violation of law;
>
> (c) under section 302A.559 or 80A.76;
>
> (d) for any transaction from which the director derived an improper personal benefit; or
>
> (e) for any act or omission occurring prior to the date when the provision in the articles eliminating or limiting liability becomes effective.

Subd. 5. Considerations. In discharging the duties of the position of director, a director may, in considering the best interests of the corporation, consider the interests of the corporation's employees, customers, suppliers, and creditors, the economy of the state and nation, community and societal considerations, and the long-term as well as short-term interests of the corporation and its shareholders including the possibility that these interests may be best served by the continued independence of the corporation.

See also Va. Code Ann. § 13.1-690:

A. A director shall discharge his duties as a director, including his duties as a member of a committee, in accordance with his good faith business judgment of the best interests of the corporation.

B. Unless a director has knowledge or information concerning the matter in question that makes reliance unwarranted, the director is entitled to rely on information, opinions, reports, or statements, including financial statements and other financial data, if prepared or presented by:

1. One or more officers or employees of the corporation whom the director believes, in good faith, to be reliable and competent in the matters presented;

2. Legal counsel, public accountants, or other persons as to matters the director believes, in good faith, are within the person's professional or expert competence; or

> 3. A committee of the board of directors of which he is not a member if the director believes, in good faith, that the committee merits confidence.
>
> C. A director is not liable for any action taken as a director, or any failure to take any action, if he performed the duties of his office in compliance with this section.
>
> D. A person alleging a violation of this section has the burden of proving the violation.

See also Bos. Children's Heart Found. v. Nadal-Ginard, 73 F.3d 429 (1st Cir. 1996) which states:

> The basic standard of care of corporate officers or directors is well-established under Massachusetts law. In essence, it is the "standard of complete good faith plus the exercise of reasonable intelligence." *Murphy v. Hanlon*, 322 Mass. 683, 79 N.E.2d 292, 293 (Mass. 1948). Under this standard, officers or directors are not responsible for mere errors of judgment or want of prudence in the performance of their duties. *See Sagalyn v. Meekins, Packard & Wheat, Inc.*, 290 Mass. 434, 195 N.E. 769, 771 (Mass. 1935). Further, if officers or directors act in good faith, albeit imprudently, they are not subject to personal liability absent clear and gross negligence in their conduct. *See Spiegel v. Beacon Participations, Inc.*, 297 Mass. 398, 8 N.E.2d 895, 904 (Mass. 1937).

However, a director who does not act within the statutory standard or who breaches his or her fiduciary duties can be held liable, to the corporation, for the damages those actions caused.

See also Francis v. United Jersey Bank, 87 N.J. 15, 36, 432 A.2d 814, 824 (1981) stating:

> [A] director's duty of care does not exist in the abstract, but must be considered in relation to specific obligees. In general, the relationship of a corporate director to the corporation and its stockholders is that of a fiduciary. *Whitfield v. Kern*, 122 N.J.Eq. 332, 341 (E. & A. 1937). Shareholders have a right to expect that directors will exercise reasonable supervision and control over the policies and practices of a corporation. The institutional integrity of a corporation depends upon the proper discharge by directors of those duties.

See also In re James River Coal Co., 360 B.R. 139, 154–55 (Bankr. E.D. Va. 2007) (footnote and citations omitted):

> The local law of the state of incorporation will be applied to determine the existence and extent of a director's or officer's liability to the corporation, its creditors and stockholders, except where, with respect to the particular issue, some other state has a more significant relationship under the principles stated in Section 6 [of the Restatement (Second) of Conflict of Laws] to the parties and the transaction, in which event the local law of the other state will be applied.

In addition, typically under state statues governing directors, a director who votes for a dividend, distribution, or stock purchase made in violation of law or the articles of incorporation, is liable, with all other directors, to the corporation for the amount of the payment that exceeds what could have been paid without violating the law or the articles. *See e.g.* Ohio Rev. Code Ann. § 1701.95 and Del. Code Ann. tit. 8, § 174.

Corporations may eliminate or limit their directors' liability for a breach of fiduciary duty by so providing in their articles of incorporation. However, in general, they cannot eliminate or limit liability for a breach of the duty of loyalty, for acts made in bad faith or which involve intentional misconduct or a knowing violation of law, for approving unlawful dividends, distributions or stock purchases, or for any transaction in which the director derived an improper personal benefit.

When analyzing the standard of care for directors one must look to the applicable jurisdiction's statute governing standard of care for directors. This is because the statutory standards of care for directors and officers can differ from state to state, and the differences can have different results for officers who might live up to the standard of care in one jurisdiction, but fall short in another.

See also FDIC v. Dee, 222 F. Supp. 3d 972, 1001 (D.N.M. 2016):

> The FDIC argued that § 53-11-35(B) provides directors' standard of care and the business judgment rule provides officers' standard of care. The FDIC explained that §§ 8.30 and 8.31 of the Model Business Corporation Act dictate such a conclusion. The FDIC explained that, in 1998, the Model Business Corporation Act ("MBCA") separated § 8.30 – "which is the standard of conduct" -- from § 8.31 – "which is the standard of liability." The FDIC asserted that § 8.31 codifies the business judgment rule. The FDIC stated that, before 1998, all that existed was § 8.30, and "the New Mexico statute that's in place here essentially mirrors what the original § 8.30 was" -- in other words, New Mexico never adopted § 8.31. In the FDIC's view, if it brought a case in a jurisdiction that has adopted § 8.31, it would have to plead that a director did not have a reasonable basis for making his decision. According to the FDIC, because New Mexico has not adopted § 8.31, it needs to allege only facts indicating that the directors were negligent and that the officers lacked a reasonable basis for their actions.

Also corporate officers and directors may also be subject to liability for violations of the extensive anti-fraud and disclosure requirements of the federal securities laws - particularly the Securities Act of 1933 and the Securities Exchange Act of 1934.[2]

See also In re MF Glob. Holdings Ltd., 507 B.R. 808, 810-11 (S.D.N.Y. 2014):

> In general, under Delaware law, directors and officers owe fiduciary duties of care to their corporation. *See Gantler v. Stephens,* 965 A.2d 695, 708–09 (Del.2009).
>
> Defendants argue that in this case, the business judgment rule protects them from liability. Delaware law "presumes that in making a business decision the directors

[2] This case law update is not an in-depth overview of securities law and thus will not address these issues.

> of a corporation acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company." *In re Walt Disney Co. Deriv. Litig.,* 906 A.2d 27, 52 (Del.2006) (internal quotation marks omitted). A plaintiff can overcome this presumption if the directors' conduct was grossly negligent. *See Brehm v. Eisner,* 746 A.2d 244, 259 (Del.2000).
>
> * * *
>
> Directors and officers of a Delaware corporation owe a duty of loyalty to the corporation. *See Gantler,* 965 A.2d at 708–09. The duty of loyalty requires an officer or director to (1) avoid fiduciary conflicts of interest and (2) act in good faith for the corporation's best interest. *See Stone ex rel. AmSouth Bancorporation v. Ritter,* 911 A.2d 362, 370 (Del.2006). Bad faith encompasses circumstances when the director or officer does not act "with an honesty of purpose and in the best interest and welfare of the corporation." *In re Walt Disney Co. Derivative Litig.,* 907 A.2d 693, 755 (Del.Ch.2005), *aff'd,* 906 A.2d 27 (Del.2006).

In summary corporate directors and officers must discharge their duties in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances, and in a manner they reasonably believe to be in the best interests of the corporation. Officers also owe duties of fidelity, honesty, good faith, and fair dealing to the corporation. An officer will not be liable for any action taken as an officer, or any failure to take any action, if the officer performed his or her duties in compliance with these standards.

3) Directors and Officers and COVID-19 Liability Exposure

Recent suits against Directors and Officers involving COVID-19 have typically been for violations of the Securities Exchange Act of 1934 ("SEA"), typically section 10(b).

> *The SEA was created to govern securities transactions on the secondary market, after issue, ensuring greater financial transparency and accuracy and less fraud or manipulation. The SEA authorized the formation of the Securities and Exchange Commission (SEC), the regulatory arm of the SEA. The SEC has the power to oversee securities—stocks, bonds, and over-the-counter securities—as well as markets and the conduct of financial professionals, including brokers, dealers, and investment advisors. It also monitors the financial reports that publicly traded companies are required to disclose.*[3]

In fact, "[a]t least 50 federal securities cases with references to COVID-19 have been filed in the past three months, including merger challenges, regulatory enforcement actions and sprawling investor suits.." https://www.law360.com/articles/1278091 by Dean Seal, May 29, 2020.

Most of these types of cases involve stocks rising and then falling in a short period of time due to allegedly false or misleading statements made by officers, particularly in press releases and form 10-Ks. Some, were (allegedly) outright lies and fabrications made by officers, such as in *Praxsyn*,

[3] https://www.investopedia.com/terms/s/seact1934.asp by Will Kenton, updated May 15, 2020.

SCWorx and *Sorrento*; Some cases involved allegations of officers knowing more information than was released, such as in *Zoom*, *Carnival* and *Norwegian*[4], where the allegedly misleading statements were more subtle. Generally speaking, "honesty is the best policy", and if Directors and Officers want to attempt to shield themselves from COVID-19 related liability, their best course of action is to admit what they know, admit what they don't know, and avoid false and/or misleading statements in press releases and in 10-Ks.

A good summary of the types of COVID-19 related D&O lawsuits comes from Kevin M. Lacroix's D&O Diary website:

> As we enter the fifth month of the coronavirus outbreak in the U.S., the COVID-19-related D&O claims continue to accumulate. There have now been a total of 16 COVID-19-related securities class action lawsuits filed. The lawsuits filed so far fall into three basic categories: (1) cases involving companies that experienced COVID-19 in their facilities (such as the lawsuits against cruise lines Carnival Corporation and Norwegian Cruise Lines and private prison operator The Geo Group); (2) cases involving companies that are alleged to have made misrepresentations about the company's ability to gain from the pandemic (such as lawsuits against diagnostic testing company Co-Diagnostics and vaccine maker Inovio); and (3) cases involving companies that have experienced financial issues or operating disruptions as a result of the pandemic (such as the lawsuit against Elanco Animal Health and Colony Capital). There are a couple of cases that do not fall into one of these three categories, such as the PPP-related lawsuit filed against Wells Fargo, and the privacy-related lawsuit filed against Zoom.

Source:https://www.dandodiary.com/2020/07/articles/coronavirus/covid-19-and-do-insurance-july-update/

Timeline of Specific COVID-19 Related D&O Class Action Cases

1. March 12, 2020: *Douglas v. Norwegian Cruise Lines*, 20-cv-21107 (S.D. Fla.)

2. March 12, 2020: *McDermid v. Inovio Pharmaceuticals, Inc.*, 20-cv-01402 (E.D. Pa.)

3. April 7, 2020: *Drieu v. Zoom Video Communications, Inc.*, 20-cv-02353 (N.D. Cal.)

4. April 15, 2020: *Riback v. iAnthusCapital*, 20-cv-03044 (S.D.N.Y.)

5. April 24, 2020: *Wandel v. Phoenix Tree Holdings, Ltd.*, 20-cv-03259 (S.D.N.Y.)

6. April 29, 2020: *Yannes v. SCWorx Corp.*, 20-cv-03349 (S.D.N.Y.)

7. May 20, 2020: *Hunter v. Elanco Animal Hospital, Inc.*, 20-cv-1460 (S.D.Ind.)

8. May 26, 2020: *Wasa Medical Holdings v. Sorrento Therapeutics, Inc.*, 20-cv-00966 (S.D. Cal.)

[4] See in depth discussion of these cases below.

9. May 26, 2020: *Swartzenruber v. Colony Capital, Inc.,* 20-cv-4673 (C.D. Cal.)

10. May 27, 2020: *Service Lamp Corp. Profit Sharing Plan v. Carnival Corporation*, 20-cv-22202 (S.D. Fla.)

11. June 10, 2020: *Guafeng Ma v. Wells Fargo & Company*, 20-cv-3697 (N.D. Cal.)

12. June 10, 2020: *The Arbitrage Fund, et al. v. Forescout Technologies, Inc*., et al., 20-cv-03819 (N.D. Cal.)

13. June 15, 2020: *Gelt Trading v. Co-Daignostics, Inc.,* 20-cv-00368 (D. Utah)

14. June 16, 2020: *Cherynysh v. Chembio Diagnostics, Inc.*, 20-cv-2706 (E.D.N.Y.)

15. June 20, 2020: *Lucas v. United States Oil Fund, L.P.*, 20-cv-4740 (E.D.N.Y.)

16. July 7, 2020: *Steve Hartel, et al. v. The GEO Group, Inc., et al.*, 20-cv-81063, (S.D. Fla.)

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***Douglas v. Norwegian Cruise Lines,* 20-cv-21107 (S.D. Fla.) - March 12, 2020 - Cruise Ship case – Claims of failure to disclose knowledge and false or misleading statements of COVID-19 exposure and risks**

Intro: This is a federal securities class action on behalf of a class consisting of all persons and entities other than Defendants who purchased or otherwise acquired the publicly traded securities of Norwegian from February 20, 2020 through March 12, 2020 In order to inflate the prices of the company's securities, the defendants made materially false and misleading statements by failing to disclose that the Company was employing sales tactics of providing customers with unproven and/or blatantly false statements about COVID-19 to entice customers to purchase cruises, thus endangering the lives of both their customers and crew members, causing the plaintiff and other members of the class to suffer financial damages

Date: March 12th, 2020

Court: United States District Court Southern District of Florida

Plaintiff: Eric Douglas and Others similarly situated

Defendants:

Norwegian Cruise Lines

Defendant Frank J. Del Rio ("Del Rio") has served as the Company's Director, President, and Chief Executive Officer ("CEO") throughout the Class Period.

Defendant Mark A. Kempa ("Kempa") has served as the Company's Executive Vice President and Chief Financial Officer ("CFO") throughout the Class Period.

Background and Timeline:

On August 1, 2017, the Company updated its Code of Ethical Business Conduct which is posted to the Company's website. The Code of Ethical Business Conduct, available throughout the Class Period, discussed health and safety standards, stating in relevant part: NCLH and its team members are expected to conduct business in compliance with applicable environmental, health and safety ("EHS") laws and regulations. *NCLH's EHS programs are designed to ensure the preservation of the environment, and safety and security of NCLH's guests, team members and vendors*

On February 20, 2020, the Company filed a Form 8-K with the SEC. Attached to the Form 8-K was a press release reporting on the Company's financial results for the quarter and full year ended December 31, 2019. In that press release, Defendants discussed positive outlooks for the Company in spite of the COVID-19 outbreak stating, " *Despite the current known impact from the COVID-19 coronavirus outbreak, as of the week ending February 14, 2020, the Company's booked position remained ahead of prior year and at higher prices on a comparable basis… our Company has an exemplary track record of demonstrating its resilience in challenging environments and we remain confident in our ability to deliver strong financial performance over the long-term*"

The Company also described the procedures they had in place to protect its guests and crew. In pertinent part, the press release stated: "The Company has proactively implemented *several preventative measures to reduce potential exposure and transmission of COVID-19 and to protect the health, safety, security and well-being of its guests and crew.* These measures include enhanced pre-boarding and onboard health protocols that go above and beyond standard operating procedures."

