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RESEARCH

In Length of Time to Settlement in Securities Class Actions, the Pandemic's Fingerprint Lingers

Among last year's settlements, the median time from when a case was filed to a settlement hearing date was 3.7 years, the second-highest for any year in Cornerstone Research records going back to 1996.

March 06, 2024 at 07:30 AM



Ross Todd
Editor/columnist



Back at the onset of the pandemic, there was lots of speculation about how court closures would affect settlement dynamics.

Would plaintiffs be cash-strapped and willing to cut deals?

Without a trial date to motivate defendants to come to the table, would they and their counsel be happy to let the clock run?

Well, at least in the world of securities class action litigation, it looks like we're starting to get some answers to those questions. Economic and financial consulting firm Cornerstone Research released their annual review of securities class action settlements. From looking at the latest data, it appears the securities plaintiffs bar, at least, has been patient with cases that have lingered longer than usual and that's yielded some larger settlements.

According to Cornerstone, there were 83 class action settlements with a total value of about \$3.9 billion last year—both numbers down from the 105 settlements that totaled about \$4.0 billion in 2022. But the median settlement amount last year, \$15 million, was the highest number since 2010 and marked an 11% increase from 2022. The average settlement amount, \$47.5 million, was up by 25% year-over-year, buffered by nine mega-settlements of more than \$100 million or more, the most in any year since 2016.

But here's where last year was even more of an outlier: The median duration from the filing of a case to the settlement hearing date reached 3.7 years, up nearly 17% year-over-year. According to Cornerstone's records, which go back to 1996, the elapsed time to settlement reached this level in only one other year, 2006.

Big cases. A longer time to settlement. One might think that would mean more work for all the lawyers involved. But that wasn't necessarily the case. The median number of docket entries, which could be viewed as a proxy of the amount of complexity or legal work in a given case, ticked up only slightly from 138 entries in cases settled in 2022 to 142 in cases settled in 2023. Here's how the report's authors, Cornerstone Research principal Laarni Bulan and senior advisor Laura Simmons summed up that point:

Longer times to reach a settlement and more advanced litigation stages are also typically correlated with greater case activity, as measured by the number of entries on the court dockets. Surprisingly, the median number of docket entries increased only slightly compared to 2022. This, and the fact that over 80% of cases settled in 2023 had been filed by the end of 2020, suggests that the lengthened time to settlement can potentially be explained by delays related to the COVID-19 pandemic.

They say “can potentially be explained.” I’m going to go ahead and say it’s likely.

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Lyft's Earnings Gaffe Draws Investor Suit Over 46-Minute 'Fraud'

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March 5, 2024, 4:51 PM PST

Rachel Graf

Bloomberg News

Lyft Inc. may want to move on from last month's earnings gaffe, but a shareholder is making a federal case out of it.

On Tuesday, an investor filed a proposed class-action securities suit over the typo in a Feb. 13 company press release that caused the stock to briefly surge 67% in after-hours trading.

Read More: A 'Clerical Error' in Lyft Outlook Triggered 67% Jump

The complaint filed in San Francisco federal court alleges the ride-share company defrauded investors when it mistakenly said it expected adjusted earnings margins, calculated as a percentage of bookings, to expand by 500 basis points — when it was actually 50 basis points.

The gaffe was corrected within an hour and attributed to a "clerical error," but shareholder Yuan Chen claims he bought 20,000 shares during the 46 minutes that the stock traded at "artificially inflated" prices.

"To company insiders who were responsible for ensuring the accuracy of the press release and supplemental data, the misrepresentation was so apparent that it went beyond mere negligence, and amounted to a reckless indifference to the truth," Chen's lawyers wrote in the complaint.

Lyft didn't acknowledge the mistake until an analyst asked Chief Financial Officer **Erin Brewer** about it 24 minutes into the quarterly earnings call, according to the complaint. The delay in correcting the statement "is corroborating evidence that the initial misstatement was either knowing or severely reckless," according to the complaint.

In an interview with Bloomberg Television the day after the earnings report, Lyft Chief Executive Officer **David Risher** took responsibility for the error and claimed it was corrected “within seconds of finding it.”

WATCH: (Feb. 14) Lyft CEO David Risher says “my bad” on a clerical error in the company’s fourth-quarter earnings, and discusses a strike by drivers and not focusing on whether or not the company is a takeover target.

Source: Bloomberg

Both Brewer and Risher were named as defendants in Chen’s complaint. Chen is seeking unspecified damages for the losses he and other shareholders suffered.

Representatives of Lyft didn’t immediately respond to a request for comment.

The case is Chen v. Lyft, Inc., 24-cv-01330, US District Court, Northern District of California (San Francisco).

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March 5, 2024, 5:19 PM PST

Calpers Looks to Outsiders, Compiles Short List for New CIO (1)

By Eliyahu Kamisher, Dawn Lim and Marion Halftermeyer

- Pension's short list includes Lacera CIO Jonathan Grabel
- Previous CIO Nicole Musicco left after less than two years

Bloomberg Law News 2024-03-06T10:58:4362910865-05:00

Calpers Looks to Outsiders, Compiles Short List for New CIO (1)

By Eliyahu Kamisher, Dawn Lim and Marion Halftermeyer2024-03-05T20:19:32849-05:00

- Pension's short list includes Lacera CIO Jonathan Grabel
- Previous CIO Nicole Musicco left after less than two years

The largest US public pension fund is looking externally for its next chief investment officer, following a long spell of lackluster returns and leadership churn.

The short list of candidates to run the California Public Employees' Retirement System's roughly \$490 billion portfolio includes **Jonathan Grabel**, CIO of the Los Angeles County Employees Retirement Association, according to people familiar with the matter.

He's among the final four candidates — all of them from outside the pension fund — being considered to run the portfolio, one of the people said.



Marcie Frost

Photographer: Michaela Vatcheva/Bloomberg

The short list doesn't include interim CIO **Dan Bienvenue**, a 20-year Calpers veteran. Bienvenue told acquaintances he decided not to make a bid for the job after being passed over in two past CIO search rounds, according to some of the people. Calpers plans to announce its choice by the end of the month, said spokesperson **Brad Pacheco**.

Whoever takes over will lead a team of about 370 people on a high-pressure quest to meet the chronically underfunded pension's annualized return target of 6.8%, while also navigating political tensions and intense public scrutiny.

The last person to hold the post was **Nicole Musicco**. Calpers announced her departure in September, less than two years after she took over as the pension's fourth CIO since 2009.

"I don't know that there are any other seats on any US company or US public pension plan that have the same transparency and visibility," Calpers CEO **Marcie Frost** said in an interview last year. "And some people don't know if they're wired for it — or they think they're wired for it — until they actually sit in the seat."

Calpers declined to comment. Grabel didn't respond to requests for comment.

Proactive Board

Last week, the entire board participated in the second and final interviews. The session, which included post-interview deliberations, lasted more than 10 hours.

After the successive CIO resignations, the 12 members of the board are taking a proactive role in the selection process, according to people familiar with the matter. Board members called on Calpers staff and its executive search firm, Dore Partnership, to make sure they sought diverse candidates and gave applicants a clear-eyed view of the pension's political environment.

While an outsider can bring fresh perspective, any newcomer faces a steep learning curve navigating the interests of the Service Employees International Union, climate activists and lawmakers.

"We need to be up front that whoever is going to be successful in our CIO role has to understand the politics," **Lisa Middleton**, a Palm Springs city council member, said during a meeting last year.

Frost and five board members spent two full days in January interviewing eight candidates, according to documents posted by the board and obtained through a public records request. The committee narrowed it to five candidates, one of whom dropped out, one person said.

Calpers, which manages money for more than 2 million retired police, firefighters and public services employees, has only 72% of the assets it needs to pay for future benefits owed. That means the stakes are high for the next CIO to meet its return target. If it falls short, municipalities across California could be forced to make up the difference and even cut services to meet obligations.

Calpers gained 5.8% for the fiscal year ended in June. Over the most recent five-year period, the fund ranked in the bottom 90th percentile when compared to peers tracked by Wilshire Trust Universe Comparison Service, and its 10-year record is in the bottom 84th percentile.

The new chief would have to get a handle on a portfolio that has grown more complex through management changes and an aggressive expansion into private equity and private credit. At Lacera, Grabel opened the fund's private equity co-investment strategy to a larger pool of managers to access more deal flow.

The interviews are in part a redo for Grabel, who was a finalist during Calpers' 2018 recruiting process, according to a person familiar with the matter. Grabel is experienced in navigating an often politicized role that's equal parts investment expertise and catering to diverse public opinions, having spent six years at two state pension funds with city council members and law enforcement officers on their boards.

"We're looking for someone with experience dealing with labor interests, employer interests and someone not coming out of the corporate world," said Terry Brennand, director of revenue, budgets and pensions at SEIU, California's largest union, which closely monitors Calpers' policies. "We've been assured that all the candidates meet that."

(Updates with date of prior CIO's departure in sixth paragraph.)

Health insurers slam renewed \$185 million fee bid by Quinn Emanuel

 [reuters.com/legal/legalindustry/health-insurers-slam-renewed-185-million-fee-bid-by-quinn-emanuel-2024-03-06](https://www.reuters.com/legal/legalindustry/health-insurers-slam-renewed-185-million-fee-bid-by-quinn-emanuel-2024-03-06)

Mike Scarcella

The corporate logo of the UnitedHealth Group appears on the side of one of their office buildings in Santa Ana, California, U.S., April 13, 2020. REUTERS/Mike Blake Purchase Licensing Rights , opens new tab

March 6 (Reuters) - A group of U.S. health insurers have asked a judge to deny a renewed request from law firm Quinn Emanuel Urquhart & Sullivan for \$185 million in class action legal fees, calling the demand “indefensible” after an appeals court last year struck it down.

UnitedHealthcare Inc and Kaiser Foundation Health Plan Inc made their objection to Quinn Emanuel's requested legal fee in a filing , opens new tab on Tuesday in the U.S. Court of Federal Claims in Washington, D.C.

Quinn Emanuel secured a \$3.7 billion class action judgment for private insurers in 2020 over claims that the U.S. government failed to meet its obligations under an Obamacare provision aimed at encouraging medical coverage to uninsured Americans.

An appeals court last year struck down the \$185 million in fees initially awarded to the firm, ruling that the lower court should conduct a new analysis of the amount in relation to the hours the lawyers invested. Now Quinn Emanuel and objectors — led by UnitedHealth and Kaiser — are clashing over whether a lower amount should be awarded.

Quinn Emanuel, UnitedHealthcare and Kaiser did not immediately respond to requests for comment.

The 900-lawyer Quinn Emanuel has defended the \$185 million award as appropriate for the “substantial risk” it took on and 10,000 hours it expended on the case.

UnitedHealth and Kaiser on Tuesday told the court that Quinn Emanuel used “inflated and unproven hours” to justify its request. The insurers said Quinn Emanuel should be awarded between about \$11 million and \$23 million.

“10,000 hours is a staggeringly high number of hours under the circumstances, and the objectors reasonably wonder — as should the court — how class counsel could have possibly spent so many hours on this case,” the insurers wrote.

Quinn Emanuel has said it already distributed the \$185 million award within the firm.

It had an insurance policy on the award that required it to “prosecute its interests in the attorney’s fee dispute, vigorously, in good faith, and with the same zeal as if no insurance were in place,” court documents show.

The insurers said the insurance policy “essentially forecloses” Quinn Emanuel from seeking a “reasonable” award.

“If it did so, class counsel would face the risk that its insurers would claim that it had jeopardized its insurance coverage by not ‘vigorously prosecuting’ the award,” the insurers said.

The case is Health Republic Insurance Co v United States, U.S. Court of Federal Claims, No. 1:16-cv-00259-KCD.

For Health Republic: Adam Wolfson and Andrew Schapiro of Quinn Emanuel

For Class Objectors: Moe Keshavarzi of Sheppard Mullin

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Read more:

Quinn Emanuel beats bid for accounting disclosure in \$185 mln fee award fight
U.S. appeals court tosses \$185 million Quinn Emanuel fee award in Obamacare case
U.S. appeals court questions \$185 mln award to law firm Quinn Emanuel
Reporting by Mike Scarcella

Bayer notches more wins in Roundup weedkiller cancer trials

[reuters.com/legal/bayer-notches-more-wins-roundup-weedkiller-cancer-trials-2024-03-06](https://www.reuters.com/legal/bayer-notches-more-wins-roundup-weedkiller-cancer-trials-2024-03-06)

Brendan Pierson

Roundup's list of ingredients, including Glyphosate, is seen on a bottle set for sale in a store in Manhattan, New York City, U.S., June 30, 2022. REUTERS/Andrew Kelly/File Photo
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March 5 (Reuters) - Bayer (BAYGn.DE) , opens new tab on Tuesday said it won a trial in a lawsuit brought by a retired postal service worker in Pennsylvania who alleged he developed non-Hodgkins lymphoma from using the company's Roundup weedkiller.

In addition to the jury verdict in the Philadelphia Court of Common Pleas, Bayer said a California farmer, who said he contracted the same type of cancer from exposure to the product, and his wife on Tuesday voluntarily dropped their lawsuit while a trial was underway in the in state court in Sonoma County, California.

"We continue to stand behind the safety of Roundup and will confidently defend the safety of our products and our good faith actions in any future litigation," Bayer said in a statement.

Scott Love, a lawyer for Carl Kline, the plaintiff in the Pennsylvania case, said the jury had not been allowed to hear key evidence, including a finding by a World Health Organization body that glyphosate, Roundup's active ingredient, was likely capable of causing cancer.

A lawyer for the California plaintiffs, Michael and Bobbie Meyer, did not immediately respond to requests for comment. It was not immediately clear why the Meyers dropped their case.

Tuesday's victories come on the heels of another trial win for the company in Arkansas on Friday. Bayer has now prevailed in 13 of the last 20 Roundup trials, while plaintiffs have scored large verdicts totaling more than \$4 billion, including \$2.25 billion in a single case in January.

The company is appealing its trial losses, which include large punitive damages awards that are likely to be reduced because they exceed U.S. Supreme Court guidance.

Around 165,000 claims have been brought in the U.S. against Bayer over Roundup, which the company acquired as part of its \$63 billion purchase of U.S. agrochemical company Monsanto in 2018. Many were resolved as part of a \$9.6 billion settlement in 2020, but about 54,000 remain.

Bayer CEO Bill Anderson told investors in a call on Tuesday that he was "considering every possible means to bring closure" to the litigation, including solutions "outside the courtroom,"

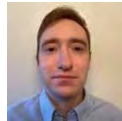
though he did not offer details.

The company phased out sales of glyphosate products for home use last year, though it still sells other formulations under the Roundup name.

Reporting By Brendan Pierson in New York, Editing by Alexia Garamfalvi and Bill Berkrot

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Brendan Pierson
Thomson Reuters

Brendan Pierson reports on product liability litigation and on all areas of health care law. He can be reached at brendan.pierson@thomsonreuters.com.

Stanley cups maker taps Arnold & Porter as defense counsel in lawsuits over lead

[reuters.com/legal/litigation/stanley-cups-maker-taps-arnold-porter-defense-counsel-lawsuits-over-lead-2024-03-05](https://www.reuters.com/legal/litigation/stanley-cups-maker-taps-arnold-porter-defense-counsel-lawsuits-over-lead-2024-03-05)

Diana Jones

Signage is seen outside of the law firm Arnold & Porter at their legal offices in Washington, D.C., U.S., May 10, 2021. REUTERS/Andrew Kelly Purchase Licensing Rights  , opens new tab

March 5 (Reuters) - The maker of the popular Stanley cups has hired U.S. law firm Arnold & Porter Kaye Scholer as defense counsel in several federal lawsuits that accuse the company of failing to tell customers it uses lead to seal the cups while marketing them as part of a healthy lifestyle, court filings show.

Complex litigation partners James Speyer and E. Alex Beroukhim are representing Seattle-based Pacific Market International, Stanley's parent company. Speyer has represented retailers like Kohl's Department Stores and 7-Eleven, according to the firm.

