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# U.S. SUPREME COURT TO HEAR APPEAL CONCERNING SECURITIES FRAUD PLEADING STANDARD

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The U.S. Supreme Court recently agreed to hear an appeal of a Ninth Circuit decision that could have a significant impact on future securities fraud claims nationwide.  At issue is how heavy a burden plaintiffs will bear in pleading facts to support a securities fraud complaint under the Private Securities Litigation Reform Act of 1995 (the "PSLRA").  In particular, the case addresses whether plaintiffs can plead the scienter  – or wrongful intent – element of a securities fraud claim without citing to the contents of specific internal documents that are alleged to show that a company knew its public statements were false or misleading when made.

In *Nvidia Corp. et al. v. E. Ohman J:Or Fonder AB et al.* (No. 23-970), plaintiff-investors alleged that microchip manufacturer Nvidia misled them into believing that growth in sales of the company's graphics processing units ("GPUs") came primarily from video game users.  Instead, plaintiffs alleged, those sales were being driven by use of the GPUs by cryptocurrency miners, a much more volatile market.  Once cryptocurrency prices began to drop in 2018, plaintiffs alleged, sales of the company's GPUs also fell dramatically, causing the company's share price to decline.

In their complaint, plaintiffs used expert witness analysis to contend that Nvidia's internal documents must have reflected the extent to which sales relied on cryptocurrency miners, supporting plaintiffs' contention that the company's statements downplaying sales to cryptocurrency miners were knowingly false.  But, plaintiffs did not specifically cite to or reference any particular internal company documents to support their contention. Arguing for dismissal of the complaint, Nvidia contended that plaintiffs' reliance on expert analysis to suggest what the company's documents may have stated, instead of alleging the actual contents of those documents, could not establish the pleading specificity required under the PSLRA.

The District Court for the Northern District of California initially dismissed plaintiffs' securities fraud claim against Nvidia under the PSLRA.  That court held that plaintiffs failed to sufficiently plead that defendants' statements were materially false or misleading, and that the statements were made knowingly or recklessly, given that plaintiffs' allegations relied solely on expert witness analysis and not on the actual content of underlying company documents. The district court further found that plaintiffs had not sufficiently disclosed their expert's analysis or the assumptions relied

upon with sufficient particularity to establish that they were reliable, and that plaintiffs' allegations of scienter were deficient because plaintiffs did not tie the contents of any Nvidia documents to the allegedly misleading statements to show that those statements were knowingly false or reckless.

On appeal, the Ninth Circuit reversed and resuscitated plaintiffs' complaint. The appeals court itself was split, with the two-judge majority ruling that plaintiffs adequately alleged that Nvidia had knowingly made false or misleading statements to investors in 2017 and 2018 when it repeatedly downplayed the significance of the company's sales to cryptocurrency miners. The majority found that plaintiffs' expert's assumptions were sufficiently reliable and that they were not the only foundation for plaintiffs' allegations of scienter. The dissenting judge agreed with the district court in emphasizing that the complaint failed to cite to any actual document that would have put Nvidia on notice that statements concerning GPU sales were false or misleading at the time.

Nvidia argued in its petition for Supreme Court review that the Ninth Circuit had deepened a split in the circuit courts concerning the evidence necessary to plead scienter under the PSLRA, which was enacted to deter frivolous investor lawsuits. The Second, Third, Fifth, Seventh and Tenth Circuits have held that the PSLRA requires that plaintiffs plead with particularity the actual contents of internal company documents relied upon in complaints. The First Circuit, however, and now the Ninth Circuit, has held that claims can go forward without such specific details. As an amicus curiae brief in support of Nvidia's appeal filed by a former SEC commissioner noted, these seven circuits 'courts handle approximately 86% of all securities class action cases. Given the volume of cases heard by the circuits in disagreement, Nvidia argued that this split is an issue of substantial interest to all public companies subject to U.S. securities laws.

Nvidia also argued that the Ninth Circuit decision created a second split to be resolved by the Supreme Court concerning whether expert opinion could form the basis for particularized allegations of falsity, since the Second and Fifth Circuits have ruled that expert opinion cannot meet the standard for pleading falsity. Indeed, the critical requirement of PSLRA pleading requirements, along with Rule 9(b) of the Federal Rules of Civil Procedure, is to plead specific *facts*. An expert's findings are generally referred to as opinion, not fact.

The Supreme Court's determination of these issues could resolve the split in the circuits and clarify for public companies how to respond to complaints based on expert analysis concerning what company documents likely show (rather than specific allegations of their actual contents).

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## MEET THE TEAM



**Eric Rieder**

New York

eric.rieder@bclplaw.com
+1 212 541 2057



**Chris LaRocco**

New York

chris.larocco@bclplaw.com
+1 212 541 3163



**John R. Bielema**

Atlanta

john.bielema@bclplaw.com
+1 404 572 4504