On February 27, 2020, the Company filed its Form 10-K with the SEC for the year ending December 31, 2019. The 2019 10-K discussed the Company's focus on health and safety of the guests and crew and stated that customer safety was of the utmost priority and taken very seriously, with above industry standard levels in place to ensure customer safety.

On March 11, 2020, *Miami New Times* reported in the article "Leaked Emails: Norwegian Pressures Sales Team to Mislead Potential Customers About Coronavirus" that leaked emails from a Norwegian employee showed that the Company directed its sales staff to lie to customers regarding COVID-19. The article contained a script used by agents to ensure customers that there was nothing to fear, that corona could not survive in warm temperatures, etc.

Additionally, the *Miami New Times* article revealed the financial impact the COVID-19 outbreak was causing on the Company and its employees, quoting an employee stating that "sales are at all-time lows". On this news, the Company's shares fell $5.47 per share or approximately 26.7% to close at $15.03 per share on March 11, 2020, damaging investors.

On March 12, 2020, the *Washington Post* published the article, "Norwegian Cruise Line managers urged salespeople to spread falsehoods about coronavirus", detailing how employees were directed to ensure customers that they would be safe from Corona. On this news, the Company's shares fell a further $5.38 or approximately 35.8% to close at $9.65 on March 12, 2020, further damaging investors.

The Complaint:

In the 2019 10-K Norwegian stated that safety was its highest priority and that it would keep its customers safe. Additionally, under direction from executives, Norwegian sales agents disseminated false information to keep sales up, endangering customers. As a result of the false information, Norwegian's share price was artificially inflated.

Statutory Violations:

Sections 10(b) and 20(a) of the Exchange Act of 1934 and Rule 10b-5 under the SEC (17 C.F.R § 240.10b-5).

McDermid v. Inovio Pharmaceuticals, Inc.**, 20-cv-01402 (E.D. Pa.) - March 12, 2020 – Claims of false representations by company that it had developed a vaccine for COVID-19**

The *Inovio Pharmaceuticals* securities class action lawsuit alleges that during the Class Period, defendants capitalized on widespread COVID-19 fears by **falsely claiming that Inovio had developed a vaccine for COVID-19**. First, on February 14, 2020, defendant Kim appeared on *Fox Business News* and stated that Inovio had developed a COVID-19 vaccine "in a matter of about three hours once we had the DNA sequence from the virus," and that "our goal is to start phase one human testing in the U.S. early this summer." Two weeks later, following a well-publicized March 2, 2020 meeting with President Trump to discuss the COVID-19 outbreak, defendant Kim again claimed that Inovio had developed a COVID-19 vaccine. As a result of defendants' misrepresentations, the price of Inovio common stock was artificially inflated to more than $19 per share during the Class Period.

However, in truth, Inovio had not developed a COVID-19 vaccine. On March 9, 2020, before trading commenced, Citron Research exposed defendants' misstatements, calling for an SEC investigation into the Company's "ludicrous and dangerous claim that they designed a [COVID-19] vaccine in 3 hours." In response to the news, Inovio's stock price plummeted from its March 9, 2020 opening price of **$18.72** per share to close at **$9.83** per share. The following day, March 10, 2020, Inovio's stock price fell from its **$9.30** per share opening price to close at **$5.70** per share. **The two-day price drop wiped out approximately $643 million of Inovio's market capitalization and marked a 70% decline from the stock's Class Period intra-day high**. In a message to shareholders that same day, Inovio attempted to blunt the impact of the Citron revelations but only highlighted its own misstatements, admitting that it had not developed a COVID-19 vaccine, but rather, had merely "designed a vaccine construct" – *i.e.*, a precursor for a vaccine – and that it believed it had a "viable approach to address the COVID-19 outbreak."

On April 27, 2020, Citron published a report calling Inovio **"[t]he COVID-19 Version of Theranos"** and setting a target price of $1. The Citron report set forth, among other things, that "[i]t's been over **40 years since Inovio was founded, yet the company has NEVER brought a product to market**, **and all the while insiders have enriched themselves with hefty salaries and large stock sales**." The Citron report also purports to detail "why Inovio shareholders have been 'Theranosed,'" a reference to the ill-fated health technology company whose founder was indicted for wire fraud and conspiracy after claims of Theranos' supposedly breakthrough blood test technology proved to be false. The Citron report went on to note that "[m]uch like Theranos, Inovio claims to have a 'secret sauce' that, miraculously, no pharma giant has been able to figure out. This is the same 'secret sauce' that supposedly developed a vaccine for COVID-19 in just 3 hours." Citron concluded that "[a]t every opportunity, Inovio is guilty of issuing highly misleading information to pump the company's stock price in response to the latest outbreak. In the case of COVID-19, they are taking advantage of retail investors while they're stuck in quarantine."

https://www.businesswire.com/news/home/20200504005062/en/Notice-Lead-Plaintiff-Deadline-Shareholders-Inovio-Pharmaceuticals

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***Drieu v. Zoom Video Communications, Inc.*, 20-cv-02353 (N.D. Cal.) - April 7, 2020 – Claims of failure to disclose alleged issues with Zoom's privacy and security settings**

Intro: This is a federal securities class action on behalf of a class consisting of all persons who purchased Zoom securities between April 18, 2019 and April 6, 2020. The class is seeking to recover based on Defendants' violations of the federal securities laws involving false and misleading statements about the safety and security of Zoom, resulting in an artificially inflated share price, damaging the plaintiffs.

Date: April 7, 2020

Court: United States District Court California Northern District

Plaintiff: Michael Drieu and others similarly situated

Defendants:

Zoom Video Technologies

Eric S. Yuan, Zoom's President and Chief Executive Officer.

Kelly Steckelberg, Zoom's Chief Financial Officer.

Background and Timeline:

On April 18, 2019, Zoom filed a prospectus on Form 424B4 with the SEC in connection with its IPO, which purported to provide information necessary for investors to consider before partaking in its IPO and purchasing the Company's newly publicly-issued stock. In the Offering Documents, Defendants touted that Zoom's "unique technology and infrastructure enable [inter alia] best-inclass reliability," and that Zoom "offer[s] robust security capabilities, including end-to-end encryption, secure login, administrative controls and role-based access controls"

The Offering Documents also noted that the Company's "security measures have on occasion, in the past, been, and may in the future be, compromised"; that "[c]onsequently, our products and services may be perceived as not being secure," which "may result in customers and hosts curtailing or ceasing their use of our products, our incurring significant liabilities and our business being harmed"; and that "actual or perceived failure to comply with privacy, data protection and information security laws, regulations, and obligations could harm our business." Plainly, the foregoing risk warnings were generic "catchall" provisions that were not tailored to Zoom's actual known risks concerning weaknesses in its cybersecurity and data protection systems

That same day, Zoom conducted its IPO and began trading publicly on the Nasdaq Global Select Market ("NASDAQ") under the ticker symbol "ZM." Pursuant to Zoom's IPO, the Company sold 9.91 million of the Company's shares to the public at the offering price of $36.00 per share

In June 7, 2019, Zoom filed its first Quarterly Report on Form 10-Q with the SEC following its IPO, reporting the Company's financial and operating results for the quarter ended April 30, 2019. The report contained substantively the same information as the offering documents describing the way Zoom interacts with various operating systems and third-party applications, the trust its platform builds with customers and users, and the Company's efforts relating to privacy, data protection and information security; and providing generic "catch-all" provisions that were not tailored to Zoom's actual known risks concerning weaknesses in its cybersecurity and data protection systems.

The truth about the deficiencies in Zoom's software encryption began to come to light as early as July 2019. In July 8, 2019, during intraday trading hours, security researcher Jonathan Leitschuh linked an article published by him that day to his Twitter account, which allegedly exposed a flaw allowing hackers to take over Zoom webcams. According to the article,"[a] vulnerability in the Mac Zoom Client allows any malicious website to enable your camera without your permission," and "[t]he flaw potentially exposes up to 750,000 companies around ahe world that use Zoom to conduct day-to-day business

On this news, Zoom's stock price fell $1.12 per share, or 1.22%, to close at $90.76 per share on July 8, 2019.

On July 11, 2019, public interest research center the Electronic Privacy Information Center filed a complaint against Zoom before the U.S. Federal Trade Commission, alleging that the Company "placed at risk the privacy and security of the users of its services". On this news, Zoom's stock fell $1.32 per share, or 1.42%, to close at $91.40 per share on July 11, 2019.

On March 20, 2020, six days before the truth fully emerged regarding Zoom's deficient security and privacy systems, Zoom filed its first Annual Report on Form 10-K with the SEC since its IPO, reporting the Company's financial and operating results for the quarter and yearended January 31, 2020. As with the Offering Documents, the 2020 10-K stated that Zoom's "unique technology and infrastructure enable best-in-class reliability".

The 2020 10-K also states that the Company's Zoom Video Webinars feature "easily integrates with Facebook Live . . . providing access to large bases of viewers," without disclosing how integration with Facebook could implicate users' personal data, if at all or how the Company employed SDKs to partner with other digital platforms and app providers, the trust its platform builds with customers and users, the Company's efforts relating to privacy, data protection and information security, the lack of any legal proceedings likely to have a material adverse effect on the Company's business, operating results, cash flows or financial condition; providing generic "catch-all" provisions that were not tailored to Zoom's actual known risks concerning weaknesses in its cybersecurity and data protection systems; and containing SOX certifications signed by the Individual Defendants attesting to the accuracy and reliability of the financial report those certifications were appended to as an exhibit.

On March 26, 2020 Vice Media reported the security issues and that Zoom was sending consumer data to Facebook.

On March 27, 2020, Zoom issued a statement by Defendant Yuan, disclosing "a change that [Defendants] have made regarding the use of Facebook's SDK" after being "made aware on Wednesday, March 25, 2020, that the Facebook SDK was collecting device information unnecessary for us to provide our services."

Yuan also promised that Zoom "remain firmly committed to the protection of our users' privacy," and that zoom was "reviewing our process and protocols
for implementing these features in the future to ensure this does not happen again.

On March 30, 2020, the *New York Times* reported that Zoom is under scrutiny by the office of New York State Attorney General "for its data privacy and security practicices." *Bloomberg* also reported that a user of Zoom's services had filed a lawsuit against the Company "who claims the popular video-conferencing service is illegally
disclosing personal information".

On March 31, 2020, the Federal Bureau of Investigation reportedly issued a warning about so-called "Zoom-bombing," the phenomenon identified by the *New York Times* where hackers can take over video-conferencing on the Company's app.

Between March 27, 2020, and April 2, 2020, Zoom's stock price fell $29.77 per share, or 19.62%, to close at $121.93 per share on April 2, 2020.

On April 3, 2020, *The Street* reported that Defendant Yuan "recently dumped $38 million of the company's stock ahead of an investigation into security breaches at the video conferencing company," and that SEC "filings viewed by the Daily Mail showed that Yuan and several other senior executives sold millions of dollars worth of their shares while the company has been addressing privacy issues." Specifically, the article disclosed that Defendant "Yuan . . . made $10.5 million in sales on Jan[uary] 14, another $12.5 million on Feb[ruary] 12, and $15.5 million on March 16," while "Chief Marketing Officer Janine Pelosi has made close to $14 million
in trades since February.

On April 6, 2020, New York City's Department of Education announced that it had banned the use of Zoom in the city's classroom.
As a result, Zoom's stock price fell $5.26 per share, or 4.10%, to close at $122.94 per share on April 6, 2020

The Complaint:

Throughout the class period, Defendants made false and/or misleading statements, as well as failed to disclose material adverse facts about the Company's business, operational and compliance policies resulting in artificially inflated prices. Specifically, Defendants made false and/or misleading statements and/or failed to disclose that:

1) Zoom had inadequate data privacy and security measures

2) Contrary to Zoom's assertions, the Company's video communications service was not end-to-end encrypted

3) As a result, users of Zoom's communications services were at an increased risk of having their personal information accessed by unauthorized parties, including Facebook

4) Usage of the Company's video communications services was foreseeably likely to decline when the foregoing facts came to light

5) As a result, the Company's public statements were materially false and misleading at all relevant times.

Statutory Violations"

Sections 10(b) and 20(a) of the Exchange Act and Rule 10b-5 under the SEC (17 C.F.R. § 240.10b-5).

***Riback v. iAnthusCapital*, 20-cv-03044 (S.D.N.Y.) - April 15, 2020 – Claims that canabis Industry Investment Company used COVID-19 as an improper excuse not to make loan payment**

Investors in iAnthus Capital Holdings Inc. claim the publicly traded cannabis company is **trying to use the coronavirus pandemic to explain away a missed $4.4 million interest payment**.

In a putative class action filed Wednesday, iAnthus investors told a New York federal court that the company's stock dropped 62% this month after an announcement that iAnthus would not be able to make a substantial interest payment to Gotham Green Partners, a private equity firm specializing in cannabis and cannabis-related enterprises.

The company blamed its inability to make the $4.4 million payment on a decline in public equity cannabis markets and extraordinary market conditions created by the COVID-19 pandemic, but according to investors, iAnthus has yet to explain why $5.7 million held in escrow for the firm's financing agreement with Gotham Green was not used to pay the tab.

"The members of the class, who relied upon defendants' class period statements concerning the intended use, and availability, of the escrowed funds to protect against a default under the debenture agreements with [Gotham Green], were ignorant of defendants' unwillingness to use, and/or the unavailability of, the escrowed funds," the investors claim.

The suit claims iAnthus is a highly leveraged holding company that acquires and operates a diversified portfolio of cannabis licenses and investments. It entered into a $50 million loan agreement with Gotham Green in May 2018 that provided for the withholding of $5.7 million in an escrow account to effectively pay one year's interest should iAnthus default, the investors allege.

The company entered into an amended agreement with Gotham Green last September that provided it with an additional $20 million in funding and maintained the escrow provision, the investors said.

Then, on April 6, iAnthus issued a press release announcing it had not been able to satisfy a $4.4 million interest payment due on March 31, attributing its inability to a "decline in the overall public equity cannabis markets, coupled with the extraordinary market conditions that began in Q1 2020 due to the novel coronavirus known as COVID-19 pandemic."

"The company is currently in default of the obligations to its secured debenture holders and the existence of such default triggers a cross-default of the obligation to its unsecured debenture holders," iAnthus' announcement said.

The press release also disclosed that iAnthus' board of directors had formed a special committee to investigate potential conflicts of interests and/or required disclosures with respect to its CEO and "certain related parties" and to explore "strategic alternatives available to the company in light of the prospective liquidity requirements of the company, the condition of the capital markets affecting companies in the cannabis industry and the rapid change in the state of the economy and capital markets generally caused by COVID-19."

News of the default caused the company's stock to fall from $0.469 per share on April 3 to $0.179 per share on April 6.

According to investors, iAnthus failed to disclose either that it could forgo using the escrow account to satisfy an interest payment or that the escrowed funds are exhausted, diminished or otherwise unavailable.

https://www.law360.com/articles/1264198/cannabis-firm-using-crisis-to-hide-shortfall-investors-say

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***Wandel v. Phoenix Tree Holdings, Ltd.*, 20-cv-03259 (S.D.N.Y.) - April 24, 2020 – Claims of REIT failing to adequately disclose significant apartment leases in Wuhan and potential negative impact of COVID-19 on those investments, IPO in January, 2020**

A putative class-action securities lawsuit was filed Friday against a Chinese real estate firm that had its initial public offering in January, charging it made only an oblique reference to the already raging coronavirus pandemic in its offering documents.