Neither Speyer nor Beroukhim immediately responded to requests for comment, nor did representatives for the firm. Representatives at Pacific Market did not respond immediately to a request for comment.

The Stanley cups, formally known as the Stanley Quencher cups, retail for between \$35 and \$50. Recent sales of the cups, driven largely by social media, propelled the 100-year-old, privately held Stanley brand to a 10-fold increase of \$750 million in revenue last year, according to CNBC in December.

Court records show at least five proposed class actions are pending in federal courts in Washington, California and North Carolina, claiming Pacific Market International misled consumers by failing to disclose the cups contain lead, a toxic substance. The first lawsuit was filed Feb. 1 in state court in California. Pacific Market has since moved the case to federal court.

The company has acknowledged in a statement posted on its website that there is lead present in the seal for the cup's vacuum insulation, but it said "no lead is present on the surface of any Stanley product that comes into contact with the consumer nor the contents of the product."

The plaintiffs claim that they would not have purchased the cups had they known that the cups contained lead, arguing that they could have been exposed to the metal. They do not allege that they ingested lead.

The lawsuits seek monetary damages and injunctions barring Stanley from using lead in the cups, among other things.

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Diana Novak Jones

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Co-author of the Daily Docket, Reuters' daily legal industry newsletter. Diana reports on litigation, mass torts and the plaintiffs' bar. She previously worked at Law360 and the Chicago Sun-Times.

Judge trims shepherd wage class action against US ranch companies

 [reuters.com/legal/litigation/judge-trims-shepherd-wage-class-action-against-us-ranch-companies-2024-03-05](https://www.reuters.com/legal/litigation/judge-trims-shepherd-wage-class-action-against-us-ranch-companies-2024-03-05)

Mike Scarcella

REUTERS/Andres Stapff Purchase Licensing Rights , opens new tab

March 5 (Reuters) - A federal judge has dismissed part of a class-action lawsuit accusing ranching companies of conspiring with a trade association to artificially suppress wages for shepherders in the western United States.

Chief U.S. District Judge Miranda Du in Las Vegas ruled on Monday , opens new tab that the plaintiff, a Peruvian citizen who was temporarily working as a herder in Nevada in 2020, had not alleged enough information to support a wage-fixing conspiracy for now against the ranchers.

The proposed class-action lawsuit, originally filed in 2022, accused the trade group Western Range Association of violating antitrust law by fixing wages and conspiring with the ranching companies to restrict herders from freely seeking work at other ranches.

Du on Monday dismissed the plaintiff's claims against Borda Land & Sheep Company, Ellison Ranching Company, Faulkner Land and Livestock Company, and several other ranching companies, leaving Western Range Association as the lone defendant.

The judge said "more specific factual allegations are required to plausibly allege that these specific ranch defendants entered into any such agreement." An association's members are not automatically liable for alleged antitrust violations by the association, the ruling said.

Lawyers for the plaintiff and the ranching companies did not immediately respond to requests for comment. They have denied any wrongdoing.

Du said the plaintiff can amend their lawsuit and refile it within 30 days.

The shepherd who filed the lawsuit was employed in the United States on a temporary H-2A visa for agricultural guest workers. The U.S. Labor Department administers the visa program.

The shepherd's case is among a wave of others in recent years accusing employers of labor-related violations of U.S. antitrust law.

Other lawsuits have been filed against aerospace engineering firms, asset and wealth management companies and major shipbuilders.

Law firm blasts L'Occitane case challenging mass arbitration claims

 [reuters.com/legal/litigation/law-firm-blasts-loccitane-case-challenging-mass-arbitration-claims-2024-03-05](https://www.reuters.com/legal/litigation/law-firm-blasts-loccitane-case-challenging-mass-arbitration-claims-2024-03-05)

David Thomas

A view of L'Occitane en Provence logo in Paris, France, August 10, 2023.

REUTERS/Stephanie Lecocq Purchase Licensing Rights , opens new tab

March 5 (Reuters) - Plaintiffs' law firm Zimmerman Reed has asked a U.S. judge to dismiss a lawsuit against it by France's L'Occitane, claiming the skincare company "fabricated" conspiracy allegations and improperly invoked an anti-wiretapping law in a bid to escape thousands of consumer arbitration claims.

"There is no factual or legal basis for L'Occitane's claim, and it should be denied without leave to amend," the law firm told , opens new tab U.S. District Judge Percy Anderson in Los Angeles.

L'Occitane sued Zimmerman Reed last month, claiming the law firm was "manufacturing" mass arbitration claims against it under the California Invasion of Privacy Act by having people visit the company's website and claim their privacy was violated by third-party tracking software.

The lawsuit seeks an injunction against the firm and an order that would declare parts of CIPA unconstitutional. The California law prohibits covertly eavesdropping or recording telephone conversations and includes a private right of action.

The law firm also separately asked , opens new tab for L'Occitane's lawsuit to be sent to arbitration, alleging that the skincare company is breaking its own terms of use by pursuing its claims in federal court.

Attorneys for L'Occitane and Zimmerman Reed did not respond to requests for comment.

L'Occitane's lawsuit said Zimmerman Reed had threatened that it represented 3,100 users of the company's website and had filed more than 100 arbitration claims with the American Arbitration Association, all alleging claims under CIPA. L'Occitane said it received letters from Zimmerman Reed and AAA to pay more than \$45,000 in total for fees relating to the arbitration claims.

Website operators have been flooded with CIPA claims that they are "wiretapping" their own websites by using third-party tracking software, like Google Analytics, following a 2022 9th Circuit U.S. Court of Appeals ruling, L'Occitane alleged.

That ruling held that CIPA "applies to Internet communications," and anyone who accesses such communication "without the consent of all parties" can be held liable.

The case is L'Occitane Inc. v. Zimmerman Reed LLP, U.S. District Court for the Central District of California, 2:24-cv-01103.

For L'Occitane: Allan Anderson, Adam Bowser and Andrea Gumushian of ArentFox Schiff

For Zimmerman Reed: Chase Scolnick, Jennifer Keller and Jay Barron of Keller/Anderle; and Caleb Marker and Jeff Westerman of Zimmerman Reed

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Reporting by David Thomas

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California Supreme Court Wrestles With COVID Insurance Coverage Questions

During oral arguments, the justices asked repeatedly why COVID-19 business losses should be covered by commercial property insurance policies.

March 05, 2024 at 05:43 PM

COVID-19



Cheryl Miller



California Supreme Court justices on Tuesday repeatedly pressed counsel for a concert production company to explain how the COVID-19 virus directly caused property damage covered by its insurance policy.

During oral arguments in a case closely watched by insurers, retailers and even professional sports teams, the justices appeared unpersuaded by arguments that the pandemic spread of SARS-CoV-2 and the resulting stay-at-home orders that shuttered venues temporarily were comparable to mold, asbestos or water damage.

“Unlike asbestos, which ... is part of the property and requires remediation and will persist because it’s an inanimate, enduring substance that if not remediated will simply persist and cause harm, that’s not what we have here,” said Justice Goodwin Liu.

Kirk Pasich of Pasich, who argued on behalf of Another Planet Entertainment, said that just as if he had poured super glue on the courtroom lectern, any reasonable person would agree that a surface contaminated with the COVID virus had been altered.

“We have to talk about what direct physical loss or damage means,” Pasich said. “And I think when we look at the policy language, first of all, there’s no requirement for it to be visible to the naked eye. So if we could demonstrate a molecular alteration, I think that would suffice.”

Pasich told the justices on Tuesday that Another Planet had not been able to introduce scientific evidence about the COVID virus’s impact on physical property because of its early loss on a motion to dismiss.

Another Planet, which operates the Greek Theatre, the Bill Graham Civic Auditorium and five other concert venues, sued Vigilant Insurance Co. for breach of contract, bad faith and fraud for refusing to cover the operator’s business losses when health officials ordered businesses closed during the pandemic. In June 2021, U.S. District Judge Vince Chhabria of California’s Northern District dismissed Another Planet’s case, finding that the closure orders and not the potential presence of the virus halted its business.

Another Planet appealed, and in December 2022 the U.S. Court of Appeals for the Ninth Circuit [certified](#) a question to the California Supreme Court: Does the actual or potential presence of COVID-19 on an insured’s property constitute direct physical loss or damage triggering insurance coverage?

That issue has attracted amicus briefs from insurance companies and their trade organizations as well as Major League Baseball, the Los Angeles Lakers, Ross Stores Inc. and other businesses suing their insurers for failing to pay pandemic-related income-loss claims.

O’Melveny & Myers partner Jonathan Hacker, representing Vigilant Insurance, said no one doubts that Another Planet suffered financially when it could not host concerts due to COVID restrictions.

“But our insurance policy does not insure against the diminished ability to use, does not insure particular uses of property,” Hacker said. “It insures against damage to property.”

The Supreme Court is expected to render its decision in *Another Planet Entertainment v. Vigilant Insurance* within 90 days.

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EXCLUSIVE FINANCE

New York Community Bancorp Seeks Cash Infusion

Struggling lender has contacted investment firms on potential equity raise

By [Justin Baer](#) [Follow](#) and [Gina Heeb](#) [Follow](#)

Updated March 6, 2024 11:57 am ET



NYCB has been in crisis mode since the bank in January revealed signs of trouble in its commercial real-estate books. PHOTO: BING GUAN/BLOOMBERG NEWS

New York Community Bancorp **NYCB -32.30% ▼** is seeking to raise equity capital in a bid to shore up confidence in the troubled regional lender.

NYCB, buffeted by fears over potential real-estate loan losses, weaknesses in its internal controls and a sharp drop in its stock price, has dispatched bankers to gauge investors' interest in buying stock in the company, people familiar with the matter said.

There's no guarantee there will be a deal, or that one would succeed in addressing the bank's challenges, which as of Wednesday morning had led to a roughly 70% decline in its stock price since January.

NYCB has been in crisis mode since the bank in January revealed signs of trouble in its commercial real-estate books, saying it swung to a loss in the fourth quarter and slashed its dividend. Then last week, the bank disclosed that it had found “material weaknesses” in the way it assesses and monitors loans. The disclosures have triggered several credit downgrades.

The bank’s woes have touched off concerns of another banking crisis after three regional lenders collapsed roughly a year ago.

Of particular concern to investors is NYCB’s concentration in loans for rent-stabilized buildings in New York City. That market that has struggled with rising interest rates and the aftermath of a 2019 law that capped how much landlords can increase rent on some units. Roughly half of NYCB’s portfolio of loans on multifamily residential properties is subject to rent regulations.

NYCB has sought to reassure investors over the past month, overhauling its management and saying in early February that its deposits were stable.

Newly appointed executive chairman Alessandro DiNello took over as CEO last week, replacing Thomas Cangemi. DiNello previously ran Flagstar Bank, which NYCB acquired in late 2022. The bank also named new chief risk and audit officers Friday. Two of its board members have left.

Last month, DiNello laid out a series of options the bank could explore to bolster its balance sheet, including selling assets from certain noncore businesses. The bank has also considered turning to newfangled financial instruments that would share the risks of those loans with outside investors, people familiar with the matter said.

Finding takers for those assets, at least at prices that would make a deal worthwhile, has been challenging, and U.S. officials have expressed reservations with banks pursuing credit-risk transfers that would shift the burden of potential losses to entities outside of the regulated banking system.

Moody’s Investors Service and Fitch Ratings have both downgraded New York Community’s credit ratings to below investment grade.

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Matt Levine's Money Stuff: Elon Musk Wanted Control, Not Charity

By Matt Levine
Opinion

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Matt Levine's Money Stuff: Elon Musk Wanted Control, Not Charity

By Matt Levine 2024-03-06T13:51:42763-05:00

OpenAI

Here is a partial list of things that Elon Musk has thought are the most important things in the world:

- 1. "Solving the environment," by building electric cars at Tesla.
- 2. Making humanity a "multi-planet species," by building spaceships at SpaceX.
- 3. Buying Twitter to prevent the "corrosive effect on civilization" of San Francisco's "mind virus."

I want to make a few points about this list. First: It's a fine list? Stopping climate change, colonizing space, and changing public discourse are all reasonable things to prioritize. There are tech founders who are like "I wanted to solve the problem that sometimes when I order food delivery, it arrives cold"; Elon Musk is not a founder like that.

Second: He has made a lot of progress on these problems. Tesla revolutionized electric cars; SpaceX revolutionized space; I personally do not care for the effect that Musk has had on the conversation at Twitter (now X), but he sure has had an effect, and I assume *he's* happy with it. As a founder of companies intended to solve big problems, Elon Musk has been quite effective.

This is obvious stuff. "Elon Musk tackles big problems and is unusually good at solving them" is just conventional wisdom, which is why there are glowing biographies written about him and some days he's the richest person in the world. The main way to get really rich is by solving big problems successfully.

And that's the third point that I want to make about this list: When Elon Musk has looked around and identified a big problem and set about trying to solve it, he has done so by founding (or acquiring) a for-profit company that he owns and controls. This is not the only way to (try to) solve big problems. Bill Gates, for instance, got very rich by selling software and then decided to improve the world by donating a lot of money to charitable works. Or various billionaires try to improve the world by supporting politicians who they think will do good things. Musk has dabbled in these approaches, but mostly they are not his preference. "Most philanthropy was bulls—," Musk told Gates" once, arguing that Tesla did more good for the world than most charities.

And this too is a pretty common view. It is not the only view – a lot of people think that philanthropy is good! – but in Silicon Valley tech circles it is fairly conventional to think that startups are a better way to improve the world than charity, that startups can be more ambitious, more focused on results, have a better alignment of interests and more motivated employees, and can raise and deploy a lot more money than charities. “Technological innovation in a market system is inherently philanthropic,” wrote Marc Andreessen last year, in a “Techno-Optimist Manifesto” laying out this view.

Now, I don’t think that Musk thinks that *all* profit-seeking companies, or *all* tech startups, are good; he criticizes lots of them, and had to go and buy Twitter because its previous management upset him. I just think that he thinks the best way to improve the world is generally through a for-profit company *that he runs*. And even *this* view – “the highest form of philanthropy is a for-profit company run specifically by Elon Musk” – is pretty widespread. Larry Page has mused about leaving his fortune to Musk, because Musk’s for-profit businesses are more philanthropic than any philanthropies he can think of.

Last week Musk sued OpenAI, arguing that it was founded as a nonprofit organization to build artificial intelligence for the benefit of humanity, that he was a big donor to that nonprofit, and that it has turned into a for-profit company in violation of a supposed agreement not to. What I find strangest about all this is that OpenAI was a nonprofit to begin with: Its founders, people like Musk and Sam Altman, are generally leading proponents and examples of the idea that the best way to do good in the world is with a for-profit tech startup.

At some level I can understand why artificial intelligence is different from electric cars or rockets or social networking: Powerful artificial intelligence could potentially put humans out of work, enslave us, kill us, etc.; Altman has said that AI is “probably the greatest threat to the continued existence of humanity,” terrific. Building AI that enriches its owners but immiserates everyone else would be bad. Still, all of the advantages of startups kind of remain true about AI. People might be more motivated to build AI if it will enrich them than if it won’t. It was always an odd fit for Altman and Musk to start a nonprofit together, an awkward choice to jam tech startup ideas and methods into a nonprofit box.

Anyway here’s this :

OpenAI fired back at a lawsuit filed against it by Elon Musk in a blog post Tuesday, using the billionaire’s own emails to show he backed the company’s plans to become a for-profit business and that he insisted it raise “billions” of dollars to be relevant compared with Google.

Here is OpenAI’s blog post, which explains that OpenAI was founded as a nonprofit but eventually decided it needed more money than it could get from donors:

We spent a lot of time trying to envision a plausible path to AGI. In early 2017, we came to the realization that building AGI will require vast quantities of compute. We began calculating how much compute an AGI might plausibly require. We all understood we were going to need a lot more capital to succeed at our mission—billions of dollars per year, which was far more than any of us, especially Elon, thought we’d be able to raise as the non-profit.

