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# Ninth Circuit Rules That Biopharmaceutical Company’s Announcement of COVID-19 “Cure” Did Not Violate Securities Laws

On March 25, 2024, the Ninth Circuit Court of Appeals affirmed the dismissal of securities fraud claims against biopharmaceutical company Sorrento Therapeutics, its CEO, and vice president, based on allegedly false and misleading statements about the company’s potential COVID-19 “cure.”<sup>1</sup> In a unanimous decision, the Ninth Circuit held that Sorrento’s statements did not violate Section 10(b) of the Securities Exchange Act of 1934 or the Securities and Exchange Commission’s Rule 10b-5, because (1) the statements were not materially false or misleading when considered in their full context, and (2) the complaint failed to sufficiently plead scienter.<sup>2</sup>

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## I. Factual and Procedural Background

On May 15, 2020, Sorrento Therapeutics, a clinical-stage biopharmaceutical company that develops treatments for cancer, pain, and COVID-19, announced in a press release and to the media that Sorrento had developed an antibody known as STI-1499 to treat COVID-19.<sup>3</sup> News articles quoted Sorrento CEO and chairman Henry Ji as saying, “[w]e want to emphasize there is a cure. There is a solution that works 100 percent . . . [i]f we have the neutralizing antibody in your body, you don’t need the social distancing. You can open up a society without fear,” and “what we’ve done is identified an antibody that recognizes the COVID-19 virus and completely inhibits its binding to the specific receptor.”<sup>4</sup> A news article also quoted Sorrento’s vice president as saying, “[a]s soon as [the antibody] 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.”<sup>5</sup>

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<sup>1</sup> *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at \*7 (9th Cir. Mar. 25, 2024).

<sup>2</sup> *Id.* at \*1, \*7.

<sup>3</sup> *Id.* at \*3, n.3; *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2022 WL 22609807, at \*1,\*5–6 (S.D. Cal. Apr. 11, 2022), *aff’d sub nom.*, 2024 WL 1245342 (9th Cir. Mar. 25, 2024).

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

On the day of the announcement, Sorrento's stock traded at almost 78 times its daily average volume.<sup>6</sup> Following the announcement, Sorrento's stock price rose to a high of \$9.00 per share, which was 243.5% higher than the prior close of \$2.62.<sup>7</sup> Notwithstanding these optimistic statements and high trading volume, the antibody at the center of the potential cure was still in early preclinical testing and had not been FDA-approved or tested on humans.<sup>8</sup> In the week following Sorrento's announcement, news stories and articles from investment research firms scrutinized the company's claims that it had developed a COVID-19 cure.<sup>9</sup> On May 22, 2020, Sorrento clarified that the antibody "might be" or "potentially" could be a cure, and that it could not "cure late-stage patients."<sup>10</sup> Sorrento's stock price then dropped to \$4.67 per share by May 22, 2020.<sup>11</sup>

On May 26, 2020, Sorrento investor Andrew R. Zenoff filed a purported class action complaint in the U.S. District Court for the Southern District of California on behalf of all purchasers of Sorrento stock between May 15 and May 21, 2020, alleging violations of Section 10(b) of the Securities Exchange Act and Rule 10b-5, which prohibit material misstatements or omissions in connection with the purchase or sale of a security.<sup>12</sup> Zenoff alleged that Sorrento misled investors by falsely claiming it had developed a COVID-19 cure, in order to improve the company's stock price and financial position.<sup>13</sup> Under Section 10(b) and Rule 10b-5, Zenoff had to show that Sorrento made a material misrepresentation or omission with scienter; that there was a connection between the misrepresentation or omission and the purchase of the stock; and that he relied on the misrepresentation or omission, which caused him economic loss.<sup>14</sup>

On April 11, 2022, the district court granted Sorrento's motion to dismiss under Federal Rule of Civil Procedure 12(b)(6).<sup>15</sup> First, the district court held that Zenoff failed to plead with particularity how each of Sorrento's statements was false or misleading.<sup>16</sup> It found that Sorrento's statements were non-actionable "corporate optimism," or "puffery," and that they were not misleading when examined against the full context of the publications in which they appeared.<sup>17</sup> Second, the district court held that Zenoff failed to establish a strong inference of scienter (i.e., that Sorrento intended to deceive, manipulate, or defraud).<sup>18</sup> Zenoff attempted to allege scienter by showing that Sorrento

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<sup>6</sup> *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at 2.

<sup>7</sup> *Id.*; *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2022 WL 22609807, at \*1.

<sup>8</sup> *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at \*2,\*4; *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2022 WL 22609807, at \*1.

<sup>9</sup> *Id.*

<sup>10</sup> *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at \*2,\*6; *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2022 WL 22609807, at \*1.

<sup>11</sup> *Id.*

<sup>12</sup> *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at \*1-2; 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b-5.

<sup>13</sup> *See In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at \*3.

<sup>14</sup> *Id.* at \*4 (quoting *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 37-38 (2011)).