Beijing-based Phoenix Tree Holdings Ltd., a Cayman Islands holding company that **leases and manages apartments in 13 cities in China — including Wuhan**, where the pandemic originated — raised net proceeds of $128.4 million from its sale of American Depository Shares on Jan. 22, according to the lawsuit filed in U.S. District Court in New York against the company, its officers and directors, IPO underwriters and others. The lawsuit, *Katherine Wandel v. Jin Gao et al.*, was originally discussed in the *D&O Diary* blog.

Its offering materials said only that the company's business could be adversely affected by "the effects of Ebola virus disease, H1N1 flu, H7N9 flu, avian flu, Severe Acute Respiratory Syndrome, or SARS, or other epidemics" even though as of the offering materials' effective date "the coronavirus was already ravaging China — particularly Wuhan," according to the lawsuit.

The offering price for the ADS, which are traded on the New York Stock Exchange, at the time of the IPO was $13.50 per share. The price at last Friday's close was $6.97.

The suit charges also that the offering materials did not reveal that the company had received renter complaints that it had signed up tenants for bank loans without their knowledge.

"These issues presented known trends, uncertainties and risk that required disclosure in the Offering Materials," said the lawsuit, which charges violations of U.S. securities law.

https://www.businessinsurance.com/article/20200427/NEWS06/912334270

***Yannes v. SCWorx Corp., 20-cv-03349 (S.D.N.Y.)* - April 29, 2020 – Claims of false or inaccurate representations by company about significant purchase of COVID-19 rapid testing kits**

Intro: This is a class action on behalf of persons and entities that purchased or otherwise acquired SCWorx securities between April 13, 2020 and April 17, 2020, inclusive. The action is based on the fact that defendants made false and misleading statements causing the shares to artificially inflate and fall, causing loss to plaintiffs.

Date: April 29th, 2020

Court: United States District Court Southern District of New York

Plaintiffs: Daniel Yannes and others similarly situated

Defendants:

SCWorx is a publicly traded company which provides data content and services related to the repair, normalization and interoperability of information for healthcare providers

Defendant Marc S. Schessel is the Company's Chief Executive Officer and interim Chief Financial Officer.

Background and Timeline:

On April 13, 2020, before the market opened, SCWorx announced that it 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 23 weeks, valued at $35M per week.

On this news, the Company's share price increased by $9.77, to close at $12.02 per share on April 13, 2020.

On April 17, 2020, Hindenburg Research issued a report doubting the validity of the deal, calling it "completely bogus." According to Hindenburg Research, the Covid-19 test supplier that SCWorx is buying from, Promedical, has a Chief Executive Officer "who formerly ran another business accused of defrauding its investors and customers" and "was also alleged to have falsified his medical credentials," Promedical claimed to the FDA and regulators in Australia to be offering COVID-19 test kits manufactured by Wondfo, but "Wondfo put out a press release days ago stating that Promedical 'fraudulently mispresented themselves' as sellers of its Covid-19 tests and disavowed any relationship," and the buyer that SCWorx claimed to have lined up does not appear to be "capable of handling hundreds of millions of dollars in orders.

On this news, the Company's share price fell $1.19, or more than 17%, over three consecutive trading sessions to close at $5.76 per share on April 21, 2020, on unusually heavy trading volume.

On April 22, 2020, the SEC halted trading of the Company's stock. As of the filing of this complaint, trading remains halted.

The Complaint:

Throughout the Class Period, Defendants made materially false and/or misleading statements, as well as failed to disclose material adverse facts about the Company's business, operations, and prospects.

Defendants failed to disclose to investors:

1) That SCWorx's supplier for COVID-19 tests had previously misrepresented its operations;

2) That SCWorx's buyer was a small company that was unlikely to adequately support the purported volume of orders for COVID-19 tests;

3) That, as a result, the Company's purchase order for COVID-19 tests had been overstated or entirely fabricated; and

4) That, as a result of the foregoing, Defendants' positive statements about the Company's business, operations, and prospects, were materially misleading and/or lacked a reasonable basis.

Causation:

Defendants' wrongful conduct directly and proximately caused the economic loss suffered by Plaintiff and the Class. During the Class Period, Plaintiff and the Class purchased SCWorx's securities at artificially inflated prices and were damaged thereby. The price of the Company's securities significantly declined when the misrepresentations made to the market, and/or the information alleged herein to have been concealed from the market, and/or the effects thereof, were revealed, causing investors' losses.

Scienter:

Defendants acted with scienter since Defendants knew that the public documents and statements issued or disseminated in the name of the Company were materially false and/or misleading; knew that such statements or documents would be issued or disseminated to the investing public; and knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements or documents as primary violations of the federal securities laws.

Safe Harbor:

The statements alleged to be false and misleading all relate to then-existing facts and conditions. In addition, to the extent certain of the statements alleged to be false may be characterized as forward looking, they were not identified as "forward-looking statements" when made and there were no meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the purportedly forward-looking statements. In the alternative, to the extent that the statutory safe harbor is determined to apply to any forward-looking statements pleaded herein, Defendants are liable for those false forward- looking statements because at the time each of those forward-looking statements was made, the speaker had actual knowledge that the forward-looking statement was materially false or misleading, and/or the forward-looking statement was authorized or approved by an executive officer of SCWorx who knew that the statement was false when made.

***Hunter v. Elanco Animal Hospital, Inc.,* 20-cv-1460 (S.D.Ind.) - May 20, 2020 – Claims of lack of disclosure of distribution problems associated with COVID-19 issues**

Date: May 20, 2020

Court: United States District Court Southern District of Indiana Indianapolis Division

Plaintiffs: Sandra Hunter and Others similarly situated

Defendants:

Elanco is an animal health company that develops, manufactures, and markets products for companion and food animals.

Jeffrey Simmons, the Company's Chief Executive Officer.

Todd S. Young, the Company's Chief Financial Officer.

Background and Timeline

This is a class action lawsuit against D & Os of an animal products company for allegedly producing misleading financial information during the corona pandemic which lead to falsely increased stock prices. Elanco provided a financial plan and share guidance for 2020 in January. Of course, as 2020 changed, Elanco needed to adapt and on February 28th filed their 10-K with the SEC, stating that "changes in distribution could negatively impact shares." On March. 24th (at which point COVID-19 was a full blown pandemic), Elanco released a corona business update press release saying that they although they had not experienced any supply disruptions, they would be removing their share guidance for 2020 and expected possible revenue decline. On May 7th Elanco released their first quarter financial results, which had declined 9% due to Corona, and included a 60 million dollar loss in channel inventory. Jeff Simons, the CEO, stated that this was a result of corona related pressures on the distributors, who would not have the ability to properly distribute according to the initial projections. The suit is based on the claim that they did not tell anyone that there could be problems with distribution.

The Complaint:

1) After consolidating its distributors from eight to four, the Company increased the amount of inventory, including companion animal products, held by each distributor;

2) Elanco's distributors were not experiencing sufficient demand to sell through the inventory;

3) As a result, the Company's revenue was reasonably likely to decline;

4) As a result of the foregoing, Elanco would reduce its channel inventory with respect to companion animal products;

5) As a result of the foregoing, Defendants' positive statements about the Company's business, operations, and prospects, were materially misleading and/or lacked a reasonable basis.

Statutory Violations:

Sections 10(b) and 20(a) of the Exchange Act of 1934 and Rule 10b-5 under the SEC (17 C.F.R. § 240.10b-5)

***Wasa Medical Holdings v. Sorrento Therapeutics, Inc.*, 20-cv-00966 (S.D. Cal.) - May 26, 2020 – Claims of false and misleading representations of COVID-19 cure**

Intro: This is a federal securities class action on behalf of all investors who purchased Sorrento Therapeutics, Inc. common stock between May 15, 2020 and May 22, 2020, seeking to recover damages caused by Defendants' violations of the federal securities laws, particularly relating to false statements made regarding a "cure" for corona which resulted in artificially inflated stock.

Court: United States District Court District of Southern California

Date: May 26th, 2020

Plaintiffs: Wasa Medical Holdings Inc and similarly situated individuals

Defendants:

Sorrento is a biopharmaceutical company. The Company researches human therapeutic antibodies for the treatment of cancer, inflammation, and metabolic and infectious diseases.

Henry Ji is the co-founder and Chief Executive Officer of Sorrento. He has also served as a director of Sorrento since January 2006 and previously served as Sorrento's Chief Scientific Officer from November 2008 to September 2012.

Mark R. Brunswick is the Vice President of Regulatory Affairs and Quality of Sorrento.

Background and Timeline:

On May 8, 2020, Sorrento announced a collaboration with Mount Sinai Health System for the purpose of "generat[ing] antibody products that would act as a 'protective shield' against SARSCoV-2 coronavirus infection, potentially blocking and neutralizing the activity of the virus in naïve at-risk populations as well as recently infected individuals."

On May 15, 2020, Sorrento announced that it had discovered an antibody that had "demonstrated 100% inhibition of SARS-CoV-2 virus infection." Defendant Henry Ji, founder and Chief Executive Officer ("CEO") of Sorrento told Fox News, "We want to emphasize there is a cure. There is a solution that works 100 percent. Defendant Brunswick also stated in the same article, "As soon as it is infused, that patient is now immune to the disease … For the length of time, the antibody is in that system. So, if we were approved [by the FDA] today, everyone who gets that antibody can go back to work and have no fear of catching COVID-19." Defendant Brunswick's statement misleadingly conflated Sorrento's finding of 100% inhibition in an in vitro virus infection with 100% inhibition in a patient.

On this news, Sorrento shares increased $4.14 to close at $6.76 on May 15, 2020, on unusually heavy trading volume. The stock continued to increase after hours and opened at $9.98 on May 18, 2020, trading at a high of $10.00 that same day, which represented an increase of 281.7% from the May 14, 2020 closing price.

On May 20, 2020, Hindenburg Research issued a report doubting the validity of Sorrento's claims and calling them "sensational," "nonsense" and "too good to be true." Hindenburg spoke with researchers at Mount Sinai who stated that Sorrento's announcement was "very hyped" and that "nothing in medicine is 100%."

On May 20th, Defendant Ji made a public statement rebuffing the Hindenburg Report, stating that "investor[s] suspecting … another pump and dump" were wrong and that "when you see a virus is not infecting the healthy cell, you know you have the real deal" and "eventually the market [will] catch[] up."

Sorrento shares closed at $5.70 per share on May 20, 2020, representing a decline of $4.30, or 43.0%, from the Class Period high, on unusually high volume.

Finally, on May 22, 2020, BioSpace published an article stating that in a May 21, 2020 interview with Defendants Ji and Brunswick, Ji "insist[ed] that they did not say it was a cure.

On this news, Sorrento shares closed at $5.07 per share on May 22, 2020, representing a decline of $4.93, or 49.4%, from the Class Period high, on unusually high volume.

The Complaint:

During the Class Period, Defendants made materially false and/or misleading statements, as well as failed to disclose material adverse facts to investors. Specifically, Defendants misrepresented and/or failed to disclose that:

1) The Company's initial finding of "100% inhibition" in an in vitro virus infection will not necessarily translate to success or safety in vivo, or in person

2) The Company's finding was not a "cure" for COVID-19

3) As a result of the foregoing, Defendants' positive statements about the Company's business, operations, and prospects were materially misleading and/or lacked a reasonable basis.

Causation:

Defendants' wrongful conduct directly and proximately caused the economic loss suffered by Plaintiff and the Class. During the Class Period, Plaintiff and the Class purchased Sorrento's securities at artificially inflated prices and were damaged thereby. The price of the Company's securities significantly declined when the misrepresentations made to the market, and/or the information alleged herein to have been concealed from the market, and/or the effects thereof, were revealed, causing investors' losses.

Scienter:

Defendants acted with scienter because they knew that the public documents and statements issued or disseminated in the name of the Sorrento were materially false and/or misleading; knew that such statements or documents would be issued or disseminated to the investing public; and knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements or documents as primary violations of the federal securities laws. As set forth elsewhere herein in detail, the Individual Defendant, by virtue of his receipt of information reflecting the true facts regarding Sorrento, his control over, and/or receipt and/or modification of Sorrento's allegedly materially misleading misstatements and/or his associations with the Company which made him privy to confidential proprietary information concerning Sorrento, participated in the fraudulent scheme alleged herein.

Presumption of reliance:

All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in making investment decisions. Given the importance of the Class Period material misstatements and omissions set forth above, that requirement is satisfied here.

Safe Harbor:

The statutory safe harbor provided for forward-looking statements under certain circumstances does not apply to any of the allegedly false statements pleaded in this Complaint. The statements alleged to be false and misleading herein all relate to then-existing facts and conditions.

Statutory Violations:

Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 under the SEC

***Swartzenruber v. Colony Capital, Inc.*, 20-cv-4673 (C.D. Cal.) - May 26, 2020 – Claims of failure to disclose significant holding of impaired hotel and health care related properties**

The *Colony Capital, Inc.* class action lawsuit charges Colony Capital and certain of its officers with violations of the Securities Exchange Act of 1934 and seeks to represent purchasers of Colony Capital's securities between August 9, 2019 and May 7, 2020 (the "Class Period"). The *Colony Capital* class action lawsuit was commenced on May 26, 2020 in the Central District of California and is captioned *Swartzendruber v. Colony Capital, Inc.*, No. 20-cv-04673.

Colony Capital is a leading global investment management firm with assets under management of $55 billion. Colony Capital manages capital on behalf of its stockholders, as well as institutional and retail investors in private funds, and traded and non-traded real estate investment trusts.

The *Colony Capital* class action lawsuit alleges that defendants made false and/or misleading statements and/or failed to disclose that: (i) Colony Capital's sale of its industrial real estate portfolio and the bifurcation of Colony Credit Real Estate Inc.'s portfolio were foreseeably likely to negatively impact Colony Capital's financial and operating results; (ii) **certain of Colony Capital's remaining portfolio companies carried unsustainable levels of debt secured by**

<u>hotels and healthcare-related properties and were thus at a significant risk of default</u>; and (iii) as a result, Colony Capital's public statements were materially false and misleading at all relevant times.

On November 8, 2019, Colony Capital reported a GAAP net loss of $555 million, or ($1.15) per share, which "notably included reductions of goodwill, real estate and provision for loan losses totaling $540.3 million . . . of which $387.0 million was attributable to the reduction of goodwill primarily as a result of the pending sale of [Colony Capital's] industrial investment management business and related real estate portfolio, and the decrease in management fees from Colony Credit Real Estate, Inc. resulting from impairments related to its portfolio bifurcation." On this news, Colony Capital's stock price fell nearly 9%.

Then, on May 8, 2020, Colony Capital reported that its portfolio companies had **<u>defaulted on $3.2 billion of debt secured by hotels and healthcare-related properties and that Colony Capital had received a notice of acceleration covering $780 million of the defaulted debt</u>**. On this news, Colony Capital's stock price fell an additional 3.81%.

https://www.rgrdlaw.com/cases-colony-capital-inc-class-action-lawsuit.html

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***Service Lamp Corp. Profit Sharing Plan v. Carnival Corporation,* 20-cv-22202 (S.D. Fla.) - May 27, 2020 - Cruise Ship case – Claims of failure to disclose knowledge and false and misleading statements of COVID-19 exposure and risks**

Intro: Class action for plaintiffs for the class period of 28th 2020 and May 1st

Date: May 27th, 2020

Court: United States District Court of Southern Florida

Plaintiffs: Service Lamp Corporation Profit Sharing Plan and others similarly situated

Defendants: Carnival Corp. – Crusie Ship Lines

Carnival has operations in North America, Australia, Europe and Asia, operating a portfolio of global, regional and national cruise brands that sell tailored cruise products, services and vacation experiences on 104 cruise ships to destinations around the world

Defendant Arnold W. Donald is the president and chief executive officer of Carnival.