Yes, right, it turns out that it is easier to motivate people to give you computing power if you pay them for it, it is easier to motivate researchers to develop artificial intelligence if you give them stock options, and it is easier to get people to give you money if you offer them a share of your financial returns. (OpenAI has raised roughly 100 times as much money from investors as it ever did from donors.) If you want to build a car company or a rocket company or a social network, this is also true, so it seems intuitive to apply the same reasoning to AI.

Elon Musk knows this and, apparently, agreed that OpenAI should pivot to profit. But he took his usual view, that the best way to do good for the world was through a for-profit company *that he controlled*:

In late 2017, we and Elon decided the next step for the mission was to create a for-profit entity. Elon wanted majority equity, initial board control, and to be CEO. In the middle of these discussions, he withheld funding. Reid Hoffman bridged the gap to cover salaries and operations.

We couldn't agree to terms on a for-profit with Elon because we felt it was against the mission for any individual to have absolute control over OpenAI. He then suggested instead merging OpenAI into Tesla. In early February 2018, Elon forwarded us an email suggesting that OpenAI should "attach to Tesla as its cash cow", commenting that it was "exactly right... Tesla is the only path that could even hope to hold a candle to Google. Even then, the probability of being a counterweight to Google is small. It just isn't zero".

Elon soon chose to leave OpenAI, saying that our probability of success was 0, and that he planned to build an AGI competitor within Tesla. When he left in late February 2018, he told our team he was supportive of us finding our own path to raising billions of dollars.

And now Elon Musk in fact does have a for-profit artificial intelligence startup that he controls and that competes with OpenAI. The Wall Street Journal reports:

After Musk filed his lawsuit, Altman wrote a memo to his staff: "The implication that benefiting humanity is somehow at odds with building a business is confusing," he said. "I miss the old Elon."

No, see, he still thinks that building a business is the best way to benefit humanity, which is why he's doing it. But the old Elon also liked to make outlandish claims in court; you just can't take this stuff too seriously.

Celsius

When I worked as a mergers-and-acquisitions lawyer and then as an investment banker, I thought that you could trade stocks in the US from 9:30 a.m. to 4 p.m. New York time, Monday through Friday. Was that completely accurate? No, of course not: There were, and still are, early morning and after-hours trading sessions, and I knew that. But it was close to true: There was, and still is, much more trading during normal market hours than in the extended sessions.

And it was a very *useful* approximation of the truth. In particular, here are two stylized facts that are sort of true and that work very nicely together:

- 1. "The market is closed evenings, early mornings and weekends."
- 2. "Public companies have an obligation to keep their investors informed about material stuff that is going on."

For example: Public-company mergers and acquisitions tend to be intensively negotiated over the weekend, and are often announced on Monday mornings. Why? Well, because if a public company reaches an agreement to sell itself, that is an extremely material fact, and it should really announce that right away. You do not want people blithely buying and selling the stock at \$35 when the company has already signed a merger agreement to sell itself for \$50 per share. If you sign that deal at 11:46 a.m. on a Wednesday, first of all, every second that you spend drafting the press release is precious, and second, whenever that press release *does* come out, it's going to be disruptive: The stock will spike up, people will make and lose fortunes, people who see the press release a millisecond before everyone else will have a huge advantage, and you will generally have disorderly and unpleasant trading. In fact, if you *do* find yourself needing to announce a merger at 11:46 a.m. on a Wednesday, you will ordinarily ask the stock exchange to halt trading in the stock first, and reopen it only after the announcement has gone out and everyone has had a few minutes to read it.

But that is stressful and disruptive too, and it's much better to just get everything buttoned up on Sunday evening, get the press release ready to go, and put it out first thing Monday morning, well before the market opens. Give everyone plenty of nontrading time to digest and understand the news, so that when trading starts everyone is on a level playing field. Also, if for some reason there is a glitch in the system when you hit publish on the press release at 6 a.m., you have time to fix it: If it goes out at 6:20, that's fine too.

(To be clear, this stylized fact is good and useful from the abstract perspective of the public company, but it was very bad from my perspective as a young M&A lawyer. Terrible hours!)

Anyway, I mostly still think that

- “market hours” are 9:30 to 4, Monday through Friday,
- you are supposed to put out material news “outside of market hours,” and
- it doesn’t matter all *that* much exactly when you do that, as long as you leave plenty of time before the market opens.

And I think a lot of other people still think that too, in part out of old habit, and in part because it is still sort of true, and in part because it remains very useful.

But there has been some creep toward always-on financial markets – we talked last week about a proposed 23-hour-a-day stock exchange – and I worry that this stylized fact is no longer true. We talked a few weeks ago about a typo in Lyft Inc.’s earnings release. Lyft put out the release right after the market closed on a Tuesday, there was a material typo, Lyft did an earnings call at 4:30 p.m., it verbally corrected the typo, and it filed a corrected earnings release at 5:51 p.m. Absolutely no harm, no foul, on the traditional way of thinking: All of this happened after hours, and by 9:30 the next morning everyone had had plenty of time to digest it.

But in fact \$700 million worth of Lyft stock traded in the after-hours extended session that Tuesday, roughly three times as much as Lyft usually trades in the *regular* trading session. And there were news stories about it, and readers emailed me to be like “is this securities fraud,” and Lyft’s CEO had to go on television to say he was sorry. I forgive him! I wrote:

It is customary to do these things after market hours for – well, not exactly for this reason, but kind of for this reason? You put out the press release just after the market’s regular trading session closes at 4 p.m., and investors have 17.5 hours to think about it before the market opens again at 9:30 a.m. the next day. They can ponder the earnings release at their leisure, update their models, ask questions on the earnings call, and generally take their time to digest the new information and formulate a price view before the market opens and they have to trade on it. If there’s anything ambiguous or surprising in the earnings release – or a typo! – the company and the investors have time to clarify it, and they can trade the next day with well informed views. ...

Lyft can’t stop its shareholders from trading after hours, but in some rough sense that’s not its responsibility. If you want to trade in the after-hours market the second the press release hits the tape, the risk of typos is on you.

And then last week Celsius did this :

Celsius Holdings Inc.’s quarterly results were sitting online, waiting to give anyone who looked a sneak peek at the earnings that would set off a 20% rally in the energy-drink company’s stock price.

Not many people, it seems, knew they were there.

The company, which has a market value of about \$19 billion, was scheduled to release its fourth-quarter and full-year results at 6 a.m. New York time on Thursday.

But they appeared on Celsius’s website Wednesday night shortly after 7 p.m., with screenshots later circulating on X. The stock edged higher around that time, but on featherweight volumes. Trading picked up right at 6 a.m. Thursday, with shares falling more than 5% premarket before surging during the regular session by the most since August. They ended the day at an all-time high. ...

It appears to be the latest blunder of what’s been a fairly gaffe-heavy earnings season, with notable clerical errors in reports from Lyft Inc., Planet Fitness Inc., Mister Car Wash Inc. and Rivian Automotive Inc. ...

Of course, even if investors did see Celsius’s report when it became available Wednesday night, they may not have been able to trade on it at the time and would’ve waited until Thursday’s premarket session, said Kenneth Polcari, chief market strategist at Slatestone Wealth LLC.

"I think it's just sloppy," Polcari said of the early release. "But I don't think anyone was disadvantaged."

It's fine! This is how it's supposed to work! There are two sorts of time in the stock market:

- 1. From 9:30 a.m. to 4 p.m., people are trading and every millisecond counts.
- 2. From 4 p.m. to 9:30 a.m., and all weekend, time stops mattering: That whole stretch of 17.5 or 65.5 hours is effectively a single point, and there is no meaningful difference between 7 in the evening and 6 the next morning.

If you put your earnings up on your website at 7 p.m. and then put them out on a news wire at 6 a.m., that's fine! Those times are the same time! You did exactly what you are supposed to do; you got the information out there in the quiet time between when the market closed and when it opened again. Except the market was kind of open the whole time.

The board is in charge

The other day I mentioned a lawsuit against Crown Castle Inc., whose estranged co-founder sued over a deal the company struck with Elliott Investment Management. Elliott had run an activist campaign and threatened a proxy fight, and Crown Castle settled by giving Elliott two board seats. The co-founder, Ted Miller, wants to nominate his own board candidates and objected to Crown Castle's agreement to endorse Elliott's directors without even considering his. "The affairs of Delaware corporations," his lawyers wrote, "must be managed by boards of directors, not backroom deals."

Well, this week Crown Castle and Elliott amended their deal to add a "fiduciary out." That is: They still have a contract saying that the board will endorse Elliott's nominees, but now the contract specifically says that the board can change its mind if it decides that that's in the best interests of shareholders:

If the Board in good faith determines (a "Recommendation Determination"), after consultation with counsel, that the fiduciary duties of the members of the Board as directors of the Company require that the Board (x) change or withhold a prior recommendation that the Company's shareholders vote "for", or (y) recommend that the Company's shareholders vote "against", the election of a New Director (a "Specified Director"), then: [it can].

That does seem like a fairly straightforward fix. Miller's objection was a technical point of Delaware law: The board of directors has to run the company in the way that it thinks is best for shareholders, so signing a contract saying "the board will recommend your nominees" might be illegal, if (1) the board later gets other nominees, (2) it decides, in its heart of hearts, that those nominees are better, but (3) it feels bound by the contract to recommend the first, worse nominees. But if you rewrite the contract to say "the board can change its mind," that addresses the problem. And these outs are not uncommon. In particular, many public-company merger agreements let the target company's board get out of the merger if, after jumping through some hoops, they conclude that another deal is in the shareholders' best interests.

Obviously rewriting the contract to say that the board can change its mind makes it a less useful contract. But the point is that, here, the board *wanted* the deal with Elliott, and probably *doesn't* want Miller's nominees on the board. Rewriting the contract solves the technical problem but probably doesn't change what will actually happen.

Good honeypot

The internet tells me that there are about 1.2 million people in the US with top secret security clearance. You could imagine a sort of cool spy-movie world in which "top secret" secrets were really top secret and only shared with a few, carefully vetted, highly trustworthy people. But at 1.2 million people, nah. At 1.2 million people, even if your vetting process is 99.99% reliable, you will still have 120 people who forget their top secret documents on the train, or leave their top secret laptops open at the coffee shop while they go to the bathroom, or have loud top secret phone conversations in public places, or are actual spies for the other side. At 1.2 million people, no matter how good your vetting is, the far left tail of the trustworthiness distribution is going to be this guy:

A civilian employee of the U.S. Air Force assigned to the U.S. Strategic Command (USSTRATCOM), at Offutt Air Force Base, was arrested Saturday, March 2, for allegedly conspiring to transmit and transmitting classified information relating to the national defense (National Defense Information or NDI) on a foreign online dating platform beginning in or around February 2022 until in or around April 2022.

According to the indictment, David Franklin Slater, 63, of Nebraska, worked in a classified space at USSTRATCOM and held a Top Secret security clearance from in or around August 2021 until in or around April 2022, after retiring as a Lieutenant Colonel from the U.S. Army. It is alleged that Slater willfully, improperly, and unlawfully transmitted NDI classified as "SECRET," which he had reason to believe could be used to the injury of the United States or to the advantage of a foreign nation, on a foreign online dating platform to a person not authorized to receive such information.

Yes, somewhere out there, there will inevitably be a guy who (1) has a top secret security clearance and (2) will hand out military secrets to impress obviously fake partners on an online dating site. Allegedly Slater got classified briefings about Russia's invasion of Ukraine, and he had a fake online girlfriend "who claimed to be a female living in Ukraine on the foreign dating website." From the indictment:

Co-Conspirator 1 [the fake girlfriend] regularly asked DAVID FRANKLIN SLATER to provide her with sensitive, non-public, closely held, and classified NDI, to which DAVID FRANKLIN SLATER had access as a result of his employment with the United States Air Force. For example, Co-Conspirator 1 stated in 2022: ...

On or about March 11, "Dear, what is shown on the screens in the special room?? It is very interesting." ...

On or about March 15, ... "You are my secret informant love! How were your meetings? Successfully?"

On or about March 18, "Beloved Dave, do NATO and Biden have a secret plan to help us?" ...

On or about April 12, "Sweet Dave, the supply of weapons is completely classified, which is great!"

Did he ever worry that maybe she only loved him for his top secret information and not for his sparkling personality? Did he care? How could this possibly have worked? Well, it only had to work on one guy.

What does Crypto smell like?

Here's a terrible commercial from Binance. I am dying to know what it smells like, if anyone has a bottle.

Things happen

New York Community Bancorp Seeks Cash Infusion. The traders hunting for power-grid bottlenecks. SEC Scales Back New Pollution-Disclosure Rules for Companies. Bitcoin Volatility Picks Up After Token's Run to All-Time High. The Believers Who Rode Bitcoin to a Record High—and the Ones Who Missed Out. Citi Reorganization Has Gone Swifter Than Expected, CEO Says. UBS chief Sergio Ermotti hits out at Europe's 'parochial' view of banks. EV group Lucid admits it cannot rely on 'bottomless wealth' of Saudi owner. China Stock Watchdog Vows Action at Times of 'Market Failures.' Dartmouth Players Vote for Union in First for College Sports. Vax-happy 62-year-old gets COVID shot more than 200 times – leaving scientists stunned. "Oblectate, nunc hic sumus."

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- 1. He did start a company to build underground tunnels because he was sick of traffic, but honestly that's fine too.

- 2. One can quibble with "owns" and "controls," but he owns big chunks and has pretty effective control, if not necessarily majority voting control.
- 3. This might not be true; the best AI researchers might be the ones specifically motivated by helping humanity in a nonprofit structure. "OpenAI may not have the best data, but at least it has a mission structure that may help idealist researchers sleep better at night," wrote Ben Thompson in 2015, citing OpenAI's own claims. I tend to think the stock packages matter too though.
- 4. Because Elon Musk follows absolutely no conventional rules of M&A, I once made a joke about this on Twitter, about his deal to buy Twitter, which I assumed would casually be announced in the middle of the trading day. And then it was!
- 5. Actually it's not uncommon to want to announce Sunday evening, before Asian markets open.
- 6. Incidentally, sometimes when I use the word "millisecond" in this column, I get amused emails from electronic traders being like "bro a millisecond is soooooooooo long, try every microsecond counts."