<sup>15</sup> *Id.* at \*3; *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2022 WL 22609807, at \*5,\*6.

<sup>16</sup> *Id.*

<sup>17</sup> *Id.* The publications in which the statements appeared disclosed that the antibody was still in preclinical testing. *Id.*

<sup>18</sup> *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at \*3-4.

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needed to raise funds to retire high-interest debt.<sup>19</sup> But the court found such “generalized assertions of motive based on potential profit” insufficient.<sup>20</sup>

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## II. Ninth Circuit’s Decision

On appeal, the Ninth Circuit affirmed, holding that (1) Sorrento’s statements were not materially false or misleading, and (2) Zenoff failed to establish the requisite strong inference of scienter.<sup>21</sup>

Sorrento’s statements were not materially false or misleading.

Under Section 10(b) and Rule 10b-5, plaintiffs must allege each materially false or misleading statement “with particularity” and explain “the reasons why [they are] misleading.”<sup>22</sup> The Ninth Circuit found that Sorrento’s statements, while “enthusiastic,” were not materially misleading when examined “in context,” because the publications in which they appeared clarified that the antibody was in early preclinical testing.<sup>23</sup> The court found that, upon a “fair reading” of the publications, Sorrento did not “promise [] an immediate 100% cure,” and that a “reasonable person reading the articles” would not believe that the antibody, “without further testing, was an immediate cure for COVID-19.”<sup>24</sup> Zenoff also attempted to utilize the fact that there is still “no cure for COVID-19” to show that Sorrento “could not, in good faith, have thought that [the antibody] was a cure.”<sup>25</sup> But the Ninth Circuit rejected this argument, finding that “many initially promising discoveries do not survive the testing required for FDA approval,” and that such “failure to survive testing is hardly evidence” that “initial enthusiasm was unwarranted or inherently false at the time.”<sup>26</sup>

Zenoff failed to show that Sorrento acted with scienter.

To sufficiently allege scienter under Section 10(b) and Rule 10b-5, plaintiffs must state “with particularity[,] facts giving rise to a strong inference that the defendant acted with the required state of mind.”<sup>27</sup> Zenoff attempted to demonstrate scienter “through the combination” of Sorrento’s CEO and vice president having access, through their “management roles,” to data concerning the antibody; the “blatant falsity” of their statements to the press; the “extremely short time period” between the statements and Sorrento’s subsequent “admission of falsity;” and Sorrento’s “dire financial situation.”<sup>28</sup>

The Ninth Circuit rejected Zenoff’s argument. First, there was no “indication or allegation” that Sorrento’s CEO and vice president had access to non-public information about the antibody through their roles. Second,

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<sup>19</sup> See *id.* at \*4; see also *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2022 WL 22609807, at \*6–7.

<sup>20</sup> See *id.*

<sup>21</sup> *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at \*1.

<sup>22</sup> *Id.* at \*3–4. Further, under Federal Rule of Civil Procedure 9(b), a party must “state with particularity the circumstances constituting fraud or mistake,” even though “[m]alice, intent, knowledge, and other conditions of a person’s mind may be alleged generally.” See also *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2022 WL 22609807, at \*3 (“In other words, the complaint must set forth what is false or misleading about a statement, and why it is false.”).

<sup>23</sup> *In re Sorrento Therapeutics, Inc. Sec. Litig.*, 2024 WL 1245342, at \*5.

<sup>24</sup> *Id.*

<sup>25</sup> *Id.*

<sup>26</sup> *Id.*

<sup>27</sup> *Id.*, at \*4.

<sup>28</sup> *Id.* at \*5.

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Sorrento's statements were not false when viewed in context, and later clarifications by Sorrento were "consistent elaborations of what was initially stated" rather than an "admission of falsity."<sup>29</sup> Third, even if Sorrento's financial position benefited from the announcement of the development of the antibody, Zenoff "identifie[d] no individual stock sales at all," and thus failed to make the "requisite showing of trading history necessary to raise an inference of scienter."<sup>30</sup>

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### III. Conclusion

*In re Sorrento* may encourage more defendants in the Ninth Circuit and elsewhere to assert "puffery" defenses in securities fraud cases, particularly in those involving optimistic statements about new, breakthrough drugs that are still to be tested. The Ninth Circuit's decision also reaffirms that courts must examine statements in their full context to assess their falsity and to distinguish between enthusiasm and falsehood.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email authors John MacGregor (Partner) at 212.701.3445 or [jmacgregor@cahill.com](mailto:jmacgregor@cahill.com); Jason Rozbruch (Associate) at 212.701.3750 or [jrozbruch@cahill.com](mailto:jrozbruch@cahill.com); or Ryan M. Maloney (associate) at 212.701.3269 or [ryan.maloney@cahill.com](mailto:ryan.maloney@cahill.com); or email [publicationscommittee@cahill.com](mailto:publicationscommittee@cahill.com).

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<sup>29</sup> *Id.* at \*6.

<sup>30</sup> *Id.* at \*6–7.

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