Defendant David Bernstein is at all times relevant, chief financial officer of Carnival.

Background and Timeline:

On January 28, 2020, the first day of the Class Period, Carnival its annual report on Form 10-K for the fiscal year ending November 30, 2019. In its Form 10-K carnival discussed stated, among other things, that it provides "regular health, environmental, safety and security support, training, guidance and information to guests, employees and others working on our behalf," that it had developed and implemented "effective and verifiable management systems to fulfill our health, environmental, safety, security and sustainability commitments," and that it reports and investigates "health, environmental, safety and security incidents and take[s] appropriate actions".

By February 5, 3,700 passengers and crew were quarantined about the Diamond Princess, a Gem-class ship operated by Princess Cruises, a cruise line owned by Carnival. On February 12, 2020 Carnival released a press release called which stated " Th*e safety of guests and employees, compliance and protecting the environment are top priorities for the company. The company's medical experts are coordinating closely with the U.S. Centers for Disease Control and Prevention and the World Health Organization to implement enhanced screening, prevention and control measures for its guests, crew and ships."*

On February 20, the Grand Princess, the first of the Grand-class cruise ships, docked in San Francisco and at least one known COVID infected person disembarked. That COVID infected individual had reportedly been seen by the ship doctor. By March 4, 2020 there was a COVID related fatality on board the Grand Princess, and seven (7) Company ships accounted for 49 of the 70 cruise ship fatalities.

On March 19th, they released another press statement saying: "*Carnival Corporation and its brands are calling on governments and health authorities to consider using cruise ships as temporary healthcare facilities to treat non-COVID-19 patients."*

On April 16, 2020, when the Company still had at sea two of its cruise ships, *Bloomberg Businessweek* published an article which revealed that Carnival may have failed to adequately protect passengers from COVID-19 on a series of cruise voyages and indeed continued to operate new cruise departures despite knowledge of the proliferation of COVID-19. The article also detailed Carnival's failure to take timely action after being apprised of COVID-19 threats to its fleet and passengers. Notably the article also intimated that Carnival executives, including Defendant Donald, knew about the scale of the COVID-19 outbreak before the Company filed its Form 10-K on January 28, 2020, and indeed knew of the magnitude of the issue much earlier than most. On this news, the Company's share price fell $0.53 per share from a prior close of $12.38 per share to close at $11.85 per share on April 16, 2020.

Then, on May 1, 2020, *The Wall Street Journal* published an article titled "Cruise Ships Set Sail Knowing the Deadly Risk to Passengers and Crew," which detailed how cruise ships, including Carnival ships, facilitated the spread of COVID-19 and provided new facts about early warning signs Carnival and its cruise lines possessed and the Company's related COVID-19 disclosure failures. The article also noted that testimony from an investigation in Australia revealed that Carnival and its cruise lines may have misled shore officials by concealing those exhibiting COVID-19 symptoms before docking. On the same day, it was revealed that the Chair of the House Committee on Transportation and Infrastructure and Chair of the House Subcommittee on Coast Guard and Maritime Transportation had initiated a records request regarding the response of Carnival to Covid-19 or other infectious disease outbreaks aboard cruise ships. On this news, the Company's share price fell $1.97 per share from a prior close of $15.90 per share to close at $13.93 per share on May 1, 2020, further damaging Carnival investors.

The Complaint

1) Increased Corona exposure on company ships

2) Violated regulations by failing to report COVID outbreak on ships

3) Failed to follow safety protocols for outbreaks

4) Continued operations spread corona throughout the world

5) Because of this, the positive statements about the company's financial well-being were materially false and misleading

Statutory Violations:

Sections 10(b) and 20(a) of the Securities Exchange Act of 1934

Scienter:

During the Class Period, the Defendants had both the motive and the opportunity to commit fraud. Defendants also had actual knowledge of the misleading nature of their statements, or acted with reckless disregard for the true information known to them at the time they made those statements. In so doing, Defendants engaged in a course of conduct that operated as a fraud on Class Period purchasers of Carnival common stock.

Causation:

During the Class Period, Defendants made false and misleading statements and engaged in a scheme to deceive the market and a course of conduct that artificially inflated the prices of Carnival common stock. Later, when the market became aware of Defendants' prior misrepresentations, the price of Carnival common stock fell sharply, as the prior artificial inflation came out of the trading price of Carnival. As a result of their purchases of Carnival common stock during the Class Period, Plaintiff and other members of the Class suffered economic loss under the federal securities laws

Safe Harbor:

There is no safe harbor because the defendants knew that the statements were false and misleading.

***Guafeng Ma v. Wells Fargo & Company*, 20-cv-3697 (N.D. Cal.) - June 10, 2020 – Claims of improper and unfair administration of PPP Loan Program and untrue statements about this**

A proposed securities class action filed against Wells Fargo in California federal court Thursday accuses the banking giant of hiding its dishonest policy for administering federal Paycheck Protection Program loans for small businesses struggling during the COVID-19 pandemic, causing its stock price to drop twice in two weeks.

Small businesses have filed lawsuits against Wells Fargo, accusing it of unfairly pushing their loan applications to the back of the pile in favor of requests from larger businesses that would yield larger processing fees instead of processing applications on a first-come, first-served basis.

By handling larger companies first beginning April 3, small applications were reviewed only just before the program ran out of money, those lawsuits allege.

In Thursday's putative class action filing, investor Guofeng Ma alleges that in misrepresenting its handling of the PPP loans, Wells Fargo opened up the bank to litigation and possible regulatory scrutiny and enforcement actions, allegations of which caused the stock price to drop more than 5% in April and again fall more than 6% in May.

Wells Fargo and other banks have been administering the PPP loans coming from the Coronavirus Aid, Relief, and Economic Security Act, with Wells Fargo tasked with distributing $10 billion to small-business customers.

Paid for by the U.S. Small Business Administration in two rounds of funding, the PPP authorizes up to $659 billion in forgivable loans to businesses with 500 or fewer employees to pay them during the coronavirus crisis.

Thursday's lawsuit alleges investors were harmed after the country's fourth-largest bank lied when it said it was focused on lending to businesses with fewer than 50 employees and nonprofits, when in fact, investors claim, it selected loans between $2 million and $10 million to make up to $100,000 in processing fees, as opposed to making up to $17,500 for processing smaller loans under $350,000.

Wells Fargo is also facing lawsuits accusing it of improperly requiring businesses to have pre-existing checking accounts to apply for the PPP loans.

The investor suit cites press releases from Wells Fargo that commit the bank to "focus lending to nonprofits and small businesses with fewer than 50 employees" and giving processing fees to nonprofits focused on small businesses.

The Federal Reserve on April 8 announced it would allow Wells Fargo to exceed the $2 trillion asset cap it had imposed in 2018 following revelations that the bank had opened millions of customer accounts without the customers' permission.

In a press release that day, the bank said it would expand its program and "offer loans to a broader set of its small-business and nonprofit customers subject to the terms of the program."

In an April 14 first-quarter earnings call, Wells Fargo CEO Charles W. Scharf said the bank "extended [their] participation in the PPP program and hope to provide significant relief to [their] small-business customers."

Scharf and Chief Financial Officer John R. Shrewsberry are named in the investor suit, which argues they "had a duty to disseminate accurate and truthful information with respect to Wells Fargo's financial condition and results of operations, and to correct promptly any public statements issued by Wells Fargo which had become materially false or misleading."

By misleading investors and the public about its focus on smaller businesses, Wells Fargo increased the company's litigation risk, increased regulatory scrutiny and/or potential enforcement actions, the suit claims.

On April 19, USA Today published an article highlighting a lawsuit filed against Wells Fargo for giving the government-backed PPP loans to larger companies.

As a result, the stock fell more than 5% over two trading days to close at $26.84 per share on April 21, investors allege.

On May 5, in its quarterly report filed with the U.S. Securities and Exchange Commission, Wells Fargo disclosed that it had "received formal and informal inquiries from federal and state governmental agencies regarding its offering of PPP loans."

Following this news, Wells Fargo's stock price fell by more than 6% over two trading days, closing at $25.61 per share on May 6.

The investor lawsuit alleges Wells Fargo used "fraud and deceit" in its management of PPP funds and by lying about how they were handling the program they did "artificially inflate and maintain the market price of Wells Fargo securities."

The suit seeks to represent a class of people who acquired Wells Fargo securities between April 5 and May 5, 2020.

https://www.law360.com/banking/articles/1280063?utm_source=rss&utm_medium=rss&utm_campaign=section

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***The Arbitrage Fund, et al. v. Forescout Technologies, Inc., et al.*, 20-cv-03819 (N.D. Cal.) - June 10, 2020 – Claims for failing to disclose negative impact of COVID-19 on its business in midst of attempted merger deal with Advent**

http://securities.stanford.edu/filings-case.html?id=107434:

> According to the Complaint, Forescout Technologies, Inc. provides "security at first sight" by delivering software that enables device visibility and control that enables enterprises and government agencies to gain improved situational awareness of their environment (devices on their networks) and orchestrate actions to reduce cyber and operational risk.
>
> The Complaint alleges that Defendants made materially false and misleading statements and omissions of material facts regarding the significant and disproportionate decline in Forescout's financial performance and the related risk Forescout's planned acquisition by Advent International Corp. would not close. As a result, Class members that purchased Forescout common stock during the Class Period did so at artificially inflated prices.
>
> Specifically, the Complaint alleges that by the start of the Class Period on February 6, 2020 – when Forescout announced the Merger Agreement with Advent and positive fourth quarter 2019 earnings— Forescout knew that its business had begun to suffer a dramatic and undisclosed downturn, including it its fast-growing Asia

> Pacific and Japan ("APJ") region that was impacted by COVID19 starting in January. In addition, Forescout was aware that its fourth quarter 2019 revenues were inflated through an abnormal transaction with one of its largest resale customers, Merlin International Inc., which a whistleblower has alleged to Advent was the result of a "channel stuffing scheme" in the fourth quarter of 2019. Because of these factors, Forescout knew that the consummation of the Transaction was exceptionally risky at the time it announced the Merger Agreement.
>
> Forescout neither disclosed these facts to investors nor Advent at the time it signed the Merger Agreement. Nor did Forescout disclose that its financial collapse would preclude the availability of the debt financing needed to close the transaction. In fact, while Forescout provided certain revised projections during the sales process to bidders, it did not disclose the true known extent of its financial downturn, including the early impacts of COVID-19 on the APJ region, nor the abnormal transaction with Merlin.

***Gelt Trading v. Co-Daignostics, Inc.*, 20-cv-00368 (D. Utah) - June 15, 2020 - Claims regarding reliability of company's COVID-19 tests**

Covid-Test Maker Sued by Investor Over '100% Accurate' Claim

A maker of Covid-19 tests was sued by an investor who accused the company of falsely claiming its tests were 100% accurate in order to juice its share price while officers and directors were exercising their stock options.

Co-Diagnostics Inc. was named in a securities-fraud suit filed Monday in federal court in Salt Lake City by Gelt Trading Ltd. Sandy, Utah-based Co-Diagnostics was among a number of small-cap diagnostic companies that saw their market value multiply earlier this year because of the importance of testing in combating the coronavirus.

Worth less than a dollar at the end of last year, shares in Co-Diagnostics soared as high as $29.72 based on the company's representations of the accuracy of its tests and orders it received, according to the complaint.

"Unlike many securities fraud cases, the Co-Diagnostics fraud is blunt and simple to understand," Gelt said in its lawsuit. "Co-Diagnostics, its chief technology officer, and its other officers and directors made unequivocal statements to the market that its Covid-19 tests were 100% accurate -- a staggering claim that appeared to set Co-Diagnostics apart from other competitors developing Covid-19 tests."

Co-diagnostic's share price fell last month after the U.S. Food and Drug Administration said no Covid-19 test is 100% accurate, according to the complaint. The company was trading at around $17.71 on Monday afternoon.

In February, Co-Diagnostics said it had received regulatory clearance to sell its tests in the European Union, making it the first company in the world to receive this clearance, according to the investor's lawsuit. In April, the company said it had received emergency use authorization for its tests from the FDA, according to the complaint.

https://news.bloomberglaw.com/securities-law/covid-test-maker-sued-by-investor-over-100-accurate-claim

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***Cherynysh v. Chembio Diagnostics, Inc.*, 20-cv-2706 (E.D.N.Y.) - June 16, 2020 - Claims regarding accuracy and reliability of company's COVID-19 tests**

The Class Action, *Sergey Chernysh v. Chembio Diagnostics, Inc.*, et al., Case No.: 2:20-cv-02706, was filed in the United States District Court for the Eastern District of New York on behalf of shareholders who purchased CHEMBIO common stock between April 1, 2020 and June 16, 2020, inclusive (the "Class Period"). The lawsuit seeks to recover damages against CHEMBIO and certain officers for alleged violations of federal securities laws.

Specifically, the alleges that throughout the Class Period, defendants misrepresented the efficacy of its DPP COVID-19 test for the detection of antibodies in determining exposure to the COVID-19 virus, thereby engaging in a scheme to deceive the market; and that on May 11, 2020, defendants took advantage of the inflated stock price and closed a public offering of approximately 2.6 million shares of stock for gross proceeds of approximately $30.8 million.

On June 16, 2020, the FDA disclosed that it revoked CHEMBIO'S Emergency Use Authorization ("EUA") due to performance concerns with the accuracy of the test. Data submitted by CHEMBIO as well as an independent evaluation of the Chembio test at NCI showed that the test generates a higher than expected rate of false results and higher than that reflected in the authorized labeling for the device. The FDA concluded that the risk to public health from the false test results makes EUA revocation appropriate to protect the public health or safety, and that the test could not be distributed. On this news, CHEMBIO'S stock fell over 60% in intraday trading on June 17, 2020.

https://www.globenewswire.com/news-release/2020/06/19/2050546/0/en/CHEMBIO-ALERT-Barbuto-Johansson-P-A-Informs-Investors-that-a-Securities-Class-Action-Lawsuit-Has-Been-Filed-Against-Chembio-Diagnostics-Inc-Sued-for-Misrepresentations-of-COVID-19-.html

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***Lucas v. United States Oil Fund, L.P.*, 20-cv-4740 (E.D.N.Y.) - June 20, 2020 – Claims regarding disclosures and representations of oil price speculation investment company**

The USO class action lawsuit charges USO and certain of its officers and directors with violations of the Securities Exchange Act of 1934. USO is an exchange traded fund ("ETF") purportedly designed to track the daily changes in percentage terms of the spot price of West Texas Intermediate ("WTI") light, sweet crude oil delivered to Cushing, Oklahoma. Because retail investors are generally not equipped to buy and sell barrels of oil or authorized to trade oil futures, ETFs such as USO provide one of the primary means by which such investors can gain exposure to fluctuations in oil prices.