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Elon Musk’s OpenAI Lawsuit: Sorting Truth From Hype (1)

By Max Chafkin

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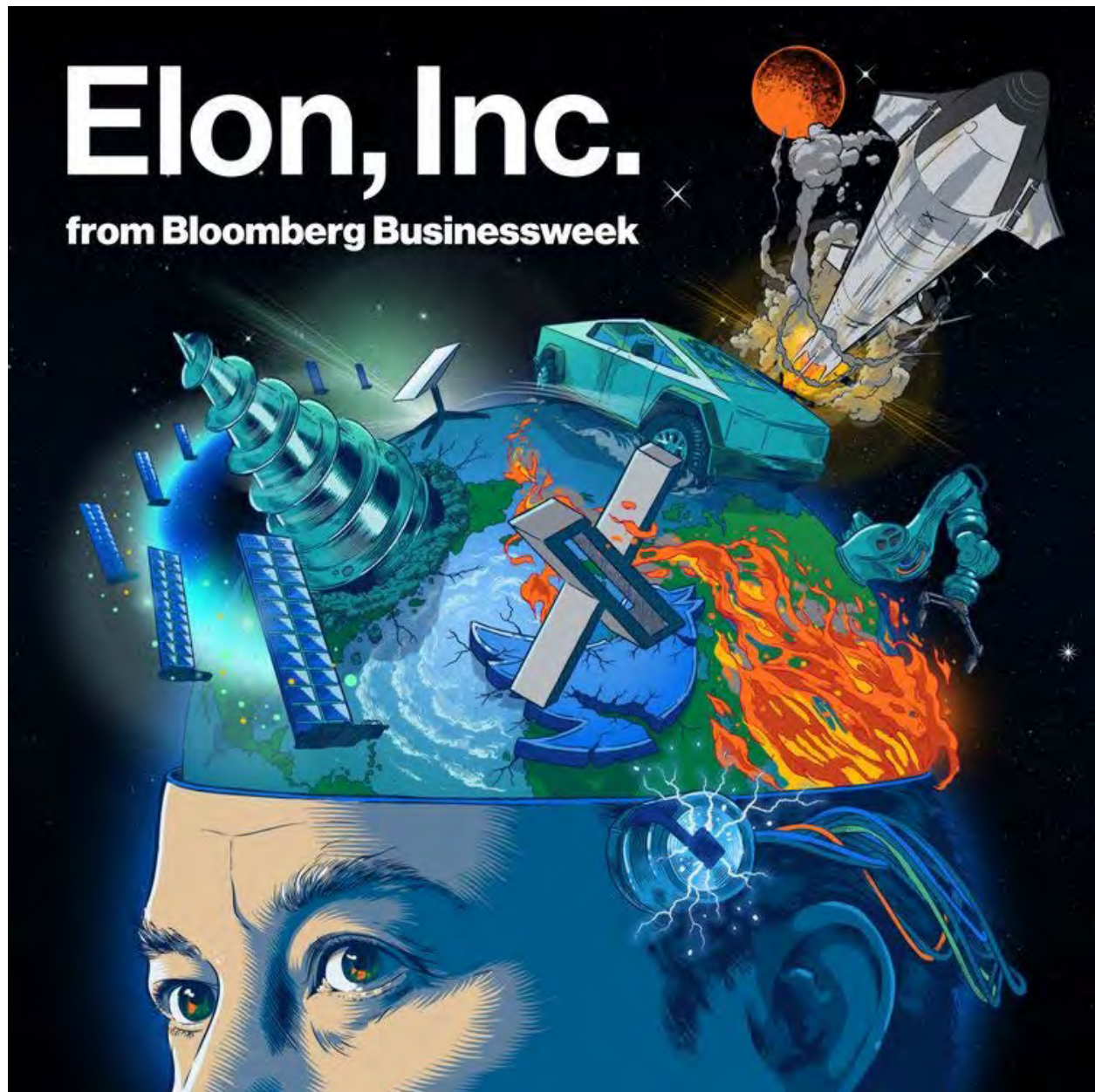
Elon Musk’s OpenAI Lawsuit: Sorting Truth From Hype (1)

By Max Chafkin2024-03-06T10:06:14281-05:00

Fast-growing technology companies exaggerate constantly. This isn’t to say they lie; it’s just that when you’re raising large sums of money, it helps to present an impressionist picture of your current business rather than a photorealistic one. Google’s founders talked about organizing “the world’s information” back when they weren’t even the most successful search engine from Stanford University; Airbnb’s founders argued that vacation rentals would, by some unknown alchemy, end hatred; and WeWork spun a fairly conventional real estate startup into a pseudo-spiritual lifestyle brand.

This form of BS is mostly benign, but it can create vulnerabilities when it’s overused or when a company that has previously stretched the truth finds itself targeted by an equally adept BSer. That’s the case with OpenAI, Silicon Valley’s hottest startup and the developer of ChatGPT. On Feb. 29 the [company was sued](#) by Elon Musk , the trollish billionaire with a simmering grudge against it and a lot of experience in delivering an overambitious sales pitch.

Musk’s complaint centers on the chasm between OpenAI’s image as a nonprofit research lab dedicated to preventing harms caused by artificial intelligence and the reality that it’s also the dominant maker of commercial AI software via a for-profit subsidiary that’s backed by Microsoft Corp. and valued at \$86 billion. Musk provided seed funding for the nonprofit in 2016 but broke with the organization around the time it went for-profit, and he’s long professed outrage over this discrepancy. “This would be like, let’s say you funded an organization to save the Amazon rainforest,” Musk said in a television interview last year. “And instead they became a lumber company.” In a blog post OpenAI suggested that Musk’s account was incomplete and that he’d only turned against OpenAI when the non-profit resisted his effort to take it over. In an [internal memo](#) the company also suggested that Musk had picked a fight out of jealousy.



According to the suit, Musk and Sam Altman, OpenAI's chief executive officer, have a history that began almost a decade ago when both men were loudly warning about the dangers posed by so-called artificial general intelligence, or AGI. They feared, in essence, a *Matrix*-like scenario in which computers develop superhuman intelligence and then threaten to exterminate humankind. Many experts think this distracts from less cinematic threats posed by AI, but Musk and Altman persisted, founding OpenAI in 2015 as a nonprofit that promised "to advance digital intelligence in the way that is most likely to benefit humanity," an announcement explained.

The idea was that OpenAI would race to develop an altruistic AGI (before a less scrupulous software company did so first) and head off the risk of a hostile takeover by out-of-control code. It's never been entirely clear how this would work, but Musk has said he hoped to weaken the market leader, Google, whose co-founder Larry Page had suggested to him in a private conversation that machine dominance of humans would "be the next stage of evolution," according to the suit. (Musk has made versions of this claim before; Page hasn't commented on it.) In response, Musk claims, he donated \$44 million to OpenAI, recruited scientists and even came up with the name.



Musk

Photographer: Grzegorz Wajda/SOPA Images/LightRocket/Getty Images

In 2019 the nonprofit spun off its capped-profit arm and struck a deal with Microsoft that would ultimately put the company's chatbots into the Bing search engine and Microsoft's wildly successful Office suite. The deal also helped finance ChatGPT, which became a successful product in its own right as Altman made grandiose claims about plans to capture and redistribute most of the world's wealth, flirting with the prospect of [raising billions](#) (or even trillions) to speed things further.

In Musk's telling, this adds up to a betrayal: A philanthropic venture was "transformed into a closed-source de facto subsidiary of the largest technology company in the world," according to the lawsuit. "Where some like Mr. Musk see an existential threat in AGI, others see AGI as a source of profit and power," the suit says, apparently referring to Altman.

There are many reasons to question Musk's rationale and motives. The lawsuit claims OpenAI breached its agreement with Musk, but that agreement seems to exist mostly in Musk's mind. His lawyers have produced no contract—only an email from Altman that mentions OpenAI would operate "for the good of the world" and a copy of the articles of incorporation. Musk also has a history of ill-conceived stunts and questionable lawsuits. The same day he filed his OpenAI complaint, a federal judge referred to arguments in a separate Musk suit aimed at a different nonprofit, the Center for Countering Digital Hate, as "one of the most vapid extensions of law I've ever heard."



Altman

Source: Bloomberg

On the other hand, Musk's complaint rightly points out that Altman took the art of Silicon Valley spin to new heights. Rather than simply embellish his company's capabilities, Altman tried a new tack: His stuff was so good, he said, it might accidentally destroy the world. This was OK, though, according to Altman, because AGI was so promising. A race was on, and Altman—the self-styled “Oppenheimer of our age”—argued that the world would be better off if OpenAI prevailed, since it was governed by a nonprofit. Borrowing an old saw from the gun rights movement, Altman argued that the only way to stop a bad guy with a killer robot was a good guy with a killer robot.

It was always unclear whether OpenAI could rein itself in, but those questions became more pronounced last year when Altman was fired by his board for unspecified dishonesty. Days later, a [Microsoft-backed counter coup](#) brought him back and led to a purge of the board. An internal investigation is underway—along with reports of a US Securities and Exchange Commission inquiry—but it's hard to believe the board would feel more empowered in the future.

Apart from questions of oversight, Altman's logic seemed a bit self-serving. If you truly believed you were making a weapon of mass destruction, a rational response might be to shut it down, instead of sticking it into hundreds of millions of copies of Microsoft Excel. By issuing warnings about worst-case scenarios, Altman diverted attention from OpenAI's more mundane failings, especially its penchant for making stuff up, even as ethicists warned that ChatGPT would be misused by scammers and propagandists.

Musk's lawsuit portrays Altman as a self-promoting [hypocrite](#), a description that might also apply to Musk, who's the master of cloaking entrepreneurial ambitions in exaggerated claims of do-goodery and who has a strong incentive to disrupt OpenAI's business. Two Musk companies compete with OpenAI: Tesla Inc., which recruits engineers from the same talent pool as OpenAI, and xAI Corp., which offers a chatbot that Musk promotes as a less woke version of ChatGPT.

Moreover, the suggestion that Altman's control of OpenAI represents a threat to the nonprofit's mission is rich coming from Musk, who himself tried to take over OpenAI in 2018, according to a report from *Semafor*, turning critic only after the board rejected his offer. Tesla, unlike the rest of Musk's empire, is publicly traded and subject to board oversight—though Musk seems to have little problem subverting that whenever he feels the need. In January, a Delaware judge ruled that the [\\$56 billion pay package](#) Tesla had awarded to Musk was unlawful, because Musk had exercised undue influence over the board. Musk is expected to appeal the ruling, and in the meantime he's asked for a second stock award that could be worth another \$50 billion or more. If he doesn't get it, he's said that he'll develop AI products outside Tesla—that is, inside a company he controls.

In making this demand for greater pay, Musk adopted the same high-minded rhetoric about safety that Altman has employed, saying he would feel “uncomfortable growing Tesla to be a leader in AI & robotics” without an equity stake worth at least 25%. But behind this is the same basic motivation that Musk attributes to Altman. Both men say they're focused on the risks posed by AI. Their actions suggest that in the meantime they wouldn't mind taking advantage of those risks to make themselves very, very rich.

Read next: [Can AI Unlock the Secrets of the Ancient World?](#)

(Updates with OpenAI blog post in paragraph 3.)

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Bloomberg Law

OpenAI

OpenAI releases Elon Musk emails to show he backed for-profit plans

ChatGPT maker says Tesla boss wanted top job and board control as feud over AI start-up deepens



Sam Altman, left, and Elon Musk. Musk left OpenAI's board in 2018 after clashing with Altman © AFP/Getty Images

George Hammond in San Francisco YESTERDAY



OpenAI has hit back at Elon Musk, releasing emails to show that he supported its plan to create a for-profit entity and raise billions of dollars — decisions at the heart of the Tesla boss's lawsuit against the artificial intelligence start-up.

[Musk](#), who was part of OpenAI's founding team, claimed in the suit he filed last week that it had breached an agreement to make breakthroughs in AI "freely available to the public" by forming a multibillion-dollar alliance with Microsoft, which has committed \$13bn to the company.

"OpenAI, Inc has been transformed into a closed-source de facto subsidiary of the largest technology company in the world: Microsoft," Musk's lawsuit alleged.

In a [blog post](#) published late on Tuesday, founding members of OpenAI including Sam Altman, Greg Brockman and Ilya Sutskever contested that allegation, claiming instead that Musk had spearheaded early efforts to raise more money from investors.

“When starting OpenAI in late 2015, Greg and Sam had initially planned to raise \$100mn,” they wrote, but “Elon said in an email: ‘We need to go with a much bigger number than \$100mn to avoid sounding hopeless . . . I think we should say that we are starting with a \$1bn funding commitment.’”

OpenAI’s original non-profit structure hampered its ability to raise funds from traditional investors. Given the expense of building AI tools, that presented a barrier to its stated mission to develop increasingly sophisticated AI “that benefits all of humanity”.

“In late 2017, we and Elon decided the next step for the mission was to create a for-profit entity. Elon wanted majority equity, initial board control, and to be CEO. In the middle of these discussions, he withheld funding,” according to the blog post.

“We couldn’t agree to terms on a for-profit with Elon because we felt it was against the mission for any individual to have absolute control over OpenAI. He then suggested instead merging OpenAI into Tesla. In early February 2018, Elon forwarded us an email suggesting that OpenAI should ‘attach to Tesla as its cash cow,’” Altman and his colleagues wrote on Tuesday.

The exchange highlights tensions over the direction of Silicon Valley’s most feted start-up, which kicked off an AI boom with the launch of ChatGPT in November 2022 and has since set the pace among competitors including Anthropic, Inflection and Google.

The start-up has become a commercial juggernaut with revenues of more than \$2bn on an annualised basis and has drawn billions of dollars of investment from Microsoft and a host of venture capital firms since launching a for-profit entity in 2019, rocketing to a private market valuation of about \$80bn, according to a person familiar with the matter.

But concerns over governance and safeguards at the company remain, after the dramatic ousting and reinstatement of Altman as chief executive by members of the board — including Sutskever — last November.

An internal investigation into the boardroom tumult is expected to be completed in the next month, while the US Securities and Exchange Commission has separately probed some actions by the company and its executives during last year.

Musk — who left OpenAI’s board in 2018 after clashing with Altman — is raising money for his own AI project, named xAI.

“We’re sad that it’s come to this with someone whom we’ve deeply admired — someone who inspired us to aim higher, then told us we would fail, started a competitor, and then sued us when we started making meaningful progress towards OpenAI’s mission without him,” wrote the remaining leadership team.

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OpenAI seeks to dismiss Musk claims, says billionaire pushed for merger with Tesla

 [reuters.com/technology/openai-seeks-dismiss-all-musks-claims-lawsuit-2024-03-06](https://www.reuters.com/technology/openai-seeks-dismiss-all-musks-claims-lawsuit-2024-03-06)

Reuters

March 5 (Reuters) - OpenAI on Tuesday rejected Elon Musk's claims that the startup had abandoned its original mission of developing artificial intelligence for the benefit of humanity, and said the billionaire had demanded a merger between the ChatGPT-maker and Tesla (TSLA.O) [↗](#), opens new tab.

OpenAI said in a blog post it intends to move to dismiss [↗](#), opens new tab all of Musk's claims. Musk filed a lawsuit against the startup he co-founded last week, alleging breach of contract, saying the Microsoft-backed (MSFT.O) [↗](#), opens new tab firm is now focused on making money.

OpenAI said Musk wanted the company to merge with electric vehicle maker Tesla (TSLA.O) [↗](#), opens new tab, and he forwarded an email that said the startup should "attach to Tesla as its cash cow".

Tesla shares were down 2% in premarket trading on Wednesday.

OpenAI said the suggestion came after Musk and the company decided the next step was to create a for-profit entity in 2017 to generate capital for building artificial general intelligence (AGI).

The billionaire entrepreneur then wanted majority equity, initial board control, and to be CEO of OpenAI, the company said.

But OpenAI and Musk could not agree to the terms on a for-profit because the startup felt it was against the mission for any individual to have absolute control over the firm.

[1/2] Tesla and SpaceX's CEO Elon Musk pauses during an in-conversation event with British Prime Minister Rishi Sunak in London, Britain, Thursday, Nov. 2, 2023. Kirsty Wigglesworth/Pool via REUTERS/File Photo Purchase Licensing Rights [↗](#), opens new tab

In his lawsuit, Musk said OpenAI's three founders originally agreed to work on AGI, a concept that machines could handle tasks like a human, but in a way that would "benefit humanity,".

Musk also pushed OpenAI to announce an initial \$1 billion funding commitment in 2015, after CEO Sam Altman and co-founder Greg Brockman initially planned to raise \$100 million.

"We're sad that it's come to this with someone whom we've deeply admired - someone who inspired us to aim higher, then told us we would fail, started a competitor, and then sued us when we started making meaningful progress towards OpenAI's mission without him,"

OpenAI said.

Musk and Tesla did not immediately respond to Reuters requests for a comment on the blog.

Musk's lawsuit is a culmination of his long-simmering opposition to the startup.

OpenAI has since become the face of generative AI, partly due to billions of dollars in funding from Microsoft.

Musk went on to found his own artificial intelligence startup, xAI, launched last July.

Reporting by Abinaya Vijayaraghavan in Bengaluru; Editing by Rashmi Aich and Anil D'Silva

Boeing Faulted for 'Absurd' Lack of Cooperation in US Probe

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March 6, 2024, 9:12 AM PST

Alan Levin

Bloomberg Editorial



- NTSB still seeking documents, information in Max 9 review
- Investigators haven't been able to interview door staff: NTSB

By Alan Levin

(Bloomberg) --

Boeing Co. officials have failed to fully cooperate with US investigators looking into how a panel blew off of a 737 Max 9 in January, a Senate hearing was told Wednesday.

The National Transportation Safety Board hasn't received all the documents and information it has sought from Boeing since the dramatic Jan. 5 incident, agency Chair Jennifer Homendy told lawmakers Wednesday.

"It's absurd that two months later we don't have that," Homendy said.