The complaint alleges that during the Class Period, defendants stated that USO would achieve its investment objective by investing substantially all of its portfolio assets in the near month WTI futures contract. However, unbeknownst to investors, extraordinary market conditions in early 2020 made USO's purported investment objective and strategy unfeasible. Oil demand fell precipitously as governments imposed lockdowns and businesses halted operations in response to the coronavirus pandemic. In addition, in early March 2020, Saudi Arabia and Russia launched an oil price war, increasing production and slashing export prices in a bid to increase the global market share of their domestic petrochemical enterprises. As excess oil supply increased and oil prices waned, the facilities available for storage in Cushing, Oklahoma approached capacity, ultimately causing a rare market dynamic known as "super contango" in which the futures prices for oil substantially exceeded the spot price. At the same time, retail investors began pouring hundreds of millions of dollars into USO in an attempt to "buy the dip," believing (correctly) that the price of oil would rebound as economies exited lockdown periods and the Russia/Saudi oil price war ended. Because of the nature of USO's investment strategy, these converging factors caused the Fund to suffer exceptional losses and undermined the Fund's ability to meet its ostensible investment objective.

According to the complaint, defendants, as the creators, issuers and operators of the largest oil-related ETF in existence and active market-making players in the complex commodities and futures markets that determined the Fund's performance, possessed inside knowledge about the negative consequences to the Fund as a result of these converging adverse events.

However, rather than disclose the known impacts and risks to the Fund as a result of these exceptional threats, defendants instead commenced an offering of USO shares in March 2020, ultimately selling billions of dollars' worth of USO shares to the market. Although the offering increased the fees payable to defendants, it also exacerbated the undisclosed risks to the Fund by magnifying trading inefficiencies and causing USO to approach position and accountability limits as a result of the Fund's massive positions in the WTI futures market.

Ultimately, the Fund suffered billions of dollars in losses and was forced to abandon its investment strategy. Through a series of rapid-fire investment overhauls, USO was forced to transform from the passive ETF designed to track spot oil prices that defendants had pitched to investors to an almost unrecognizable actively managed fund struggling to avoid a total implosion. In April and May 2020, defendants belatedly acknowledged the extreme threats and adverse impacts that the Fund had been experiencing at the time of the March offering, but which they had failed to disclose to investors.

https://apnews.com/8b7efd0d532741f4b7e20b86432fd066

***Steve Hartel, et al. v. The GEO Group, Inc.*, et al., 20-cv-81063, (S.D. Fla.) - July 7, 2020 – Claims regarding false and/or misleading statements and/or failed to disclose that company maintained allegedly woefully ineffective COVID-19 response procedures.**

http://securities.stanford.edu/filings-case.html?id=107458:

> According to the Complaint, GEO Group is purportedly the first fully integrated equity real estate investment trust specializing in the design, financing, development, and operation of secure facilities, processing centers, and community reentry centers in the U.S., Australia, South Africa, and the United Kingdom. GEO

> Group is also purportedly a leading provider of enhanced in-custody rehabilitation, post-release support, electronic monitoring, and community-based programs. The Company's worldwide operation include the ownership and/or management of, among other facilities, halfway houses in the U.S.
>
> The Complaint alleges that throughout the Class Period, Defendants made materially false and misleading statements regarding the Company's business, operational and compliance policies. Specifically, Defendants made false and/or misleading statements and/or failed to disclose that: (i) GEO Group maintained woefully ineffective COVID-19 response procedures; (ii) those inadequate procedures subjected residents of the Company's halfway houses to significant health risks; (iii) accordingly, the Company was vulnerable to significant financial and/or reputational harm; and (iv) as a result, the Company's public statements were materially false and misleading at all relevant times.

Examples of SEC Enforcement Actions

***SEC v. Praxsyn Corp. and Frank J. Brady* - April 28, 2020**

Intro: This is an SEC complaint against Praxsyn and it's CEO Frank Brady. The complaint is based on false and misleading statements that the company and CEO made in press releases causing shares to artificially inflate and fall. In addition to civil penalties, the SEC requested bar against Brady from functioning as an officer or director of any publicly traded company

Date: April 28th, 2020

Court: United States District Court District of Southern Florida

Plaintiff: Securities and Exchange Commission

Defendants:

Praxsyn is a Nevada corporation incorporated in 2014 with its principal offices purportedly located in West Palm Beach, Florida. Praxsyn claims to be a "specialty finance company focused on providing cash flow solutions and medical receivables financing to healthcare providers in the US that focus on personal injury and workers compensation." Neither Praxsyn nor its securities are registered with the Commission. Praxsyn's common shares are quoted on OTC Link (previously "Pink Sheets") operated by OTC Markets Group Inc. The Commission suspended trading in Praxsyn's securities from March 26 through April 8, 2020.

Frank Brady, Praxsyn's chief executive officer

Background and Timeline:

On February 27, 2020, Praxsyn issued a press release stating, among other things, that it was negotiating the sale of millions of masks meeting the standards for N95 masks set by the National Institute for Occupational Safety and Health (and similar standards), and that the company was vetting suppliers to guarantee a dependable supply chain of the masks.

On March 4, 2020, Praxsyn issued another press release asserting it had a large number of N95 masks on hand and had created a "direct pipeline from manufacturers and suppliers to buyers" of the masks. Those masks have been and continue to be in high demand around the world. Brady was quoted in both press releases, including stating that Praxsyn was only taking orders of 100,000 masks or more.

Both press releases were blatantly false. Praxsyn never had either a single order from any buyer to purchase masks, or a single contract with any manufacturer or supplier to obtain masks, let alone any masks actually in its possession. Dozens of emails and other documents from late February through March show Brady and at least one Praxsyn director knew efforts to obtain and sell N95 or other masks were proving futile. Praxsyn admitted as much when, after regulatory inquiries, it issued a third press release on March 31, 2020 acknowledging it never had masks on hand.

Every factual statement in the March 4 press release was false. At the time, Praxsyn had no masks in its possession, no orders from any purchaser to buy masks, and no agreements to buy masks from any supplier or manufacturer. Because there were no orders, no agreements, and no masks, there was no pipeline. And there was no worldwide network – only email exchanges between Praxsyn and four foreign companies in which Praxsyn was trying to find masks to buy. There were a total of three inquiries from potential buyers, none of them going beyond the initial inquiry stage, by March 4th.

Furthermore, Praxsyn had reason to doubt the validity of the promises of manufacturers or others to supply masks. On the same day Praxsyn issued the March 4 release, one of its directors sent an email acknowledging that "there is a lot of competition out there that is quite unscrupulous" on the supply side and trying to get answers to various fundamental questions in vetting suppliers. Because of the problems identifying suppliers with the appropriate masks, Praxsyn had no idea whether any of the masks it was seeking could protect against the COVID 19 virus, and it had no idea whether it could offer "the fairest price on the market" as its press release claimed. Brady received many of the emails the director sent and received, and therefore knew the true situation with Praxsyn's efforts to buy and sell masks.

Over the next four weeks, Praxsyn, largely through the director's efforts, continued without any success to find both suppliers and purchasers of masks. Finally, 27 days after falsely claiming that it had masks, had created a direct pipeline from manufacturers and suppliers to buyers, and was working through a worldwide network, Praxsyn (only after regulatory inquiries) issued a third press release on March 31 admitting that it had not ever had any masks to sell.

Praxsyn's stock trading volume increased significantly after both releases, and its stock price also increased significantly after the second release. In the three months prior to February 27, Praxsyn's share price fluctuated between $0.0048 and $0.009, with an average daily trading volume of 384,165 shares. On February 27, Praxsyn's share price approximately doubled, fluctuating between $0.0095 and $0.0188 with a trading volume of 30,819,560 shares (approximately 80 times the pre-February 27 volume). On March 4, the share price fluctuated between $0.0053 and $0.0091 with a trading volume of 12,043,460 shares.

Through their conduct, Praxsyn and Brady violated Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §78j(b) and 17 C.F.R. §240.10b-5. The

Commission seeks injunctive relief and civil penalties against both Defendants, and an officer-and-director bar against Brady.

Statutory Violations:

Section 10(b) of the Exchange Act of 1934 and Rule 10b-5(a-c) under the SEC (17 C.F.R. § 240.10b-5).

Additional remedy requested:

Issue an Order barring Brady from serving as an officer or director of any public company pursuant to Section 21(d) of the Exchange Act and Section 305(b)(5) of the Sarbanes-Oxley Act.

***SEC v. Turbo Global Partners, Inc. et al* - May 14, 2020**

Intro: This is an SEC complaint against Turbo and it's CEO for making intentionally false statements about a partnership with another company which would provide corona scanning devices, violating Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5.

Court: United States District Court Middle District of Florida

Date: May 14th, 2020

Plaintiffs: United States Securities and Exchange Commission

Defendants:

Turbo Global Partners, Inc. is a Nevada corporation with its principal place of business in Tampa, Florida. The Commission temporarily suspended trading in TRBO's securities from April 9, 2020 to April 23, 2020. TRBO purports to be a digital marketing company that places digital displays inside any business or location that attracts consumers, focused on pharmacies.

Robert W. Singerman, is the chief executive officer and chairman of TRBO and resides in Tampa, Florida. Singerman is a recidivist securities violator. The Commission previously charged Singerman with fraud in 1999 based on his fraudulent sale of securities through a network of boiler rooms, and a permanent injunction was entered against Singerman in connection with that conduct.

Background and Timeline:

In February 2020, TRBO issued two press releases announcing that it had formed a "strategic alliance" with BeMotion. Under this alliance, TRBO would purchase digital vending machines from BeMotion and install them in pharmacies with which TRBO had a relationship. These press releases represented that TRBO and BeMotion were actively selling equipment that scans large crowds to detect individuals with elevated fevers, and claimed that this unique technology could be instrumental in breaking "the chain of virus transmission through early identification of elevated fever, one of the key early signs of COVID-19." The press releases further claimed, among other things, that TRBO was the "intermediary in this private/public partnership," the product was available to be deployed immediately, and that RBO could ship the product within five days of receiving an order.

In March 2020, as the COVID-19 crisis escalated, BeMotion signed a contract with a company in China that manufactured thermal scanning equipment. The contract empowered BeMotion to sell the thermal scanning equipment outside of China. The scanning equipment could be installed in retail or other establishments to scan for persons with above normal body temperatures. BeMotion then began looking for possible distributors to assist with the sale of this product.

During March 2020, BeMotion shared a thermal scanning product brochure with TRBO. Singerman expressed to BeMotion an interest in TRBO becoming the exclusive distributor for the product. BeMotion's CEO responded that TRBO could not be an exclusive distributor and could only be a distributor if it had customers willing to buy the product.

BeMotion and TRBO never reached agreement on the terms of any distribution arrangement for the thermal scanning equipment.

During March 2020, Singerman asked the CEO of BeMotion whether he knew of anyone who might be interested in investing in TRBO. The CEO of BeMotion replied negatively.

On March 30th TRBO issued a press release drafted by Singerman, which contained a number of materially false and misleading statements. The release falsely stated that BeMotion "is [the] front facing Partner in the multi-national public-private-partnership (PPP) for this innovation which simply stated, is the only scanning technology on the planet with non-contact intelligent human temperature screening and facial recognition.

In fact, BeMotion was not engaged in any public-private partnership or any partnership involving a governmental entity. Further, the scanning equipment in question did not have facial recognition technology. The technology only had face detection ability (i.e., it could distinguish a face from a cup of coffee).

The release further falsely stated that TRBO is "the lead intermediary" and "the U.S. Coordinating agent and Intermediary," suggesting that it was the authorized selling agent in the United States for this product.

In fact, prior to the release, BeMotion had advised TRBO that TRBO would not be allowed to be the sole U.S. distributor and that it could only distribute the equipment if TRBO had customers willing to buy it. Further, no agreement relating to the scanning technology had been finalized between BeMotion and TRBO.

The release also quoted the CEO of BeMotion as stating: "Our technology instantly RED FLAGS an elevated body temperature and is 99.99% accurate, and is the only system that includes both state-of-the-art human body temperature scanning and facial recognition."

In fact, the CEO of BeMotion did not make or authorize the statement attributed to him and the technology did not have facial recognition capability, but only face identification technology. Further, the system is not the only system available with that ability.

The release further quoted the CEO of BeMotion as stating that: "TURBO and BeMotion, through our PPP are ready to deploy and help coordinate any expedited procurement process. After receipt of orders, systems ship in 5-days thereafter. *** This technology is designed to be deployed IMMEDIATELY in each State, with coordinated participation of Local, County, State and Federal Agencies working together to break the chain of virus transmission with early elevated fever detection."

In fact, the CEO of BeMotion did not make or authorize the above statement attributed to him. Moreover, BeMotion had advised TRBO through Singerman, that although BeMotion would be able to ship the systems in five days once BeMotion had an inventory of the systems in Canada, BeMotion could not presently ship the systems that quickly because it did not have the systems in Canada.

On April 3, 2020, TRBO issued another press release drafted by Singerman, in which Singerman "confirmed" that the Governor's offices for all 50 states and their Chiefs of Staff had been contacted regarding the availability of BeMotion's equipment, and that each office had been provided "the Technical Documents for our technology." Singerman also represented that he had personally contacted the CEOs for various major retail companies, such as Target, WalMart, and Costco, and "advised we are standing by to assist with expedited procurement."

TRBO's misleading releases materially affected the trading market for TRBO stock. From March 16 through March 30, 2020 (the 11 trading days immediately preceding the March 30 release), TRBO trading volume averaged around 31.9 million shares per day, and the share price ranged between $0.0016 and $0.0059. On March 31, the first trading day after the March 30 release, TRBO's trading volume jumped to 77.8 million shares and the share price hit an intraday high of $0.0068, before closing at $0.0044.

On April 3 (when TRBO issued its press release regarding contacting all 50 Governors' offices), volume reached 76 million shares and the price hit an intra-day high of $0.0194, before closing at $0.0154.

TRBO's press releases materially impacted both the trading volume and share price of TRBO securities. For example, the day after one of the press releases issued, the trading volume doubled and the intraday high for the share price jumped around 15%.

The Complaint:

Defendants TRBO and Singerman, in connection with the purchase and sale of securities the use of the means and instrumentalities of interstate commerce and by use of the mails, directly and indirectly:

1) Employed devices, schemes, and artifices to defraud;

2) Made untrue statements of material facts and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and

3) Engaged in acts, practices, and courses of business which would and did operate as a fraud and deceit upon the purchasers of such securities

Defendants TRBO and Singerman knowingly, intentionally, and/or recklessly engaged in the aforementioned devices, schemes and artifices to defraud, made untrue statements of material facts and omitted to state material facts, and engaged in fraudulent acts, practices and courses of business. In engaging in such conduct, the defendants acted with scienter, that is, with an intent to deceive, manipulate or defraud or with a severely reckless disregard for the truth. Defendants TRBO and Singerman, directly and indirectly, have violated and, unless enjoined, will continue to violate Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)] and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

Other Sources of Information:

Standford Law School – Securities Class Action Clearinghouse Filings Database: http://securities.stanford.edu/filings.html

Kevin LaCroix's The D&O Diary is an excellent source for updated D&O information: https://www.dandodiary.com/

For general statistical information about COVID-19 related lawsuits see the University of Pennsylvania Carey Law School's Covid Coverage Litigation Tracker https://cclt.law.upenn.edu/

4) State Specific Example - Minnesota Law on Directors and Officers Standard of Care

Under Minnesota Law Minn. Stat. § 302A.467 provides:

> If ... an officer or director of the corporation violates a provision of this chapter, a court in this state may, in an action brought by a shareholder of the corporation, grant any equitable relief it deems just and reasonable in the circumstances and award expenses, including attorneys' fees and disbursements, to the shareholder.