The criticism runs counter to pledges of transparency by the US planemaker, which faces multiple probes and scrutiny from regulators, lawmakers and customers in response to the accident on an Alaska Airlines flight. Boeing and its chief executive officer, Dave Calhoun, have repeatedly vowed full cooperation with investigators at the NTSB and Federal Aviation Administration.

Boeing representatives didn't immediately comment on Homendy's testimony.

The NTSB said on Feb. 6 that forensic evidence and photos of work on the nearly new plane showed four bolts meant to hold a fuselage panel in place hadn't been installed on the Max 9.

The Alaska Airlines jet suffered an explosive decompression above Portland, Oregon, after the panel, or door plug, covering an unused emergency exit, flew off midflight.

NTSB investigators haven't been able to determine what led to the manufacturing lapse or other details of the work, Homendy said Wednesday.

Days after the accident, Calhoun addressed Boeing employees and said the company would approach the NTSB and FAA investigations “with 100% complete transparency every step of the way.” He has also vowed to change Boeing’s practices to bolster its safety culture.

Shares of the US planemaker fell 0.1% in New York. They have declined 23% this year, the worst performance on the Dow Jones Industrial Average.

Employee Interviews

Homendy said investigators believe a team of 25 Boeing workers were assigned to 737 doors, but the company hasn’t provided their names and the safety board hasn’t been able to interview them.

“We’ve asked repeatedly for that information,” Homendy said. “It’s not for lack of trying.”

In addition, the agency hasn’t been able to obtain documentation from Boeing showing how the work was performed, she said.

The US Justice Department is scrutinizing the incident, which could expose the company to criminal prosecution, Bloomberg reported Feb. 29.

The FAA is also investigating whether Boeing failed to comply with requirements that planes leaving their factories conform strictly to agency-approved designs. The agency has also bolstered its oversight of Boeing’s assembly lines, and barred the planemaker from increasing production rates until it’s satisfied that quality practices have improved.

(Updates with additional comments from fourth paragraph.)

--With assistance from Julie Johnsson.

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The Big Read **PDD Holdings**

The mysterious rise of the Chinese ecommerce giant behind Temu

Its finances are a black box and its operations shrouded in secrecy, but PDD's extraordinary growth has made it a darling of Wall Street

Dan McCrum in London YESTERDAY



Flanked by a wall of vivid orange packages, YouTuber Hope Allen was uncertain about the phenomenon they represented. “Temu has been taking over, and I don’t know how I feel about it.”

The ecommerce firm’s “shop like a billionaire” ad campaign to promote its online flea market was ubiquitous. Allen’s response was to buy a job-lot of undeliverable parcels that disgorged a sample of Americans’ experiment with Temu.

Among the piles of extremely cheap clothes, bags, tools, toys and kitchen implements were designer look-alikes that provoke questions. “How do they get away with that?” [asked Allen](#) of a faux Victoria’s Secret bag, before recoiling from the smell.

All were flown in from China by Temu’s parent company PDD Holdings, a self-described “agricultural group” engaged in what might be the fastest and most ambitious retail expansion in history.



Hope Allen unwraps Temu packages on her YouTube channel. 'Temu has been taking over,' she says © YouTube

With Temu, PDD wants nothing less than to change the way the world shops, a faster, leaner and [cheaper](#) version of Amazon that has spread from China to 49 countries after less than two years in operation.

The plan, as best can be inferred, is to use blanket advertising to lure western consumers to Temu's app, where algorithms and AI anticipate their whims and desires. Products are shipped for free direct from China's factory gates, cutting out the middleman and ensuring low prices.

Temu's sister app Pinduoduo already dominates China. When it still published such numbers, PDD reported more than 870mn active users in the country supplied by over 13mn merchants who, it claimed, together generated a third of all parcel traffic in the country, tens of billions of packages a year.

After just nine years in business, PDD is now bearing down on the world's biggest ecommerce group Alibaba, both in terms of retail scale and stock market capitalisation. Worth \$162bn, it regularly trades places with the older retail giant as the most valuable Chinese company listed on a US stock exchange.

But the tale told by those incredible numbers is a mystery that raises more questions than it answers.

For instance, why does PDD look like much smaller peers when staff levels and research spending are compared? Why haven't competitors described the impact of PDD's rise? Why do balance sheet metrics move at a different pace to revenues? How does a \$200bn company own less than \$150mn worth of hard assets?

These questions add up to a bigger one: why do US investors have so much confidence in an opaque operation whose financial statements seem to lack much pattern or explanation, and whose operations, management, auditors and regulators sit in a distant untouchable jurisdiction?

A PDD spokesperson said: “We respectfully disagree with that characterisation.” They encouraged the Financial Times “to review our financial reports and earnings calls for comprehensive insights” and said “disclosure rules and fairness principles” prevented it commenting on those financials to “individual media outlets”.

The American stock market is scattered with cautionary tales of Chinese promise that ends up unmet. “I drank a lot of coffee in a lot of Luckin Coffee locations, and it was still a fraud,” says one investor, of the once \$13bn Nasdaq-stock which admitted to inflating sales figures in 2020. Wish, an algorithmic Temu-like ecommerce site, saw a \$22bn market value dwindle almost to nothing.

Yet few have promised as much to investors as PDD. It operates like eBay and Amazon’s third party marketplace, connecting buyers with sellers to take a cut of each transaction and charging merchants to advertise on its platform.



Parcels are scanned at the US Customs and Border Protection overseas mail inspection facility in Chicago. With Temu, PDD wants a faster, leaner and cheaper version of Amazon © Charles Rex Arbogast/AP

In its most recent quarter those revenues almost doubled versus the previous year, to \$9.4bn, prompting Alibaba founder Jack Ma to exhort his former company to “change and reform” in [response](#). PDD reported \$2.5bn of cash flow, even as it appears to throw very large sums at the expansion of Temu.

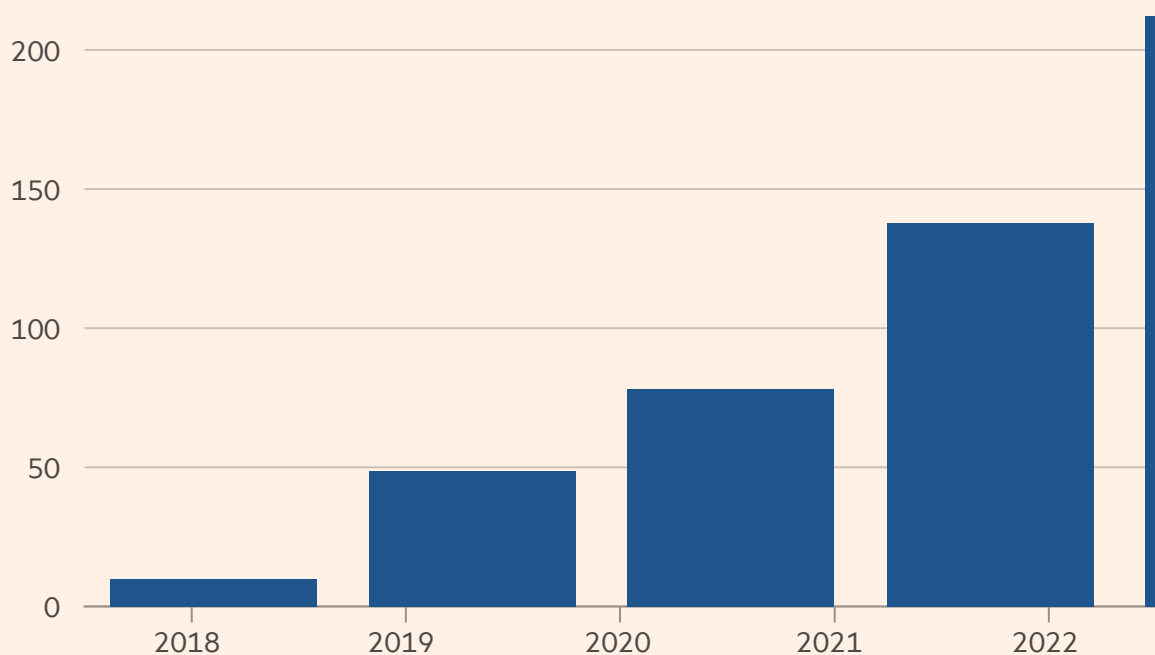
It has achieved this with a headcount that upends all assumptions about ecommerce logistics: it started last year with 12,992 employees, an order of magnitude less than Alibaba and a small fraction of Amazon’s 1.5mn staff.

PDD’s physical footprint is also minuscule, a striking contrast with Amazon, JD.com and Alibaba, where control of logistics was long seen as a competitive advantage; a way to ensure speed, capacity and satisfactory service.

Where Alibaba spends \$5bn a year on property and equipment, including the upkeep of 1,100 warehouses, PDD owns just \$146mn of hard assets — mainly office equipment and IT hardware and software.

Asset-light in the darkness

PDD's total lease obligations (\$mn)



FINANCIAL TIMES

Source: Company filings

It didn't disclose any leases of warehouses before 2021, when it said its online grocery business, then just one year old, had expanded to serve more than 300 major cities in China. It doesn't report the size, location or number of the warehouses it rents.

Those logistics, like PDD's servers and customer service call centres, are mostly outsourced, ephemeral and unenumerated. The opacity extends inside the business. Staff use pseudonyms and know little about other teams. The structure is flat, with a small group of decision makers directing the "grassroots", young people chosen for their poverty or debt obligations which motivate them to work long hours. PDD said: "Employees have access to all necessary information for effective cross-team collaboration and to fulfil their roles."

Such secrecy is a [hallmark](#) of Colin Huang, a former Google engineer who founded Pinduoduo in 2015 and for a long time hid his ownership. Initially, it attracted users by gamifying commerce. Describing itself for a while as "Costco + Disney", Pinduoduo offered games that mimicked addictive titles like Farmville and Candy Crush.

Combined with micropayments, carefully calibrated rewards, coupons and offers, the software was said to keep consumers returning to the app, where they were tempted to make impulse purchases or promote Pinduoduo to their friends. By 2018, the app boasted 300mn customers and after only three years in business the company listed on the Nasdaq stock exchange, raising \$1.7bn.

PDD vice-president of strategy David Liu, a former Goldman Sachs banker, described its "push-based business model" on a 2019 [podcast](#). He said that instead of searching for particular items, people went to Pinduoduo to browse, where algorithms and highly targeted offers encouraged social sharing of purchases. The rise of mobile internet use, according to co-chief executive officer Chen Lei, created a "[new paradigm](#)".

Their descriptions are hard to square with the numbers. Almost all of PDD's revenues then came from marketing services, where merchants "bid for keywords that match product listings appearing in search or browser results".

Another claimed benefit were insights into consumer demand that PDD passed on to merchants. As an example of this cutting-edge information, Liu talked about a glassware manufacturer that supplied big western retailers: PDD helped it to understand that Chinese people liked stubby wine glasses to go in their small cupboards.

Whoosh, the incredible expansion of Pinduoduo

PDD Holdings' gross merchandise value (\$bn)

400 —————

300 —————

FINANCIAL TIMES

Source: Company filings

That theory of PDD's business model soon clashed with reality. In a surprise shift in strategy, Pinduoduo started selling merchandise itself. It began Amazon-style first-party retailing, prompted by people searching for stuff. "We have noticed there are consumer demands in our platform, which we haven't been able to identify the appropriate merchants for," it said in late 2020.

Asked on a March 2021 earnings call "what exactly" PDD was selling in this experiment, Liu didn't give examples. He just said that the product categories were "actually quite diversified".

Over 2020 and 2021, PDD reported selling \$2bn worth of merchandise without disclosing any stocks of inventory on its balance sheet, or the costs of those goods sold, two standard retail accounting items. Then it stopped selling mystery merchandise as abruptly as it started.

The experiment's end may have been overshadowed by events. Founder Huang, one of China's richest people, stepped down in 2021 declaring a desire to research food science and life science. His [letter](#) said: "I would feel very lucky and blessed if I have the chance to become a research assistant to a future, possibly great, scientist."

He was replaced by co-chief executives, Chen and Jiazhen Zhao, who as a sideline personally control a payment services provider to the company that they purchased with the help of a \$100m loan from PDD.

A PDD spokesperson said this was "a simpler legal arrangement to secure and complete the acquisition of a payment licence."

Straight after Huang left PDD made a long-awaited flip to profitability. Having lost Rmb27bn (\$4.2bn) in three years, PDD reported earnings of Rmb2.4bn (\$380mn) for the second quarter of 2021. It was a key moment, as the group had raised \$11.6bn from sales of stock and debt that converts into shares to support a spend-now-for-profits-later business model.

Rather than focus on this milestone in the August 2021 earnings call, Chen described PDD's efforts to support Henan province after it was hit by heavy rain.

More unusual still, Chen then announced a plan for the first Rmb10bn of profits to be generated by PDD. He intended to spend it all on an "agricultural initiative" without a clear business purpose. The aim was fuzzy and broad, "to facilitate advancement of agritech, promote digital inclusion, and provide agritech talents and workers with greater motivation and a sense of achievement", he said.

Where's the initiative?

Annual R&D spending* (\$bn)

■ PDD ■ Ebay



FINANCIAL TIMES

Source: Company filings • *Ebay calls this product development

It is unclear how, or even if, the money was spent. PDD has not subsequently detailed the initiative in its financial statements, which are audited by a Chinese arm of EY, and continued to report profits. Research and development spending that year rose only slightly to \$1.5bn in total, similar in scale to eBay rather than Alibaba's \$8bn annual spend on product development.

Chen was ambiguous when asked about the initiative during a 2022 earnings call. He said he'd evaluated many proposals, that PDD was "co-operating with top agronomic universities and research institutions to jointly work on some research projects", and its investment in agriculture was "early stage".

Perhaps the biggest mystery about PDD is how large it has truly become.

A metric published by some ecommerce businesses is gross merchandise value (GMV) sold via the platform — a picture, effectively, of its entire ecosystem of sales. Ebay, for instance, reported GMV of \$73bn for its marketplace last year, from which it earned \$10bn of revenues.

PDD used to report such a figure. For 2021 it said GMV was Rmb2.4tn (\$383bn). From that, PDD generated a total of \$14.7bn of revenues from marketing and transaction services, a 3.6 per cent margin known as the “take rate”.

How big is the PDD ecosystem?

Estimates for PDD's annual gross market value (GMV, \$tn)

Equivalent to the size of ...



Sources: Company filings; IMF; FT research
© FT

However, while PDD still publishes revenue from marketing and transaction fees, it no longer reveals its GMV. Estimating how big its ecosystem has become thus depends on assumptions about what the take rate now is, or what share of GMV the company keeps for itself.

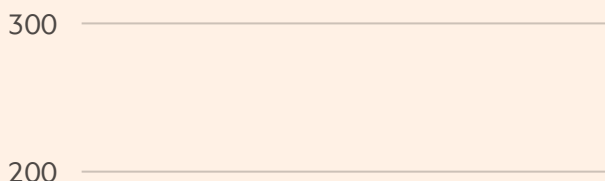
Analysts offer a range of estimates for last year’s total GMV between Rmb3.6tn (\$500bn) and Rmb4.8tn (\$700bn), according to Bloomberg, with a consensus of Rmb3.9tn (\$550bn). At the higher end, that would be similar to estimates for Amazon’s total GMV this year.

But complicating that picture are metrics on the income statement and balance sheet moving at very different speeds.

In the blow-out recent quarter, marketing services grew at roughly the same pace they have since the middle of 2021, about 40 per cent year-on-year. But over the same period, transaction fee revenues grew at more than three times the rate of marketing services.

Something has happened to PDD's transaction fees

Year-on-year growth rates for services revenues (%)



FINANCIAL TIMES

Source: Company filings

Based on the transaction fee rate PDD reported in 2021, that would suggest an improbable level of activity, making the PDD ecosystem twice the size of Alibaba and on a par with the \$2.2tn annual output of the Italian economy.

Instead, PDD must be charging its merchants a lot more. Asked about the trend on a 2022 earnings call, Chen said user engagement had contributed to earnings growth and that “it is common to see fluctuations between quarters”.