"The chapter requires that directors and officers of corporations act in a manner that the director or officer reasonably believes to be in the best interests of the corporation." *Bolander v. Bolander*, 703 N.W.2d 529, 548 (Minn. App. 2005) (citing) Minn. Stat. §§ 302A.251, subd. 1, .361 (2004). Additionally, an officer or director owes a fiduciary relationship to the corporation under common law. *See Bolander v. Bolander*, 703 N.W.2d 529, 548 (Minn. App. 2005); *In re Villa Maria, Inc.*, 312 N.W.2d 921, 922-23 (Minn.1981).

Directors and officers are often sued in securities litigation. 22 Minn. Prac., Insurance Law & Practice § 7:2 (2012 ed.)

See also Michael Sean Quinn & Andrea D. Levin, *Directors' and Officers' Liability Insurance: Probable Directions in Texas Law*, 20 Rev. Litig. 381, 386-89 (2001):

> I. Legal Duties of Directors and Officers
>
> In general, directors and officers have duties to act in good faith with loyalty to the corporation and with due care.[20] In most states, liability cannot be based on a director's negligence in breach of these duties. This is often true because of the application of the business judgment rule (BJR) or as a result of director shield statutes.[21] The business judgment rule is a commonly used defense that in some states, including Texas, raises the required standard for liability to something greater than negligence.[22] Director shield statutes, enacted after a landmark Delaware case,[23] hold both directors and officers liable for breaching a specified duty of care.[24] D&O liability for fraudulent behavior or intentional conduct is not discussed here, primarily because most, if not all, D&O insurance policies do not cover intentional condu Thus, this Article discusses the following foundation issues: (1) the duties of directors and officers, (2) their primary legal defenses (other

than attacking the merits of the claim or generic defenses such as statute of limitations bars), (3) the standard of conduct (between negligence and intentional conduct) required to impose liability, and (4) the different liability standards applied to directors and officers.

In contemplating the regulation of the conduct of directors and officers, one needs to keep in mind that the public often judges the conduct of directors and officers according to social norms rather than legal ones.[25] Indeed, one distinguished scholar of corporate law argues that social norms overshadow and may even overwhelm legal norms when it comes to regulating directorial activity.[26] Professor Melvin Eisenberg believes that social norms have become much more important in recent years.

A. D&O Duties: The Standard of Conduct

1. The Traditional Duties
Section 8.30 of the 1984 version of the Revised Model Business Corporations Act (RMBCA) codified the traditional standard of conduct for directors as including the duties of good faith, ordinary care, and loyalty. Under the statute:

> A director shall discharge his duties as a director, including his duties as a member of a committee:
> (1) in good faith;
> (2) with the care an ordinarily prudent person in a like position would exercise under similar circumstances; and
> (3) in a manner he reasonably believes to be in the best interests of the corporation.[27]

Directors are fiduciaries of the corporations they dire[28] Directors must therefore be "unselfish" (i.e ., they must demonstrate loyalty) in dealing with the corporations or entities they dire[29] Directors are required to take "extreme" measures in order to achieve candor, maintain unselfishness, and keep good faith. These requirements are "rigid, essential and salutary."[30] Finally, directors must exercise due care.

a) Directors' Liabilities under Minnesota Law

A director is generally not liable for any action taken as a director, or any failure to take any action, if the director performed the duties of his or her office in compliance with the statutory standard of conduct or in compliance with his or her fiduciary duties. ***See Potter v. Pohlad*, 560 N.W.2d 389, 391 (Minn. Ct. App. 1997).** Moreover, the business judgment rule will typically protect corporate officers from liability for failed business deals, unless officers violate their duties of good faith, loyalty or due care; with violation of due care requiring a showing of gross negligence. The business judgment rule posits "a powerful presumption" that a court will not interfere with decisions made by a loyal and informed board. *See Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del.1993), modified, 636 A.2d 956 (Del.1994).

In ***Potter*** the trust administrator brought suit against three corporate officers for violation of fiduciary duties after the corporation was bankrupted by a failed acquisition and joint venture. As part of their fiduciary duties, corporate officers "have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them. Having become so informed, they must then act with requisite care in the discharge of their duties." *Aronson v. Lewis*, 473 A.2d 805, 812 (Del.1984). This duty of care is judged under a gross negligence standard. *Id.*; *Kahn v. Roberts*, No. C.A. 12324, 1995 WL 745056, at *4 (Del.Ch. Dec.6, 1995), aff'd sub nom. *Kahn ex. rel. DeKalb Genetics Corp. v. Roberts*, 679 A.2d 460 (Del.1996).

Officers, as agents of the corporation also have an obligation to disclose information material to the board's ability to make an informed decision regarding major acquisitions. *See Science Accessories Corp. v. Summagraphics Corp.*, 425 A.2d 957, 962 (Del.1980) (an agent has the "duty to disclose information that is relevant to the affairs of the agency entrusted to him."); *cf. Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1280 (Del.1989) (corporate directors have a duty to disclose "all material information" when seeking shareholder approval). In *Potter*, the accused directors provided affidavits attesting to their understanding of the deal prior to acquisition, and upon review the court found the officers did not violate their obligations to disclose material information to outside directors. The outside directors, all experienced businesspersons, had all the information they had requested and believed necessary to make an informed decision regarding the acquisition.

In addition to the duty to inform, directors of a corporation have a duty to act in good faith. A showing that a director acted in bad faith, will rebut the presumption of the business judgment rule. *See Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993), decision modified on re-argument, 636 A.2d 956 (Del. 1994). Bad faith is evidenced by a showing that the directors "knowingly or deliberately withheld information they knew to be material for the purpose of misleading shareholders." *Emerald Partners v. Berlin*, No. C.A. 9700, 1995 WL 600881, at *7 (Del.Ch. Sept.22, 1995). In *Potter*, the evidence provided by plaintiff did not show the MEI officers deliberately withheld information from the board members in order to mislead or deceive them.

The final charge in *Potter* was for a breach of candor. To the extent that a duty of condor exists separate from the duties of care and good faith, it entails the obligation to disclose all material information to shareholders when seeking shareholder approval. *Mills Acquisition Co.*, 559 A.2d at 1280. The court found the transaction challenged did not involve shareholder approval. Therefore, the duty of candor must be analyzed in this situation under the officer's duty of care, which plaintiff failed to demonstrate exists. Thus, the accused directors were not found personally liable for their actions taken as directors.

A director who does not act within the statutory standard or who breaches his or her fiduciary duties can be held liable, to the corporation, for the damages those actions caused. In addition, a director who votes for a dividend, distribution, or stock purchase made in violation of law or the articles of incorporation, is liable, with all other directors, to the corporation for the amount of the payment that exceeds what could have been paid without violating the law or the articles. ***See Wenzel v. Mathies*, 542 N.W.2d 634 (Minn. Ct. App. 1996)**. Corporations may eliminate or limit their directors' liability for a breach of fiduciary duty by so providing in their articles of incorporation. However, in general, they cannot eliminate or limit liability for a breach of the duty of loyalty, for acts made in bad faith or which involve intentional misconduct or a known violation of law for approving unlawful dividends, distributions or stock purchases, or for any transaction in which the director derived an improper personal benefit.

In ***Wenzel,*** an action was brought against an officer and a director in a closely held corporation for breach of fiduciary duty and self-dealings when they caused the bank to issue new stock at 44.10% less than market value to themselves and related parties. Their actions resulted in a dilution of the value of the holding company's stock, and Wenzel no longer having controlling interest in the bank. Which in turn caused Wenzel's proposed purchasers to withdraw from a pending purchase agreement as Wenzel could no longer offer controlling interest in the bank.

In a closely held corporation, the shareholders, as well as the directors and officers of the corporation, have a fiduciary relationship that imposes the highest standard of integrity and good faith. *Pedro v. Pedro*, 489 N.W.2d 798, 801 (Minn.App.1992) ("The relationship among shareholders in closely held corporations is analogous to that of partners."), review denied (Minn. Oct. 20, 1992); *Evans v. Blesi*, 345 N.W.2d 775, 779 (Minn.App.1984), review denied (Minn. June 12, 1984). "Owing a fiduciary duty includes dealing 'openly, honestly and fairly with other shareholders.'" *Id.* Here, Donohoo, a director of the bank breached his fiduciary duty to Wenzel, the pledgee and equitable owner, by engaging in self-dealings by diluting the stocks' value and ceasing control of the corporation's only asset, a bank.

Rasmussen was not an officer, but was a bank director, thus he too owed the Wenzels a fiduciary duty. Members of a corporate board owe a fiduciary duty to individual shareholders to treat them fairly and evenly. *See Schwartz v. Marien,* 37 N.Y.2d 487, 373 N.Y.S.2d 122, 125–28, 335 N.E.2d 334, 337–38 (1975); *Van Schaack Holdings, Ltd. v. Van Schaack*, 867 P.2d 892, 896–97 (Colo.1994); Oberhelman v. Barnes Inv. Corp., 236 Kan. 335, 690 P.2d 1343, 1346–47 (1984). By approving and partaking of the fruits of self-dealing transactions that change control and dilute the value of the holding company's stock, Rasmussen breached this duty.

Finally, the bank was vicariously liable for both Donohoo and Rasmussen's actions as they were found to be acting within the scope of their employment with the bank when they breached their fiduciary duty to the Wenzels. *Orwick v. Belshan*, 304 Minn. 338, 343, 231 N.W.2d 90, 94 (1975). The jury found the Bank benefitted from the infusion of capital brought by the new shares, which would not have been obtained without the actions of its employees breaching their fiduciary duties, thus the Bank was also vicariously liable.

It is the universal rule that an officer of a corporation who takes part in the commission of a tort by the corporation is personally liable therefor. *Ellingson v. World Amusement Serv. Ass'n,* 175 Minn. 563, 222 N.W. 335, 339 (1928). However, a corporate officer cannot be held personally liable for a company's defamatory acts by virtue of job title alone. 19 C.J.S. Corporations § 630 (2019). ***DeRosa v. McKenzie*****, 936 N.W.2d 342 (Minn. 2019).**

In ***DeRosa,*** an action was brought by a former member of the corporate board of directors against a corporate officer for defamation. DeRosa was accused by the board for violating the bylaws and sharing confidential information with a third party. He resigned from the board of directors, and suit was pending as to those allegations. Prior to a verdict, the Board issued a press release, at defendant's direction and with his approval, which stated, "Mr. Derosa … violated his fiduciary duties to all stockholders and committed unlawful acts by sharing material non-public information." This statement was then republished by defendant through a press release and attached to an 8-K filing with the Securities and Exchange Commission.

The court found the officer could be found personally liable for the company's defamatory acts as he "authorized and approved the defamatory publication," "had control over the publication," and "authorize[d] the republication" of the press release by attaching it to an SEC filing. Thus, he took part in the commission of the tort by the corporation, and could be personally liable therefore. *Ellingson* 175 Minn. 563 at 339.

b) Officers Liability under Minnesota Law

Corporate officers—like directors—must discharge their duties in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances, and in a manner they reasonably believe to be in the best interests of the corporation. Officers also owe duties of fidelity, honesty, good faith, and fair dealing to the corporation. An officer will not be liable for any action taken as an officer, or any failure to take any action, if the officer performed his or her duties in compliance with these standards. Officers of non-profit corporations are also afforded additional protections under Minnesota's Nonprofit Corporation Act (MNCA), Minn. Stat. § 717A.257. However, if an officer fails to perform his/her duties in in the best interest of the corporation, they may lose all protections under MNCA and can be found personally liable for a breach of those duties owed to the corporation. ***Shepherd of the Valley Lutheran Church of Hastings v. Hope Lutheran Church of Hastings,*** 626 N.W.2d 436, 439 (Minn. Ct. App. 2001).

In ***Shepherd***, Collins, while acting as the vice-president of Shepherd of the Valley Lutheran Church (SOTV), incited the majority of its member to branch from SOTV and create Hope Lutheran Church of Hasting (Hope), held secret meeting and encouraged secrecy among the members, met with an attorney and in advance to prepare legal documents to transfer SOTV's real estate and personal property (church property) to Hope without any payment of money or consideration, and denied SOTV members access to the property.

An officer of a nonprofit corporation owes a fiduciary duty to that corporation to act in good faith, with honesty in fact, with loyalty, in the best interests of the corporation, and with the care of an ordinary, prudent person under similar circumstances. Minn. Stat. § 317A.361 (2000); see also *Miller v. Miller,* 301 Minn. 207, 219, 222 N.W.2d 71, 78 (1974) (recognizing the common law principle that officers of a corporation occupy a fiduciary relationship with the corporation); *Wenzel v. Mathies*, 542 N.W.2d 634, 641 (Minn.App.1996) (same), review denied (Minn. Mar. 28, 1996). In order to establish a breach of fiduciary duty claim, a plaintiff must show that:

> the action attacked is so far opposed to the true interests of the corporation as to lead to the clear inference that no officer thus acting could have been influenced by an honest desire to secure such interests.

Westgor v. Grimm, 318 N.W.2d 56, 59 (Minn.1982) (quoting *Warner v. E.C. Warner Co.,* 226 Minn. 565, 573, 33 N.W.2d 721, 726 (1948)). As Collins was an officer of SOTV, he bore a fiduciary duty to the entire SOTV congregation, not just those who were members of the Hope faction. *See Wenzel*, 542 N.W.2d at 640 (holding that a fiduciary duty is owed to all persons who have equal interests and concerns in the corporation and are subject to harm). Holding secret meetings and advance preparation of legal documents is improper conduct by an officer, amounting to a breach of fiduciary duty. *Evans v. Blesi*, 345 N.W.2d 775, 779–80 (Minn.App.1984), review denied (Minn. June 12, 1984).

Additionally, Collins was not protected by the immunity provision of Minnesota's Nonprofit Corporation Act (MNCA), Minn. Stat. § 317A.257 (2000), as he did not act in good faith and by inciting separation of the churches Collins' actions constituted willful or reckless misconduct. The MNCA provides immunity from civil liability to unpaid directors of nonprofit organizations if the director (1) acts in good faith; (2) within the scope of his responsibilities as a director; and (3) does not commit reckless or willful misconduct. *Id.*, subd. 1; *Rehn v. Fischley*, 557 N.W.2d 328, 333 (Minn.1997). The party relying upon the immunity bears the burden of proving he or she fits within the scope of the immunity. *Rehn*, 557 N.W.2d at 333. Collins was found to have breached his fiduciary duty to SOTV and was personally liable for damages.

Former corporate officers can also be held liable for breach of fiduciary duty for actions taken while officers. ***TCI Bus. Capital, Inc. v. Five Star Am. Die Casting, LLC*, 890 N.W.2d 423, 426 (Minn. Ct. App. 2017).**

In ***TCI***, an action was brought against a former chief risk officer for breach of fiduciary duty when he falsified company records to show that a Five Star's debt to the corporation was $250,000 less than what was actually owed. As a chief risk officer defendant was entrusted with the liquidation of equipment and retention of proceeds for a Five Star's account. Rather than proceeding with normal practices, defendant arranged for the equipment to be sold through individual sales, assuming it would obtain greater proceeds than through single auction. This was done without discussing the procedure with anyone at TCI, concealed from TCI management and co-workers. Defendant then falsified company records to show that Five Star's debt was $250,000 less than what was actually owed based on doctored proceeds of the auction sale. This doctored balance was then used by TCI, without its knowledge as to falsity, to negotiate a settlement with Five Star, significantly less than what TCI would have agreed to, had it known of the true value of the outstanding debt.

In a business setting, "one entrusted with the active management of a corporation, such as an officer or director, occupies a fiduciary relationship to the corporation." *Miller v. Miller*, 301 Minn. 207, 219, 222 N.W.2d 71, 78 (1974). "An officer shall discharge the duties of an office in good faith, in a manner the officer reasonably believes to be in the best interests of the corporation, and with the care an ordinarily prudent person in a like position would exercise under similar circumstances." Minn. Stat. § 302A.361 (2016). "Corporate officers owe the corporation and its stockholders the active duty of honesty and good faith." *Seitz v. Union Brass & Metal Mfg. Co.*, 152 Minn. 460, 462, 189 N.W. 586, 587 (1922).

To prevail on a claim of breach of fiduciary duty, a plaintiff must prove four elements: duty, breach, causation, and damages. *Padco, Inc. v. Kinney & Lange*, 444 N.W.2d 889, 891 (Minn. App. 1989), review denied (Minn. Nov. 15, 1989). Here, the court determined defendant as an officer owed a duty to the corporation, breached this duty by not conducting himself in good faith and by falsifying records. The corporation relied on this deception in making its business decisions and was subsequently harmed by the deception. Thus, defendant was found personally liable to the corporation for his breach of fiduciary duty.

c) Derivative claims under Minnesota Law

As a general rule, "an individual shareholder may not assert a cause of action that belongs to the corporation." ***Blohm v. Kelly*, 765 N.W.2d 147, 151 (Minn. Ct. App. 2009)** (quoting *Northwest Racquet Swim & Health Clubs, Inc. v. Deloitte & Touche*, 535 N.W.2d 612, 617 (Minn.1995).

In ***Blohm,*** Kelly, in his capacity as director, sold all of BNK Inc's assts for $112,200.00. After paying debts to creditors and earnings to himself, Kelly issued a check to Blohm (who owned 20% of the shares) for $2,400.00, which represented 20% of the proceeds. Blohm, as a shareholder brought a claim against Kelly for breach of fiduciary duties and denying Blohm access to corporate records. A Special Litigation Committee investigated the claims and concluded there were no potential viable claims against Kelly based on the allegations, and the costs of pursuing any such claims would be significant in comparison to the potential of no recovery. Thus the SLC recommended that the company refrain from instituting any legal action against Kelly.

Under the business judgment rule, if the alleged claim is derivative, a court should defer to the determinations of a Special Litigation Committee if: (1) the members of the Special Litigation Committee possessed a disinterested independence, and (2) investigative procedures were adequate, appropriate, and pursued in good faith. *In re UnitedHealth Group Inc. S'holder Derivative Litig.*, 754 N.W.2d 544, 559 (Minn.2008).

In determining whether a claim is direct or derivative, the central inquiry is "whether the complained-of injury was an injury to the shareholder directly, or to the corporation." *Wessin v. Archives Corp.*, 592 N.W.2d 460, 464 (Minn.1999). "Where the injury is to the corporation, and only indirectly harms the shareholder, the claim must be pursued as a derivative claim." *Id*. at 464; *see also Seitz v. Michel*, 148 Minn. 80, 87, 181 N.W. 102, 105 (1921). "A shareholder derivative suit is a creation of equity in which a shareholder may, in effect, step into the corporation's shoes and seek in its right the restitution he could not demand in his own." *In re UnitedHealth* 754 N.W.2d at 550.

Corporate assets "do not belong to the stockholders, but to the corporation." *Seitz* 148 Minn. at 87, 181 N.W. at 105. Here, the alleged conduct only indirectly reduced the capital distributions to Blohm, thus, the alleged injury is primarily an injury to the corporation; derivative. *See Wessin*, 592 N.W.2d at 464; *Stocke v. Berryman*, 632 N.W.2d 242, 247 (Minn.App.2001), review denied (Minn. Sept. 25, 2001); *Skoglund v. Brady*, 541 N.W.2d 17, 21–22 (Minn.App.1995), review denied (Minn. Feb. 27, 1996). Thus, the court merely reviewed whether the SLC conducted itself independently and in good faith. Here, the parties were not in dispute that the SLC comprised of one general litigation attorney who was independent, and the court's review of the SLC report determined the procedures were "adequate, appropriate, and pursued in good faith." Thus, it was only appropriate for the court to inquire whether the SLC made itself aware of the various factors that should inform its business judgment and incorporated them into its decision making. Which it did.

5) *Sample of Minnesota Corporate Law Cases*

Bolander v. Bolander, 703 N.W.2d 529 (Minn. App. 2005).

Bruce Bolander, son of David and Dorothy Bolander became the President and COO of CB&S in 1994, for a specific term which would end in 2000. As part of his parents' plan for Bruce to take over the business, a trust was established that transferred ownership of the company to Bruce, with the provision that if Bruce stopped being an employee of CB&S, the trust would be divided equally among the three siblings. The trust also stipulated that if he was terminated "with cause", he would not entitled to bonuses and benefits. The employment agreement with Bruce Bolander and the company defined cause as "embezzlement, misappropriation of funds, and material breach". In 2000, the company began performing poorly. Bruce allegedly engaged in an oral agreement to continue in his position until 2002, and by conduct continued to serve as the COO and President until his termination. Between September 1999 and March 2000, Bruce took $194,000 in cash withdrawals from company funds, writing a promissory note to repay "the loan", but instead continued to "borrow" money from the company until he took a total of $353,000. Ultimately David Bolander informed Bruce that he would be terminated for this conduct. Two days later, on October 20, 2000, CB&S made a $6,000,000 dollar sale which would have resulted in a $780,000 bonus for Bruce under the terms of his employment contract. On October 25th, 2000 the board placed Bruce Bolander on leave and fully terminated him on November 29, 2000. Because his employment was terminated, Bruce did not receive, among other things, his expected bonus in connection with the $6,000,000 sale. Bruce Bolander sued CB&S and his parents, claiming, in part, that he was terminated without due cause and therefore was entitled to his salary, bonus, and benefits through March 31, 2002, the remainder of the extended employment term.

Procedural Posture:

Bruce Bolander brought claims of shareholder oppression, breach of contract, promissory estoppel and misrepresentation against David and Dorothy Bolander as well as CB&S. CB&S countersued claiming breach of contract and fiduciary duties, theft, receiving stolen property, and accounting and constructive trust. David and Dorothy Bolander countersued claiming that Bruce Bolander violated the Business Corporations Act, breached his fiduciary duties to the Company, and for revoking an irrevocable trust. The trial judge dismissed all of the claims except for Bruce Bolander's breach of contract claim and CB&S's breach of contract claim, granting judgment for both and awarding attorney's fees to both parties.

The court had to deal with eleven issues on appeal, ranging from jury instructions to summary judgment motions and abuse of trial court discretion. First, the court questioned the jury instructions regarding the preponderance of the evidence standard for Bruce Bolander , instructing the jury that "poor performance" does not constitute a "material breach", and the choice to not instruct the jury that "corporate officers have a fiduciary duty to act in the best interests of the company, and that, "poor performance constitutes due cause" for termination. The appellate court ruled that a preponderance standard was appropriate, as well as all jury instructions given, validating the trial courts decisions.

The court then dealt with whether there was enough extrinsic evidence to show that there was an extension of the contract. They ruled that this was an area of genuine material dispute of fact, as both parties conduct indicated an extension, but there was an absence of written or oral agreement. Additionally, the court asked whether this was subject to the statute of frauds, and found that it was not because it was a contract for more than one year.

Next, the court analyzed the issue of termination "with cause", and found that Bruce Bolander's conduct did not meet the standard of a material breach. The court then addressed the issue of awarded attorney fees, and found that it was appropriate to award them.

After that, the court analyzed the dismissal of Dorothy and David Bolander's claims under Minn. Stat. § 302A.467 and for breach of fiduciary duty. The court reversed and remanded, and decided that that trial court abused its discretion in light of Bruce Bolander's conduct.

Next, the court discussed how the trust was divided with Bruce getting larger shares than his siblings, affirming the lower court's decision in dividing the trust.

Next the court addressed Bruce Bolander's claim that the trial court erred in denying him relief under Minn. Stat. § 302A.751, affirming the lower court's decision that he undercut any rights to relief when he took funds from CB&S.

The court then turned to Bruce Bolander's dismissed motion to re-open the record, and affirmed the lower court's decision, as it was not likely to produce a different result.

Next, the court analyzed the dismissal of Bruce's motion for summary judgment rejecting his shareholder repression claim, finding that the trial court erred because there was a genuine dispute of material fact at issue.

Finally, the court affirmed the lower court's decision to award CB&S attorney fees.

In re Villa Maria, Inc., 312 N.W.2d 921 (Minn. 1981).

This case concerned the involuntary dissolution or buyout of a company based on statutory violations of Minnesota law. In 1966, John Mondati and James and John Sheehan entered an arrangement to finance and develop a nursing home and incorporated Villa Re, Inc. The Sheehans secured funds through personal guarantee loans from banks, and were named as directors, while Mondati secured financing through personal loans and served as the president. Mondati also arranged for his private pharmacy, Uptown Pharmacy, to help finance the project and provide medication for the nursing home. As part of the pre-incorporation agreement, buy out was allowed at book value. When the corporation met financial difficulties and the Sheehans became dissatisfied with their investment, Mondati refused to issue dividends and unsuccessfully attempted to buy their stock at double book value. After that, Mondati took control of the company, acting with little regard to the Sheehans' interests, ignoring their demand for a special meeting, refusing to give them financial reports, and holding no annual meetings since 1973. Mondati refused to issue dividends claiming that the company wasn't ready. Finally, Mondati had Uptown Pharmacy purchase land next to Villa Re for use by Villa Re as a parking lot, despite the fact that Villa Re had already shown interest in the property and the Sheehans were not aware that it was available. The Sheehans then sought to remove Mondati as President and dissolve the corporation. The trial court ruled in favor of the Sheehans, allowing for dissolution or a buy-out at market value.

The Appellate court faced two issues on appeal.

The first issue was whether or not forced dissolution was permitted under Minnesota Law. The court found that because Minnesota Statutes grant involuntary dissolution of corporations when "the director or those in control are guilty of an abuse of authority", that the dissolution granted by the trial court was justified, affirming the judgement.

The second issue that the court dealt with was the trial court's issuing that the buy-out order be at market value rather than the book value stipulated in the pre incorporation agreement. The court found that the statutory provisions governed, not the pre-incorporation agreement, and the trial court had the discretion to decide at which value the stock should be purchased at.

In ***Janssen v. Best & Flanagan,* 662 N.W.2d 876, 882 (Minn. 2003)**, members and trustees of a nonprofit corporation brought a derivative lawsuit against defendant, naming the corporation as a nominal defendant. A special litigation committee was formed and determined it was not in the best interest of the corporation to pursue the action. In reviewing whether the special litigation committee was independent and acted in good faith, the court determined that the committee did not have sufficient independence, as they acted more like a legal advisor than a neutral decision maker. Additionally, the investigative procedures and methodologies were not adequate for the reports relied upon were only those provided by the corporation from other lawsuits, interviews of the accused parties were not conducted, and the information relied upon was not wholly relevant to the claim at hand. Finally, the special litigation committee's proffered conclusion read more like legal advice then the findings of a disinterested decision maker. Thus, the derivative suit was able to proceed on its merits.

In ***Skoglund v. Brady*, 541 N.W.2d 17 (Minn. Ct. App. 1995)**, shareholders brought a derivative action against the board for breach of fiduciary duties, usurped corporate opportunities, corporate waste and fraud. A special litigation committee was formed to investigate the claim. The committee found although not all of the proper procedures were followed, the leases were reasonable, the bonuses were not improper, and the stocks issued were within the guidelines. Thus, they chose not to pursue the corporate waste claim due to the expense associated with the lawsuit and the probability that any damages awarded would exceed the cost of litigation. Thus, it was in the best interest of the corporation not to proceed. When reviewing whether the business judgement rule applies, the court looked to the independence of the special litigation committee, and whether it conducted the investigation in good faith. The court found it did, and as the shareholder did not allege an injury to himself that was separate and distinct from an injury to the corporation, the business judgment rule applied, and the findings of the special litigation committee holds.

In **DeRosa v. McKenzie**, 936 N.W.2d 342 ((Minn. December 11, 2019), an officer was held liable for defamation based on a press release which he authorized. In 2017, Lone Star Value Management, a substantial equity owner of Dakota Plains, appointed William DeRosa to the board of directors for Dakota Plains. Craig McKenzie, Dakota Plain's CEO took issue with DeRosa's appointment, and in February 2015, accused DeRosa of violating the company bylaws by sharing confidential information with Lone Star. At Lone star's request, DeRosa resigned. Dakota Plains brought a lawsuit in Nevada against DeRosa, accusing him of breaching his fiduciary duties.

One year later, at McKenzie's direction, assignment and approval, Dakota Plains issued a press release publicizing the lawsuit in Nevada (which was still pending), stating that "DeRosa violated his fiduciary duties to all stockholders and committed unlawful acts by sharing material non-public information. DeRosa will stand trial for his actions."

DeRosa filed a separate suit in Minnesota on claims of defamation and intentional infliction of emotional distress. The district court dismissed it for failure to state a claim.

DeRosa then amended his complaint against McKenzie for his actions in directing and publishing the press release which he, as CEO, had control over. The complaint further alleged that McKenzie knew that the press release was untrue and that it was "made with bad faith and evil motive" to "disgrace and shame" DeRosa**.**
The district court dismissed the claim because it did not state that McKenzie authored the statement. The court of appeals affirmed, stating that a corporate officer can only be responsible for defamation if he is the author.

The Supreme Court dealt with two issues on appeal.

The first issue was whether or not a corporate officer can be held liable for defamation based on a press release that they did not author. The Supreme Court held that, just like other torts, corporate officers can be held liable for the actions taken by the company if they had sufficient involvement in the process. Additionally, the court held that an officer does not need to specifically author the defamatory statement, as the district and appellate court ruled, but rather if the "corporate officer, personally took part in the commission of a tort by directing, authorizing, and approving a defamatory press release" than they could be held personally liable.

The second issue that the court addressed was whether or not the pleading was sufficient for the allegations. After discussing case law regarding Minnesota's broad pleading requirements, the court ruled that the complaint was sufficient, and remanded the case back to the district court.

***In Eq. Tr. Co. Custodian ex rel. Eisenmenger IRA v. Cole*, 766 N.W.2d 334, 339 (Minn. App. 2009),** the appellate court dealt with the district court's decision to pierce the corporate veils of several entities allegedly involved in a consumer fraud scheme.