PDD told the FT it had expanded its offering to include “various transaction services”. It did not say what those additional services were. Analysts assume transaction services includes revenues from groceries and Temu, which have different dynamics to Pinduoduo.

A liability still detailed on PDD's balance sheet, meanwhile, signalled a much slower pace of growth for GMV.

At the end of September each year from 2018-21, the money "payable to merchants" ranged from seven to nine days' worth of annual GMV. The most recent figure thus suggests estimates for 2023 GMV of \$400bn to \$500bn.

At either end of that scale, it would seem inevitable that PDD's rise would be felt by its main competitors. After all, there are only so many online shoppers to go round.

PDD's impact is hard to detect in their numbers. In the battle of online flea markets, Alibaba's Taobao reported improving take rates and growing merchant numbers last month that hardly indicate obliteration by Pinduoduo. Alibaba's executives have not addressed their upstart rival by name on any of their earnings calls.

Outside China, both eBay and US discount chain Five Below said last year they hadn't seen any impact on their business from Temu. Amazon didn't mention it when reporting results last month.

Etsy's CEO Josh Silverman focused on Temu's head-scratching advertising blitz, estimated by some analysts to cost billions of dollars: "It's not obvious that they have much of an ROI [return on investment] lens on their spend. So they appear to be spending a lot of money to acquire customers who may not have very large wallets and may not be very loyal."

PDD said it anticipated "refinement of our marketing approach, placing increasing emphasis on building strong customer loyalty and advocacy".

Some of its advertisements address concerns about Temu head on. In [one](#), a pastiche of mafia movies, a beard-stroking mobster remarks: "So cheap. People may not believe it's real."

If PDD's numbers are indeed to be believed, then a shrewd executive team directing pseudonymous underlings has created one of the most successful businesses the world has ever seen.

But it is not clear how the several thousand staff who run PDD deal with the risks in administering hundreds of millions of transactions, and tens of millions of suppliers delivering tens of billions of parcels.

How, to use just one example, does the company monitor money-laundering risks — given the dangers that fake customers use fake transactions to send money to fake merchants?

PDD said it supported this vast network through “a core workforce and strategic partnerships” that leveraged “technology-driven solutions to monitor and address issues like counterfeit goods”. A Temu spokesperson also said that all partners “must strictly comply with regulatory standards”.

Investors searching for further detail were unlikely to find it at the most recent earnings call, when Chen took a total of six questions from three analysts and made pronouncements that resembled state political sloganeering.

“We are dedicated to generating value through innovations, which forms the foundation of our high-quality development,” he said, echoing a key tenet of his country’s latest five-year plan.

They would also draw a blank attempting to direct questions to a chief financial officer. PDD doesn’t have one. Instead it is on its fourth “vice-president of finance” since the 2018 initial public offering, if a period when founder Huang added the job to his duties is counted.

It seems that while profits are good, investors are willing to tolerate such opacity. On Wall Street, 53 out of 56 analysts recommend their clients buy, and not one suggests they sell.



The headquarters of Pinduoduo in Shanghai in 2018. Last year, the group relocated to Dublin. The company hasn't courted the investors who might know it best with a secondary Hong Kong listing © Reuters

Norm-breaking appears to make PDD a tabula rasa on to which foreign investors project assumptions. Unlike other large US-listed Chinese companies, PDD — which is nominally headquartered in Dublin — hasn't courted the investors who might know it best with a secondary Hong Kong listing.

The structure for foreign ownership of Chinese assets remains untested, with “heightened operational and legal risks”, according to the head of the Securities and Exchange Commission. Holders of PDD stock own shares in a Cayman Islands company that has unpublished contractual agreements said to entitle it to the profits of the Chinese operating companies.

A spokesperson said PDD had “a robust financial leadership structure” and “strong corporate governance”, that its “disclosure practices compare favourably to those of our peers”, and that its US listing provided “the necessary access to capital markets and visibility to support our business objectives”.

Huang still owns the largest stake in PDD and his shares are voted by the [board](#), whose three independent directors include a former foreign minister of Singapore and a Dutch academic expert in food safety.

Hayden Capital, an investor in the company, acknowledged in a [memo](#) that a “lack of transparency and concerns about corporate governance” had put off investors in the past.

It argued that “just because a company doesn’t give investors disclosure doesn’t necessarily mean they don’t care about investors”. To truly understand PDD’s thinking, the New York firm continued, “we have to analyse past actions”.

Data visualisation by [Steven Bernard](#)

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From SPAC Dreams to Riviera Mirage: How Lottery.com Imploded (1)

By Nicola M. White

Deep Dive

- “We are breaking the law in 42 different ways,” a board member said
- SEC, DOJ investigating company amid revival efforts

Bloomberg Law News 2024-03-06T10:57:52776518444-05:00

From SPAC Dreams to Riviera Mirage: How Lottery.com Imploded (1)

By Nicola M. White 2024-03-04T05:01:05000-05:00

- “We are breaking the law in 42 different ways,” a board member said
- SEC, DOJ investigating company amid revival efforts

They partied like they'd just won the lottery.

Aboard the yacht docked at the 2023 Monaco Grand Prix were buckets of chilled bubbly, more than \$6,000 worth of cigars, a live band, and bow-tied bartenders. UK pop star Robbie Williams dropped by to do a podcast interview.

If anyone knew how much it all cost, they weren't telling the CEO, who suspected the total was in a second set of books no one would let him see.



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LISTEN: Reporter Nicola M. White talks about this story on our news podcast, On The Merits

Lottery.com Inc. couldn't make payroll. It had no domestic lottery ticket sales. Its stock price had dived below \$1. It was so far behind on regulatory filings that Nasdaq threatened to kick it off the exchange. The French Riviera fete was a blow-out by some board members, including the future CEO, to lure well-heeled investors into what was left—a sports website with huge aspirations but no content and little to do with lotteries.

Lottery.com had promised to do for lottery ticket sales what Uber did for getting a ride or DoorDash for getting a meal. No longer would you have to go into a convenience store to get your weekly fix of Powerball or Mega Millions; you could buy a ticket from anywhere on an app.

Instead, Lottery.com came to represent all the hubris and excesses of the special purpose acquisition company era: phantom revenues, multiple CEOs hired and fired, accusations of forged documents, an alleged check-kiting scheme, trails of stiffed investors and vendors—including a church—and finally, a promised rescue by a would-be Premier League team owner that turned into something else.

New executives are working to fend off lawsuits, raise money, and get operations going again. Prominent hedge fund Balyasny Asset Management bought a stake in Lottery.com last month. But its past looms large, with Securities and Exchange Commission and Department of Justice investigations underway. At least three company insiders say they've been interviewed by the US Attorney's office for the Southern District of New York.

Lottery.com's Global Reach

The players in the Texas-based firm's saga spans three continents.



Graphic: Jon Meltzer/Bloomberg Tax

Bloomberg Tax

"This had almost every element of crookery you could imagine. And I was seeing it in real time," said Mark Gustavson, who was CEO at the time of the party but was fired two months later, replaced by a board member who was on the yacht.

Buy By Phone

"They were eager to get a deal done," DiMatteo said. "We had no idea what this game was. They were the grownups in the room."

The C-suite celebrated the Nasdaq debut with a Times Square photo of the leaders jumping in front of an electronic billboard emblazoned with the company's ticker. Within days, Lottery.com was being valued at more than \$800 million.

Cracks showed in a matter of weeks.



'Check Kite'

The company's first earnings report in November 2021 boasted \$32.2 million in revenue, an almost 2,000% increase from the year before.

But nearly all of that, \$30 million, was based on the sale of credits the company had amassed with media partners that turned out to be nontransferable, meaning they weren't supposed to be sold, the company later said when it had to correct its financials to fix its mistakes. Beyond that, the company further erred by recognizing income from the transaction before it had been paid, according to its SEC filings.

The payment hadn't come in because the buyer — a payments platform company — didn't actually have the money on hand. So the company and the buyer struck a complex financing agreement in which Lottery.com pledged its own assets to secure a line of credit that the buyer would then use to pay up, the company would disclose to the SEC a year later.

Feeling pressure to make year-end revenue projections, company officials arranged for a courier to collect a check from the buyer two days before New Year's Eve, according to people involved in the transaction and an audit committee memo reviewed by Bloomberg Tax. When the line of credit came through, the buyer covered the \$30 million check and Lottery.com in turn wired the money right back—but continued to count the money as revenue on its books until it restated, or corrected, its financial reporting five months later.

Essentially, it was "a check kite," a member of the company's management team said a year later at a meeting explaining the transaction to an outside adviser. Bloomberg Tax reviewed a recording of that meeting. Asked about the deal, Lottery.com's current leadership said the transaction is one of the subjects of SEC and DOJ scrutiny, and the company has been fully cooperating with authorities in their reviews.

A few months later, CFO Ryan Dickinson faced a substantial personal tax bill. The executive of the payments company that had been involved in the complex credit transaction suggested his Southern California church could help. The church had sold its only building, netting a few million dollars, and needed more money to buy a new property for its growing congregation.

A customer convinced church leaders, including its pastor Daniel Jones, that instead of borrowing money from a bank, they should offer the CFO a loan with a return which no normal investment would offer—\$2.7 million for one week with \$300,000 interest, according to people involved in the transaction and a lawsuit the church later filed. Even though it was a personal loan for the CFO, CEO DiMatteo and chief revenue officer Clemenson supplied the value of their shares in the company—worth about \$40 million at the time—as proof the loan could be repaid.



Lottery.com - Share Price

By Jon Meltzer on 1 Mar 2024



A Precipitous Share Price Crash

Lottery.com lost over half of its share value in November 2021 and never

Instead, according to a lawsuit filed in San Diego county, the church lost all the money.

"It's been traumatic for them. They had all this money. They were going to buy this new church and renovate it," attorney Craig Holiday said. "And all of a sudden they lost it." Dickinson, who was fired within two months of the loan arrangement, didn't respond to requests for comment.

'Beyond Breathtaking'

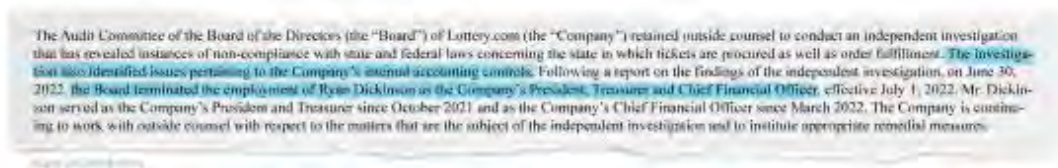
Meanwhile, it became clear that Lottery.com's core business had some serious flaws.

By mid-2022, customers in a dozen states could buy lottery tickets on their phones using the Lottery.com app. But tickets didn't instantly pop into customers' digital wallets; state lottery regulations are much more old school than that.

Like other online lottery sales companies, Lottery.com had to hire couriers in each state to go to convenience stores and gas stations to buy tickets and store them.

Couriers sometimes couldn't be found when a customer ordered a ticket, however, according to an internal investigation initiated by the company's chief legal officer, Katie Lever. When that happened with an order for a Powerball ticket from a customer in Pennsylvania, for example, the company directed that ticket to get printed in a backup hub in Texas, where the company was headquartered and had a state-licensed lottery retail outlet, the investigation revealed.

This technically made the purchase not a Pennsylvania lottery ticket, but a Texas lottery ticket. That deprived Pennsylvania of revenue from the sale and the tax revenue on any winnings. It's also illegal, board members learned as the investigation progressed. What if someone in Pennsylvania won the Powerball with a ticket produced somewhere else?



The backup printing arrangements also turned out to be much more than a backup. In a seven-month period, Lottery.com printed out more than 500,000 tickets worth more than \$1.1 million in Texas for out-of-state lottery players. The practice had been going on since before 2020, according to an internal memo reviewed by Bloomberg Tax.

Lottery.com had said in SEC filings that it had geolocation technology to confirm that web-based customers were in the state where they said they were located. But the internal investigation discovered that wasn't true. Anybody using the web-based system, as opposed to the mobile app, could skirt any jurisdictional requirement for ticket purchases, according to the investigation report and interviews.

"We are breaking the law in 42 different ways," one board member said a June 2022 meeting, according to a transcript obtained by Bloomberg Tax.

"I am without words. The potential for Homeland Security, AML, and all the other things that come into play is beyond breathtaking," the board member said, referring to anti-money laundering laws.

Board members told management to shut down the web-based application. In July, Lottery.com announced it was furloughing almost all employees and temporarily shutting down operations.



Tony DiMatteo.

Photographer: Dia Dipasupil/Getty Images for Tribeca Film Festival

DiMatteo, who resigned as CEO later in July, declined to comment on either the \$30 million transaction or the backup lottery ticket printing arrangement. Lever, the chief legal officer, didn't return requests for comment.

The law firm that conducted the internal investigation never got paid, according to a lawsuit filed last month.

The company's auditor quit in September, saying it could no longer rely on management's word. That firm, Armanino LLP, made headlines two months later as the auditor of the US arm of collapsed crypto exchange FTX. Armanino quit auditing public companies altogether in 2023. The firm didn't respond to requests for comment.

London Calling

The furloughs, the operations shutdown, and the fleeing auditor might have been it for the company, except for a last-ditch funding search by the original SPAC team.

Through old connections from Azerbaijan, an oil-rich former Soviet republic, they landed upon London-based Woodford Eurasia, a self-described specialist in turnaround situations and distressed assets. It was led by Nasib Piriyeve, the son of an Azerbaijani millionaire who had tried to buy the West Ham soccer club of the English Premier League in 2021. The group's non-executive director is Lord Simon Woolley of Woodford, a member of the British House of Lords. Woolley directed questions to the firm.

Piriyeve promised a \$2.5 million loan from the firm to start and up to \$50 million as long as Woodford Eurasia got to install a new board and his own CEO. The leader he chose was Sohail Quraeshi, a securities lender who most recently had served as CEO of a cannabis company.

Quraeshi was intrigued by the company's premise and Nasdaq listing. "It's a shitshow, but it's an interesting shitshow," he remembers thinking at the time.

He flew to Austin to see what he was getting into. He wasn't expecting much, given the company had paused operations and had stopped paying employees. But he was still disappointed by what he saw: a nondescript building on the side of a highway that contained three servers. "I said, this isn't a corporate office; this is a failed 7-Eleven with three goddamn machines," he said.

Money from London barely trickled in. Not "a single penny of this promised investment has arrived," former board member Richard Kivel wrote in a resignation letter, accusing a Piriyeve-blessed board member, Matthew McGahan, of taking "complete control of the board." In an SEC filing, the company said it "categorically and unequivocally refutes all statements made by Kivel as baseless" and that Kivel resigned to avoid being removed. Kivel declined to be interviewed for this story.

McGahan, who eventually became the company's CEO, also declined interview requests.

Piriyeve, in an interview, rejected the accusations of failing to fund the company or that he tried to take it over from overseas. Woodford and its subsidiaries poured in more than \$3 million, sometimes sending payments directly to vendors instead of through the company, he said.

The company reported that about \$991,000 came in. That wasn't enough for Quraeshi. He filed a notice of default on the promises he said Woodford Eurasia had made. The board fired Quraeshi the next day, Feb. 1, 2023, and replaced him with another turnaround specialist, Gustavson.

Another Round

Gustavson had dabbled in over-the-counter tech companies in Silicon Valley and was up for a new challenge. He flew to London, expecting to be there a week. He stayed more than a month, holed up in Piriye's office to try to get the company's financial records straight, make plans for re-launching ticket sales, and do a reverse stock split to boost the company's stock price and stave off a Nasdaq de-listing.

But as 2023 progressed, Gustavson said he began to suspect the board was keeping a second set of books. When the company filed its first-quarter financial statement, it was a surprise to Gustavson, who said he never even saw the document. Gustavson's electronic signature was on it, as required by law, but he said he didn't authorize it. Current officials said the company "followed its customary consent protocol and policies prior to making this filing and did the same for all other filings made by the Company" and it keeps a single set of financial records.

More red flags emerged. The original founders of Lottery.com pledged some of their stock to Woodford Eurasia as an incentive to invest in the company and help turn it around. The catch: it only could be sold if the stock rebounded above \$5, according to the terms of the funding arrangement. It never did.

Yet in May 2023, almost 5 million of DiMatteo's shares—worth almost \$2 million at the time — got sold in two different transactions, even though the stock was trading below 50 cents per share at the time, well under the \$5 threshold.

He says he has no idea who did it or who got the proceeds, but he later wrote to the transfer agent requesting a freeze on any future sales, according to a letter reviewed by Bloomberg Tax. "I did not receive a dime of my shares that were sold," DiMatteo said.

Regulatory filings reporting the stock sales bear the electronic signature of Alex Smotlak, who is a former director at Woodford Eurasia according to UK Companies House filings. Piriye declined to comment, saying Woodford Eurasia and DiMatteo had confidential commercial agreements in place.

At the same time, the company was planning its Monaco yacht party as a vehicle to promote Sports.com, which the company was trying to launch as a fan engagement platform. Two days before the Monaco Grand Prix, the company announced Sports.com's new president: Majed Al-Sorour, a director of the Premier League's Newcastle club and former managing director of Saudi Arabia's LIV golf tour.



Yacht party in Monaco.

Image: YouTube

With the company in dire straits financially, Woodford footed most of the bill for the party—around 400,000 euros, according to an invoice and emails reviewed by Bloomberg Tax. The yacht rental alone cost 175,000 euros, not counting damage from cigar burns on the furniture and blinds.

Gustavson said he was fired after raising questions about the quarterly filing he said he didn't approve. His replacement: McGahan, the board member who another director had accused of trying to take over.

Gustavson said he had heard about the party being planned, didn't want anything to do with it and didn't attend.

Still Standing

The SEC and Department of Justice are investigating the company and some of its founders over the findings of the internal investigation and other matters including the credit sales transaction, according to company filings and an SEC subpoena reviewed by Bloomberg Tax. The SEC declined to comment, as did the DOJ.

Lottery.com's near demise wiped out millions for shareholders and business partners. John Brier and Bin Tu, developers of the tech business that fuels the company's lottery data feed sold their business to Lottery.com, but allege they are still owed \$10 million in missed payments.

"We believe strongly the company itself has tremendous upside. Tremendous opportunity. It's all there," Brier said in an interview. "But not in the hands of these people."

Lottery.com in November filed its own lawsuit against Brier and his partner, Tu, alleging they stole company secrets to start a competing business with Gustavson. Their attorney said any noncompete and nondisclosure agreements were void because they never got fully paid for their work. In February, a federal judge granted an injunction, meaning the business partners could proceed with their plans.

Meanwhile, Lottery.com hasn't sold domestic lottery tickets since the spring of 2023. The app for buying mobile lottery tickets no longer exists.

DiMatteo said he believes the company is salvageable. He said he didn't profit from its problems.

"I've even gotten some death threats online," he said. "You go on Stocktwits, people believe I walked away with 2 million bucks, basically, and screwed everybody, which is completely untrue. It's insane."

McGahan, once picked by Woodford Eurasia to run the board, has become disconnected enough from Woodford that he changed the locks on his office door in London to keep Piriyeve out, Woodford claimed in a lawsuit alleging the company breached its loan agreement and omitted the breach from its last proxy statement. Woodford dropped the suit in February but is considering other legal action, the firm said.

If there had been any doubts about the nefarious intentions of McGahan and Battles, those doubts were removed on July 19, 2023 when Battles sent an email to personnel affiliated with Woodford instructing them not to come into the offices that Woodford itself had leased and paid for at 38 Saville Row "until we have completed a review of historic activities and established a new path for Lottery.com and Sports.com." The locks on the office Woodford had leased were immediately changed.

A skeleton crew of Lottery.com employees has stuck around, with the company tapping a loan from a London investment firm tied to McGahan. The stock still trades on Nasdaq, with a market cap 99 percent below its peak.

In late December, the stock price briefly quadrupled when it gave notice of a new investor for Lottery.com and Sports.com. In February, the company announced a stock-based deal to buy a sports content platform to beef up Sports.com's offerings.

The company is working to resume lottery ticket sales in 2024, and the Monaco party led to partnerships that are materializing for the company, Chief Operating Officer Greg Potts said in an interview.

"So much of what has been holding the company back are things that we're looking at in the rearview mirror," Potts said. "You have a new group of dedicated leadership and board members who are making sacrifices in order to turn this company around."

SPAC founder Ponomarev also remains a believer. "I think the technology there is great and I think that they will survive," he said. "I do believe in them despite all the stupidity that was going on."

Quraeshi, the first turnaround CEO, says he's heard this before. "Is this the perfect fraud or the perfect stupidity," he asked. "I don't know."

—with assistance from Lucca de Paoli of Bloomberg News

(Update in 11th paragraph from the bottom includes detail status Lottery.com's lawsuit against John Brier and business partners. An earlier update corrected a reference to an ownership stake in the company.)

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Callon Sued Over Disclosures Prior To \$4.5B APA Deal

By **Elaine Briseño**

Law360 (March 5, 2024, 4:49 PM EST) -- A Callon Petroleum Company shareholder has alleged in a proposed class action in Delaware Chancery Court that the company breached its fiduciary duties in connection with a pending \$4.5 billion acquisition by APA Corp. by not fully disclosing the details of another proposal.

Plaintiff William Durling said in his Monday suit that the terms of the **all-stock transaction** offer a negative premium to stockholders and the company should consider the offer from a rival bidder only identified as Company D in the complaint.

Callon has agreed to exchange its outstanding shares for 1.0425 shares of APA common stock. This represents an implied value of \$38.31 per Callon share based on APA's Jan. 3 closing price, the companies said when announcing the deal.

There is also no way Callon shareholders can be sure of the APA stock value because of its fluctuating prices, Durling said in his lawsuit. For example, on March 1, APA's common stock closed at \$30.41 per share, making it worth \$31.28 per share to Callon investors. However, that same day, Callon's common stock closed at \$31.86 per share.

The lawsuit names the company and its board of directors as defendants.

The materials provided to Callon stockholders failed to disclose certain information for stockholders to cast an informed vote, the lawsuit said. Those details include the premium closing price of Callon common stock in comparison to the rival bidder's stock price on the various dates it submitted proposals.

"Defendants have thus violated their fiduciary duties by engaging in improper partial disclosure," the complaint said. "Such omissions prevent Callon stockholders from being able to evaluate the premium being offered by Company D at key points during the sales process."

The boards of both companies have already approved the deal, which is expected to close in the second quarter of 2024. Callon stockholders are scheduled to vote on the transaction during a special meeting on March 27.

Durling is asking the court to stop the special meeting and prevent the company from taking any further steps until Callon "files a supplemental disclosure with the [U.S. Securities and Exchange Commission] curing the material nondisclosures." If the merger proceeds, he said stockholders should be able to recover damages related to the breaches of fiduciary duty.

The company was in talks with the Permian Basin-focused Company D since March 2022. It was then approached in October by APA about a potential transaction, according to the lawsuit. There was some back-and-forth between Callon and both companies before it settled on a deal with APA, according to the complaint.

"Given the evaporation of the premium to Callon stockholders from the final exchange ratio since the merger was announced, Callon stockholders would plainly deem it important to know the premium of Company D's proposed exchange ratio to Callon's last closing stock price ... so that they can at least consider the relative value offered by Company D's proposal as of such dates during the sales process," the lawsuit said.

Representatives for the parties did not immediately respond to requests for comment.

The proposed class is represented by Juan Monteverde of Monteverde & Associates PC, Blake Bennett of Cooch & Taylor PA and Joshua Fruchter of Wohl & Fruchter LLP.

Counsel information for the defendants was not available.

The case is William Durling v. Callon Petroleum Company et al., caseum 2024-0203, in the Court of Chancery of the State of Delaware.

--Additional reporting by Al Barbarino. Editing by Philip Shea.

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DocGo Hit With Investor Suit Over 'Limitless' Charter Clause

By **Donald Morrison**

Law360 (March 5, 2024, 6:16 PM EST) -- A mobile-healthcare company under scrutiny after being awarded a \$432 million contract to provide services for migrants in New York City has been hit with a stockholder suit in Delaware's Court of Chancery alleging that the company's charter contains "broad and limitless" provisions that run afoul of state corporate law.

John McDonald told the court on Monday that DocGo Inc.'s charter has an "impermissibly broad" provision granting the company and its CEO's permission to steer potential company deals to themselves through a blanket waiver of the corporate opportunity doctrine, saying its non-specificity leads to a complete relinquishment of the company's fiduciary duty of loyalty.

"Such a waiver of corporate opportunities must be specific, and a company's officers and directors may not be issued carte blanche to pursue opportunity belonging to the company," the complaint said. "Likewise, the duty of loyalty cannot be eliminated or limited."

McDonald alleges that the provision abuses the corporate opportunity waiver, which permits a company to waive its fiduciary duty for managers who find new business opportunities through their roles. He said in his complaint that the provision is both "limitless in scope and without qualification."

"There is no other reading of the waiver provision's language than that it is intentionally meant to, for all practical purposes, always be effective in about all circumstances," the complaint said. "It includes everything and excludes almost nothing."

McDonald said that according to Delaware law a waiver of fiduciary duty must be "clear and unambiguous" and that a duty of loyalty can never be waived or changed.

"[DocGo's] waiver provision violates both rules," the complaint said. "The specific power to renounce any expectancy of the corporation is narrowly confined to specified business opportunities, and it is expressly forbidden to eliminate or limit the liability of a corporate director's or officer's duty of loyalty."

DocGo has received extra scrutiny since last year, when the company was awarded a \$432 million contract to provide emergency housing and social services to thousands of migrants entering New York City. The contract was criticized for taking place **without a competitive bidding process**, with the city's comptroller **finding little evidence** that DocGo is qualified to care for the number of migrants entering the city.

Investors sued DocGo in October, **accusing it** of inflating its stock prices by overstating the efficacy of its mobile health and medical transportation services, leading to a steep decline after public reports questioned the business' services to migrants in New York City.

McDonald's suit alleges violation of Delaware General Corporation Law and seeks a declaration stating the waiver is invalid, as well as any court costs associated with the case.

Counsel for the investors and representatives for DocGo did not immediately respond to a request for comment on Tuesday.

Counsel information for DocGo wasn't immediately available on Tuesday.

The investors are represented by Blake A. Bennett of Cooch & Taylor PA.

The case is John McDonald et al. v. DocGo Inc. et al., case number 2024-0202, in the Court of Chancery of the State of Delaware.

--Editing by Rich Mills.

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Chegg Must Face Claims It Benefitted From Student Cheating

By **Sydney Price**

Law360 (March 5, 2024, 10:28 PM EST) -- A California federal judge said online education company Chegg Inc. must face a proposed class action alleging its share prices benefitted from students using the platform to cheat during the COVID-19 pandemic, saying the investors sufficiently show the defendants knew share prices would fall when online schooling became less prevalent.

The investors said in the most recent version of the suit filed in December 2022 that the defendants, who include some of Chegg's current and former executives, were aware Chegg's platform was used for cheating and knew that Chegg's earnings would suffer once students returned to in-person learning. The company attempted to curb investors' concerns by saying that its "dramatic growth" during the pandemic was the result of its sustainable business model, according to the suit.

U.S. District Judge P. Casey Pitts said Monday the suit sufficiently shows the defendants acted with scienter by making false statements.

To support their scienter theory, the plaintiffs say that various reports sent to Chegg by universities and faculty members about rampant cheating on the platform show the defendants knew of it.

For example, the plaintiffs allege a director at Texas A&M University was so "fed up with Chegg" that she emailed Chegg's CEO Dan Rosensweig directly, and three high-level Chegg representatives responded to her email. The plaintiffs also provide testimony from former employees to show that discussions about cheating on the platform were regularly held at company meetings.

Judge Pitts said the extensive communications between university officials and Chegg about rampant cheating on the platform combined with the former employees' statements meet the high bar for pleading scienter at this stage of litigation.

Additionally, lead counsel performed an empirical analysis of over 6,000 user-submitted questions in Chegg's platform archive, which Judge Pitts said supports the suit's falsity claim.

Though the defendants debated the validity of analysis in its motion to dismiss the suit, Judge Pitts said this evidence provides a particularized showing of cheating on the platform. The analysis identifies "parameters used to identify cheating, with examples; the resulting calculation of the percentage of questions containing obvious signs of cheating; and trends in the data before, during, and after the Class Period," Judge Pitts said.

"Further discovery will allow for a larger sample size and more robust statistical analysis," he said.

According to the suit, despite Chegg's assurances that its growth was due to its business model, when students started returning to classrooms, the stock price plunged by nearly 50% in a single day, from \$62.76 on Nov. 1, 2021, to \$32.12 per share the next day – erasing \$4 billion in shareholder value.

The investors have shown the decline in share price was connected to the defendants' misrepresentations by citing analyst reports from Forbes and Morgan Stanley, Judge Pitt said.

"The Ninth Circuit has held that when analysts note the probable relationship between alleged misstatements and a stock price decline, plaintiffs have adequately pleaded loss causation," Judge

Pitts said.

Motley Rice LLC attorney Christopher Moriarty told Law360 in an email Tuesday that the plaintiffs are satisfied with the order.

"Plaintiffs are very pleased with Judge Pitts' thoughtful opinion denying the motion to dismiss and appreciate the court's insightful questions during the hearing," Moriarty said. "We look forward to continuing to prosecute the action to try to secure the best possible result for the class members."

A Chegg representative told Law360 in an email that the company is "deeply committed to academic integrity," and that it will continue to vigorously defend itself in the litigation.

"Chegg is a learning platform and not a cheating platform," the representative said. "We respectfully disagree with the Judge's ruling."

The investors are represented by David R. Kaplan, Hani Y. Farah, Emily R. Bishop, Maya Saxena, Lester R. Hooker, Jonathan Lamet, Steven B. Singer and Kyla Grant of Saxena White PA and Max N. Gruetzmacher, Christopher F. Moriarty and Neli Traykova Hines of Motley Rice LLC.

Chegg is represented by Patrick E. Gibbs, Brett H. De Jarnette and Heather M. Speers of Cooley LLP and Dean S. Kristy, Jennifer C. Bretan, Fiona Tang, Sofia Ritala and Felix S. Lee of Fenwick & West LLP.

The case is Leventhal et al. v. Chegg Inc. et al., case number 5:21-cv-09953, in the U.S. District Court for the Northern District of California.

--Editing by Vaqas Asghar.

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Lordstown Ch. 11 Plan Confirmed After Settlements Reached

By **Ben Zigterman**

Law360 (March 5, 2024, 10:55 PM EST) -- A Delaware bankruptcy judge confirmed the Chapter 11 plan of electric vehicle maker Lordstown Motors Corp. over the objection of the Office of the U.S. Trustee after finding that the debtor is eligible for a discharge of its liabilities.

While the U.S. Trustee **had argued** that Lordstown isn't eligible for a discharge because it won't still be in business after exiting Chapter 11, U.S. Bankruptcy Judge Mary F. Walrath said at a hearing Tuesday that its business would continue in a different form.

"We have a case where there is evidence of the debtor's intent to actually proceed to, by merger or acquisition, acquire a business that will allow it to utilize its [net operating losses]," Judge Walrath said. "I think the debtor has a strong incentive to do that because the NOLs may be worth a billion dollars in value to its shareholders."

Lordstown **applied for bankruptcy protection in June**, with an eye to making an asset sale while extracting billions of dollars in damages from Taiwanese manufacturer Foxconn EV Technology Inc. for allegedly breaking promises to partner with the truck company.

Under its plan, Lordstown will retain its litigation accusing Foxconn of reneging on its part of the \$170 million partnership to develop electric pickup trucks, retain its common stock, and preserves its net operating losses and other tax attributes, as it pursues new business opportunities with a new board, according to court documents.

In October, Judge Walrath **approved a \$10.2 million asset sale** to LAS Capital LLC, a firm controlled by Lordstown founder Stephen S. Burns.