The case arose from a consolidation of 8 separate lawsuits. Geoff and Nancy Thompson joined Josef Cole and Jim Abbot as partners in forming a program called "AMP". AMP would offer exclusive "investment opportunities" to individuals who paid the membership price to join the program. The opportunities consisted of "purchasing" properties in Miami and other locations and investors were informed that the properties were rapidly appreciating in value. In fact, no purchases were made and the transactions were fraudulent. Investors also had the opportunity to finance AMP and were told that they would receive 30- 35% returns on their investments, were guaranteed by insurance of up to 25 million dollars, and the money was never returned. The insurance policy was also fraudulent.

In 2006, 178 investors brought suit against the defendants as well as the many fraudulent corporate entities involved. The suits included claims such as breach of fiduciary duty, breach of contract, misrepresentation, conspiracy, civil theft and other violations of Minnesota statutes. The suits also alleged that the companies involved were "alter egos".

The State then intervened, based on its interest in protecting consumers from fraud and requested a temporary injunction against the defendants, as well as appointing a receiver to identify and attach assets.

The district court granted the injunction and receiver appointment. Following this, the State dismissed its claims. The receiver filed a motion to expand its receivership and include an additional three corporate entities involved in the real estate scheme.

The Thompsons attempted to have the claims dismissed for failing to state a claim and were denied by the district court.

The investors then moved for summary judgement and to pierce the corporate veil, holding the Thompsons personally responsible for AMP and the various corporate entities involved, while the Thompsons filed a cross motion for summary judgement for a dismissal of the claims, claiming that because they were not shareholders or officers in the companies, they could not be held responsible under a veil-piercing theory.

The district court denied both summary judgment motions, but granted default judgment against the corporate entities. The district court also granted the request to pierce the corporate veil of each entity to hold the Thompsons personally responsible for the default judgment against the corporations. The district court found that piercing was appropriate because the Thompsons were "listed as owners and/or officers on certain documents" and because there was "substantial evidence that [the Thompsons] held themselves out as putative owners and/or officers in communications with clients and other ... employees [of the corporate entities]."

The investors later requested that the district court pierce the corporate veil against Abbott and Cole and enter judgment against all of the principals personally for the earlier default judgment order issued against the corporate entities. The district court granted the motion and entered judgment against the principals for $22.68 million, the total amount of damages allegedly caused by the real estate investment scheme.

The Thompsons then appealed.

The Court of Appeals had to decide on three issues.

The first issue involved the appropriateness of the district court's discretion in piercing the corporate veil. The Thompsons argued that because they were not shareholders, officers, or directors, piercing the corporate veil was inappropriate. The court rejected that argument, and affirmed the district court's holding, reasoning that it is "reality and not form" that matters for veil piercing, and that the Thompsons owned the corporations in fact, even if they weren't listed as controlling shareholders.

The second issue was the district courts discretion in expanding the receivership. The Thompsons argued that because the receiver was appointed under MN statute Minn. Stat. § 8.31, subd. 3c (2006), once the state withdrew from the case, expanding the receivership was inappropriate. The Court disagreed, stating that the receivership was really authorized under a different statute, Minn. Stat. § 576.01 (2006). The court also succinctly rejected the Thompson's arguments that the receiver's attachment of $750,000 was unnecessary, that the receiver did not post bond and that the receiver went beyond the parameters by attaching money from several of the corporate entities involved. The Court held that the receiver's actions in all of the above instances were wholly appropriate, and that the receiver also did post bail.

The third issue was the denial of the Thompsons' request for summary judgement on the claims brought against them personally. The Court declined to consider this argument because no final judgment had been brought on those issues at the time of the appeal.

In ***TCI Bus. Capital, Inc. v. Five Star Am. Die Casting, LLC***, 890 N.W.2d 423 (Minn. Ct. App. January 23, 2017), the Minnesota court of appeals dealt with an officer's fraudulent activities involving wire transfers between companies.

TCI Business Capital, Inc., is a commercial financing company. It provides financing to companies and assists in the collection of accounts receivable. From September 2010 to March 2013, Brian T. Flynn was employed by TCI as its chief risk officer. In that capacity, Flynn oversaw the credit, collections, legal, and external audit functions of TCI. Flynn reported to TCI's CEO. Five Star American Die Casting, LLC, was a customer of TCI. By 2012, Five Star owed approximately $350,000 to TCI, and TCI exercised the right under the contract to seize Five Star's equipment. By September the debt had increased to approximately $450,000. The equipment was supposed to be sold at auction, with the proceeds paying off the debt. However rather than selling them at auction, Flynn decided to sell the equipment piece by piece and not inform anyone at TCI. On December 17th, 2012, Flynn credited TCI's account with approximately $250,000, claiming that it was from the proceeds of the auction, which in reality never occurred.

Flynn created an elaborate series of false transactions involving another TCI customer. Flynn created the false illusion that a customer had sent products worth $313,048 to a retailer. Flynn sent documents to the customer to indicate that TCI would purchase the receivables from them. Flynn directed TCI's finance department to wire $250,378.40 to an agent of the company, which purportedly represented the amount for which TCI would purchase the receivables. A day later, Flynn contacted the customer's agent and said that TCI's treasurer had made a mistake and that the agent should wire the money back to TCI, with a notation referring to Flynn and Five Star, and the agent did so. Flynn told employees in TCI's treasury department that the funds received from customer were the proceeds of the auction of Five Star's equipment. TCI treasury employees received a wire transfer of $250,378.40 and applied the funds to Five Star's account. The credit to Five Star's account appeared to reduce the amount of Five Star's debt to TCI in TCI's accounting system. At the same time, TCI's records showed that the customer owed the same amount to TCI, but Flynn falsified the customer's monthly reports so that the customer would be unaware that TCI was recognizing such a debt.

In September 2014, TCI brought suit against Flynn alleging claims of conversion, civil theft, fraudulent misrepresentation and breach of fiduciary duty. TCI and Flynn both moved for summary judgement, and the district court ruled in favor of Flynn in summary judgement on all claims.

On appeal, the issues were whether the district court erred in granting summary judgement on each of those claims.

The first issue was the summary judgement for Flynn on conversion. The district court ruled that the transfer of money here was not conversion because Flynn did not deprive TCI of its property and did not intend to do so. The court of appeals affirmed the ruling, stating that because Flynn's intention was to pay the money back, and he in fact did so, it did not meet the standards of conversion which require intentional interference with someone's possessory rights with the intention of depriving them of their interest in the property.

The second issue was the summary judgement for Flynn on civil theft. The district court ruled that Flynn's actions did not constitute civil theft because he did not steal anything for himself, but instead transferred money between companies. The court of appeals affirmed the ruling based on analysis of the statutory definition of the word "steals". The court reasoned that that theft requires taking another's property for the purposes of keeping it or using it. Here, Flynn returned the money, and did not intend to keep or use it.

The third issue was the summary judgement for Flynn on fraudulent misrepresentation. The district court ruled that Flynn was not liable for fraudulent misrepresentation based on a lack of: intention to induce, actual reliance, and proof of damages. The court of appeals addressed each of those subsections in turn, remanding the ruling to trial for a damages assessment. They reasoned that, based on the record, Flynn did have intention to induce, and that TCI did have reasonable reliance, and that there were actual damages suffered as a result.

The Final issue was the Breach of fiduciary duty. The district court ruled that Flynn did not breach his fiduciary duties because he believed that he was acting in TCI's best interests at the time. The court of appeals disagreed with the summary judgement ruling, citing the reasonable person standard and good faith standard, stating that by lying to a customer and falsifying records, Flynn was breaching his fiduciary duty.

In ***Augustine v. Arizant, Inc.*, 751 N.W.2d 95 (Minn. 2008)**, a CEO was awarded indemnification fees and the court ruled that his having pled guilty to a federal misdemeanor did not conclusively impact the issue of good faith. Appellant Scott Augustine was the founder and a corporate officer of respondent Augustine Medical. Appellant created a form of "Warm-Up" therapy which would be marketed to nursing homes and hospitals. As part of the financial procedures of the company, approval of Medicare coverage and reimbursement was essential to profitability. These reimbursement claims are handled by fiscal intermediaries, who partner with Medicare to handle claims in particular regions. After consultation, Appellant believed that the therapy would be reimbursed by edicare.

In November 1999, Augustine Medical learned that TriSpan Health Services, a fiscal intermediary, had determined that Warm-Up would not be reimbursed by Medicare. Appellant and other Augustine Medical representatives made a Warm-Up presentation to TriSpan in January 2000, and TriSpan subsequently notified Augustine Medical that Warm-Up would be reimbursed by Medicare. Trispan than sent letters claiming that it would not be reimbursed. Appellant was confused because the FDA had approved Warm-Up, Trispan had previously stated that it would be reimbursed, and assumed that the letter was wrong and did not inform customers of its existence. Company employees stated that the general policy became to not assume that Trispan would not reimburse, but rather that they would not mandate reimbursement.

Southern Medical Distributors, part of a sting operation created to uncover Medicare fraud, ordered Warm-Up from Augustine Medical. Augustine Medical's national sales manager, met with representatives of Southern Medical in Atlanta on August 16, 2000, but did not disclose the TriSpan letter. In a telephone conversation 5 days later, he told a Southern Medical representative that Augustine Medical did not have anything in writing from TriSpan. Appellant testified that he also spoke with Southern Medical on several other occasions and that, when Southern Medical asked him about TriSpan, he explained that TriSpan had denied coverage for Warm-Up. In a conversation with a Southern Medical representative on January 22, 2001, appellant stated that TriSpan had deemed Warm-Up investigational and had decided not to cover the product. Appellant reiterated to Southern Medical on March 1 that TriSpan had denied coverage for Warm-Up.

In 2002 the appellant resigned from the company. As part of his resignation, the company agreed to indemnify, hold harmless and pay for any acts that he committed as CEO as well as provide phantom stock.

In June 2003, the appellant, Augustine Medical and Augustine Medical's parent company, Arizant were indicted for conspiracy to defraud the United States, healthcare fraud, and mail fraud in connection with obtaining medicare reimbursement for Warm-Up. The Appellant plead guilty as part of a plea bargain to knowingly concealing the Trispan letter.

In July 2004, appellant sought indemnification form the parent company, Arizant, as per the agreement in his resignation package for the costs accrued in the federal lawsuit not yet reimbursed. Arizant denied the request, stating that the requirements for indemnification under Minnesota law were not met.

The Appellant sued in district court. Both appellant and Arizant filed motions for partial summary judgment on the issue of indemnification, which was denied. The case went to trial and the district court ruled in Appellant's favor, awarding him attorney's fees, indemnification and the phantom stock. The court of appeals reversed the awarding of attorney fees and indemnification, stating that the district court erred in not granting summary judgement on that issue, because his admission that he concealed the letter conclusively indicated that he acted in bad faith.

On appeal to the Minnesota Supreme Court, the issue was whether or not the district court erred in not granting summary judgement on the issue of indemnification. The Minnesota Supreme Court overturned the Minnesota Court of Appeals' ruling, and remanded for further proceedings. The Minnesota Supreme Court ruled that "acting in good faith", which is one of the statutory requirements for indemnification, is not precluded based on some fraudulent activity. The Minnesota Supreme Court further reasoned that there was a genuine dispute of material fact as to whether the appellant was acting in good faith and that nowhere in his guilty plea did he admit to acting in bad faith. The court further described the unusual circumstances, involving a sting operation and several high fines and punishments that would have accrued had he not pled guilty, which casts doubt on whether or not an admission of guilt is the equivalent of an admission of acting in bad faith.

6) Business Judgment Rule

In matters involving derivative lawsuits, the court must balance between the court's recognized authority of corporate directors, their need to control their own destiny, and holding those same directors accountable for their decisions by allowing shareholder derivative suits. *Stoner v. Walsh*, 772 F.Supp. 790, 796 (S.D.N.Y.1991), *see e.g. Barrett v. Southern Conn. Gas Co.*, 172 Conn. 362, 374 A.2d 1051, 1055 (1977) (remarking that " '[i]f the duties of care and loyalty which directors owe to their corporations could be enforced only in suits by the corporation, many wrongs done by directors would never be remedied' " (citation omitted)); *Brown v. Tenney*, 125 Ill.2d 348, 126 Ill.Dec. 545, 532 N.E.2d 230, 232 (1988) (stating that "[t]he derivative suit is a device to protect shareholders against abuses by the corporation, its officers and directors, and is a vehicle to ensure corporate accountability"). To balance these needs, courts established a "business judgment rule" that grants a degree of deference to the decisions of corporate directors while allowing shareholders to hold directors accountable for their decisions.

"The business judgment rule is a presumption protecting conduct by directors that can be attributed to any rational business purpose." Dennis J. Block, et al., The Business Judgment Rule: Fiduciary Duties of Corporate Directors 18 (5th ed.1998). "The one thing about the business judgment rule on which everyone agrees is that it insulates directors from liability for negligence." Robert J. Rhee, The Tort Foundation of Duty of Care and Business Judgment, 88 Notre Dame L. Rev. 1139 (2013) (citation and internal quotation marks omitted). This is because "[c]ourts are 'reluctant to interfere in the inner workings of a corporation.'" *In re Xcel Energy, Inc.*, 222 F.R.D. 603, 606 (D. Minn. 2004) (citing *Westgor v. Grimm*, 318 N.W.2d 56, 58 (Minn. 1982)). The business judgment rule essentially sets forth a standard of care for the decision makers in a business.

Under Minnesota's business judgment rule the standard of care requires that "disinterested director(s) [make] an informed business decision, in good faith, without an abuse of discretion." *F.D.I.C. v. Milbauer*, 119 F. Supp. 3d 939, 943 (D. Minn. 2015) (*Janssen v. Best & Flanagan*, 662 N.W.2d 876, 882 (Minn. 2003)). However, where shareholders believe the board has acted improperly, they may bring a derivative lawsuit. The substantive decision about whether to pursue the claims advanced in a shareholder's derivative action involves "the weighing and balancing of legal, ethical, commercial, promotional, public relations, fiscal and other factors familiar to the resolution of many if not most corporate problems." *Auerbach*, 419 N.Y.S.2d 920, 393 N.E.2d at 1002. A special litigation committee is created, made up of disinterested board members or individuals appointed by the board who are charged with informing themselves fully on the issues underlying the derivative suit and deciding whether pursuit of litigation is in the best interest of the corporation. *See, e.g., Houle v. Low*, 407 Mass. 810, 556 N.E.2d 51, 53 (1990); *Drilling v. Berman*, 589 N.W.2d 503, 505–07 (Minn.App.1999).This is true for both for profit and non-profit corporations.

To qualify for the protections under the business judgment rule, at a minimum, the board must establish that the committee acted in good faith and was sufficiently independent from the board of directors to dispassionately review the derivative lawsuit. *See, e.g., Grimes v. Donal*d, 673 A.2d 1207, 1219 (Del.1996); Houle, 556 N.E.2d at 59; *PSE & G*, 801 A.2d at 312; *Auerbach*, 419 N.Y.S.2d 920, 393 N.E.2d at 1000. If unable to do so, the derivative suit proceeds on its merits. *See, e.g., Hasan v. CleveTrust Realty Investors*, 729 F.2d 372, 380 (6th Cir.1984); *Will v. Engebretson & Co., Inc.*, 213 Cal.App.3d 1033, 1043–45, 261 Cal.Rptr. 868 (1989); *Lewis v. Fuqua*, 502 A.2d 962, 972 (Del.Ch.1985); *Davidowitz v. Edelman*, 153 Misc.2d 853, 858, 583 N.Y.S.2d 340 (Sup.Ct.1992).

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