At Tuesday's hearing, Judge Walrath congratulated Lordstown on overcoming long odds to reach a largely consensual plan. The plan was supported by the lead plaintiff of securities litigation in Ohio, Foxconn, the U.S. Securities and Exchange Commission, and the unsecured creditors and equity security holders committees, according to court documents.

During its bankruptcy, Lordstown **reached a \$40 million settlement** with Karma Automotive, which had accused the debtor of stealing technology and employees, and last week, Lordstown **reached a \$25.5 million settlement** with the SEC in its probe into allegations of false statements made both before and after the company was publicly listed on the Nasdaq as part of a \$675 million merger with special purpose acquisition company DiamondPeak Holdings Corp.

Under that settlement, Lordstown promised to disgorge \$25.5 million to resolve two class action lawsuits filed in Ohio and Delaware, and the SEC has agreed to withdraw its \$45 million claim, according to court documents.

"The fact that the debtor, despite all odds and my internal prediction, has overcome all of the obstacles that were placed in its path, pre- and post-petition, including all the settlements," Judge Walrath said, "I think the debtor has climbed the mountain and shown that it is likely to achieve what it puts its mind to."

The settlement in the securities suit in the Delaware Court of Chancery was filed Monday.

Under the settlement, the Delaware plaintiffs will drop their suit and a \$15.5 million settlement trust will be created to distribute funds to class members. The settlement also will pay the plaintiffs' attorneys up to 22.5% of the settlement fund.

The Delaware Court of Chancery suit was **filed in December 2021** by two former DiamondPeak stockholders against DiamondPeak CEO David Hamamoto, four other former members of the DiamondPeak board, Diamond Peak Sponsor LLC and two of its former directors.

The plaintiffs claim that the directors of DiamondPeak breached their fiduciary duties to a class of stockholders by failing to disclose certain information about Lordstown and by putting their own interests first in the Lordstown transaction.

After Lordstown filed for bankruptcy in June 2023, the chancery action was allowed to continue when Judge Walrath declined to extend the automatic stay to the suit.

A representative of the U.S. Trustee's office declined to comment. Representatives of the other parties did not immediately respond Tuesday to requests for comment.

Lordstown is represented in the bankruptcy case by Donald J. Detweiler and Morgan L. Patterson of Womble Bond Dickinson, and Thomas E. Lauria, Matthew C. Brown, Fan B. He, David M. Turetsky, Jason N. Zakia, Roberto Kampfner, Doah Kim and RJ Szuba of White & Case LLP.

The U.S. Trustee is represented by Benjamin Hackman.

The official committee of unsecured creditors is represented by David M. Fournier, Tori L. Remington, Francis J. Lawall, Deborah Kovsky-Apap and Sean P. McNally of Troutman Pepper Hamilton Sanders LLP.

The official committee of equity security holders is represented by Eric J. Monzo and Brya M. Keilson of Morris James LLP, and Robert J. Stark, Bennett S. Silverberg, Michael S. Winograd, Sharon I. Dwoskin and Matthew A. Sawyer of Brown Rudnick LLP.

The settlement class in the chancery case is represented by Gregory V. Varallo, Jeroen van Kwawegen, Thomas G. James, Margaret Sanborn-Lowing and Glenn R. McGillivray of Bernstein Litowitz Berger & Grossmann LLP, D. Seamus Kaskela of Kaskela Law LLC, and Gustavo F. Bruckner and Samuel J. Adams of Pomerantz LLP.

The defendants in the chancery case are represented by Raymond J. DiCamillo, Kevin M. Gallagher, Alexander M. Krischik, Edmond S. Kim and Nicholas F. Mastria of Richards Layton & Finger PA.

The bankruptcy case is In re: Lordstown Motors Corp. et al., case number 1:23-bk-10831, in the U.S. Bankruptcy Court for the District of Delaware.

The chancery case is In re Lordstown Motors Corp. Stockholders Litigation, case number 2021-1066-LWW, in the Court of Chancery of the State of Delaware.

--Additional reporting by Hilary Russ and Jessica Corso. Editing by Alex Hubbard.



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Splunk Investors Get Final OK For \$30M Deal, \$7.5M Atty Fees

By **Sydney Price**

Law360 (March 5, 2024, 3:42 PM EST) -- A California federal judge has granted final approval to a \$30 million settlement, including \$7.5 million in fees for class counsel, to resolve a securities class action accusing software company Splunk of lying about strategies it used to meet cash flow goals.

U.S. District Judge Jon S. Tigar called the settlement fair, reasonable and adequate for the class in **his order** and final judgment Monday. Class counsel said the \$30 million recovery represents between approximately 5% and 20.5% of the realistic maximum damages for the class, assuming that the lead plaintiff Louisiana Sheriffs Pension and Relief Fund prevailed on class certification and on all liability issues at trial and appeal, according to the order.

The settlement, which was preliminarily approved in September, covers all Splunk shareholders who bought or otherwise acquired common stock from May 21, 2020, to Dec. 2, 2020. It stems from multiple related class actions filed by Splunk investors who alleged that the company misrepresented its operating cash flow and strategies that were purportedly being used to meet its financial goals.

Splunk denies any wrongdoing or liability and is only settling to eliminate the burden and expenses associated with further litigation, according to an accompanying notice of pendency of class action and proposed settlement filed in September.

According to the consolidated complaint filed in June 2021, Splunk had negative operating cash flows since March 2020. The investors claimed that Splunk's then-CEO Douglas S. Merritt had assured investors that the company would turn a corner by 2022 and would achieve more than \$1 billion in positive operational cash flows by 2023.

Splunk told investors it would reach its goals with continuous investments in marketing and the hiring of additional sales staff to unlock revenue growth, the suit says. The plaintiffs claimed that the market potential for Splunk products was more than \$81 billion. However, the company didn't meaningfully tap into that opportunity at the time, according to the investors. Splunk kept assuring shareholders it was investing in marketing efforts and hiring sales personnel while avoiding layoffs, which led its stock price to climb.

But Splunk never did continue investing in marketing during the class period, nor did it continue hiring new sales staff, the complaint said. Rather, the company "skipped" on operating expenses, suspended all marketing investments, implemented a lengthy hiring freeze and laid off critical employees, including the entire unit responsible for bringing in new business, the plaintiffs said. The latter layoffs hampered Splunk's ability to generate revenue and made it tough to find customers to buy its products.

The cutbacks resulted in quarterly revenues plummeting 11% year over year and net losses expanded, the plaintiffs said. They also claimed those corporate decisions were hidden from shareholders until early December 2020.

When the truth was revealed, securities analysts who had covered the company for years reported that they were "blindsided," including defendants' withdrawal of their guidance that they would achieve more than a billion dollars in positive operational cash flow by 2023, the consolidated complaint said. Splunk's stock price declined 23% in a single trading day, erasing more than \$7.7 billion in shareholder value, according to the suit.

Counsel for the parties did not immediately respond to requests for comment Tuesday.

Louisiana Sheriffs Pension and Relief Fund is represented by Jonathan D. Uslaner, Lauren M. Cruz and Caitlin C. Bozman of Bernstein Litowitz Berger & Grossmann LLP.

The Splunk defendants are represented by Sara B. Brody, Nicole M. Ryan and Matthew P. Henry of Sidley Austin LLP.

The case is In re: Splunk Inc. Securities Litigation, case number 4:20-cv-08600, in the U.S. District Court for the Northern District of California.

--Additional reporting by Gina Kim. Editing by Stephen Berg.

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Meta Tells Chancery It Didn't 'Utterly Fail' To Stop Exploitation

By **Leslie A. Pappas**

Law360 (March 5, 2024, 5:08 PM EST) -- Shareholders accusing Meta's leaders of "utterly failing" to eliminate pedophilia, human trafficking and child sexual exploitation on its social media platforms didn't ask enough about the company's efforts and haven't shown any "corporate trauma," an attorney for Meta's board told Delaware's Court of Chancery on Tuesday.

There are "hundreds of millions of daily active users" on Instagram and Facebook and "nearly 99% of issues were identified," David E. Ross of Ross Aronstam & Moritz LLP argued during a virtual hearing on behalf of Meta Platforms Inc., CEO Mark Zuckerberg, and more than 20 current and former officers and directors.

Meta is asking Delaware's Chancery Court to **dismiss the suit** or alternatively stay the case until a **related suit in Texas** is resolved.

"These are horrible situations. There's no question about that," Ross said, "but this is not an utter failure."

Meta has removed 16,000 problematic groups and identified millions of issues on its own, Ross argued. The company has a team of 40,000 working on user safety and security, with the company raising 55,000 issues every day, he said.

The derivative lawsuit, which shareholders led by the Employees' Retirement System of the State of Rhode Island first **filed in March 2023**, alleges Meta's board failed to curb rampant and systemic sex trafficking, human trafficking and child sexual exploitation on the company's social media platforms — even in the face of widespread criticism, congressional inquiries and "mountains of evidence" that predators were using the platforms.

"Meta hasn't given us any minutes that [show] these matters were ever discussed at a board meeting," the shareholders' attorney, Christine M. Mackintosh of Grant & Eisenhofer PA, told the court Tuesday, urging it to preserve the suit. The "handful of board presentations" that shareholders obtained through a demand for corporate records "further confirm that Meta didn't put into place anything remotely resembling active oversight," she said.

Meta has become the face of public outcry in response to online sexual abuse, Mackintosh said. The company has incurred "substantial" costs defending against challenges to its practices, including a **recent complaint** from New Mexico's attorney general, she said.

Ross countered that the shareholders sent a "very targeted" demand for information, so the documents Meta produced didn't fully reflect all the work it was doing. "There was nothing preventing them from asking us for more information," he said.

The complaint also fails because it doesn't show that Meta suffered any "corporate trauma" — a requirement under Delaware law since the shareholders are alleging the board acted in bad faith, Ross argued. For example, he said, the complaint says nothing about criminal charges against the company or a settlement that the company has had to pay as a result of the alleged wrongdoing.

Vice Chancellor J. Travis Laster, the Chancery Court judge overseeing the case, pushed Ross to explain why Meta didn't voluntarily offer more information in response to the shareholders' request

for documents. If it was clear that shareholders weren't getting all the information that the company had to offer on its user risk and safety efforts, the vice chancellor asked, might it not have been "prudent" or "wise" for the company to simply provide more information?

Ross replied that in the context of a demand under Section 220 — the section of Delaware General Corporation Law that allows shareholders to ask for corporate books and records — the company wasn't required to turn over more information than what shareholders specifically asked for, and in some cases, it might not have been appropriate to turn it over if there hadn't been a specific request.

The vice chancellor turned to the question of corporate harm and business risk. If Meta's board was aware that a "bomb of eventual exposure of being involved in child pornography was coming," would it be enough of a "red flag" to conclude that the directors breached their fiduciary duties to the company by not addressing it?

Ross replied that the board and the company had been working to address the issue and were not as negligent as plaintiffs allege.

Vice Chancellor Laster took the matter under advisement and did not say when he would make a decision.

The shareholders are represented by Christine M. Mackintosh, Rebecca A. Musarra, Edward M. Lilly and Barbara J. Hart of Grant & Eisenhofer PA and William S. Norton, Meredith B. Weatherby and Serena Hallowell of Motley Rice LLC.

Meta and the directors and officers are represented by Charles S. Duggan and Paulina Perlin of Davis Polk & Wardwell LLP and David E. Ross, R. Garrett Rice, Holly E. Newell and Thomas C. Mandracchia of Ross Aronstam & Moritz LLP.

The case is Employees' Retirement System of the State of Rhode Island et al. v. Mark Zuckerberg et al., case number 2023-0304, in the Court of Chancery of the State of Delaware.

--Additional reporting by Hailey Konnath and Henrik Nilsson. Editing by Janice Carter Brown.



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Judges Unsure On Atty Sanctions In Robinhood Spam Suit

By **Greg Lamm**

Law360 (March 5, 2024, 8:30 PM EST) -- Class counsel sanctioned \$750,000 for helping instigate a spam text suit against Robinhood Financial likely engaged in "shenanigans," a Washington appeals judge said Tuesday, though a colleague on the bench questioned whether those sanctions should stick if Robinhood was nevertheless liable in the case.

The case involves accusations that one of the appointed class counsel and his brother orchestrated the lawsuit by forwarding texts about Robinhood's "Refer a Friend" marketing program to plaintiffs, who then claimed they did not know who sent the messages.

A state court judge imposed \$750,000 in sanctions and fees for filing a frivolous lawsuit in the case Isaac Gordon v. Robinhood Financial LLC. But that was before a federal judge in a similar case ruled that Robinhood could still be on the hook for violating anti-spam law if the company assisted in the text marketing program.

During Tuesday's hearing, Judge Robert Lawrence-Berrey noted that the Gordon case before the three-judge panel was first filed in state court, then moved to federal court, only to be sent back to state court.

Judge Lawrence-Berrey said that appointed counsel Brian Cameron and plaintiff Gordon were held liable for their actions in federal court when they were not under the constraints of state court rules.

"The shenanigans, though, that it seemed like the trial court and the federal court found that occurred, those shenanigans weren't limited to the complaint," Judge Lawrence-Berrey said, adding that there were also problems with discovery in federal court.

An attorney for Robinhood, Kenneth E. Payson of Davis Wright Tremaine LLP, said the lawsuit was frivolous and should not have been filed in the first place in state court.

Judge Rebecca Pennell said it appears there was a degree of misconduct by Gordon, who "knew full well" where the text messages were coming from.

But Judge Pennell said that might be irrelevant because of the ruling by U.S. District Court Judge Barbara J. Rothstein. In a case in which Robinhood **agreed to pay \$9 million** to resolve proposed class claims, Judge Rothstein determined that as long as Robinhood played a role in the Refer a Friend program, it did not matter that the spam texts were coming from class counsel, Judge Pennell said.

Judge Pennell said that would not be palatable to her, but she asked whether an attorney working on the case could say, "Hey, brother of mine, why don't you sign up for Robinhood Financial and send a bunch of text messages to people?"

Judge Pennell asked whether there could be a valid claim if the plaintiff does not collude with the attorney.

"Is it possible for an attorney to do that and that to be ethical or not show a violation as long as the recipient is not asking for or not aware of the texts?" Judge Pennell said.

Payson said it would be unethical for an attorney to cause the very injury that the attorney was suing for on behalf of a client.

"That would be akin to plaintiffs' counsel dropping a banana peel in front of storefront so their plaintiff could slip on it," Payson said.

Philip A. Talmadge of Talmadge/Fitzpatrick, representing the plaintiffs, urged the court to reverse the trial court's ruling on sanctions, saying the penalties were an attempt by Robinhood to chill consumer litigation.

Talmadge told the panel there was an issue of whether Gordon consented to receive unsolicited spam messages.

Judge Pennell interrupted Talmadge, saying she did not understand that to be the case. Judge Pennell said text messages seemed to have been modified to conceal who had sent them when Gordon first filed his complaint claiming he didn't know whom they came from.

"When I read the complaint, it was Mr. Gordon who said, 'I don't know who sent them to me.' And that's just false by anyone who knows how to read a text message," Judge Pennell said.

"But nonetheless, in the complaint there is a misstatement," Judge Pennell said.

In his original complaint filed in 2019, Gordon accused Robinhood of violating the Washington Consumer Protection Act and the Washington Commercial Electronic Mail Act by sending "refer-a-friend" texts to residents who had not previously consented to receive them.

Robinhood alleged that the claims in the original complaint were manufactured by one of the appointed counsel, Cameron, and his brother.

A state court judge dismissed the complaint with prejudice as frivolous, and awarded \$750,000 in sanctions and fees to Robinhood.

Judges George Fearing, Robert Lawrence-Berrey and Rebecca Pennell sat on the panel for the Washington State Court of Appeals, Division III.

Gordon is represented by Kirk Miller of Kirk D. Miller PS, Brian G. Cameron of Cameron Sutherland PLLC and Philip A. Talmadge and Aaron P. Orheim of Talmadge/Fitzpatrick.

Robinhood Financial is represented by Kenneth E. Payson and Lauren Rainwater of Davis Wright Tremaine LLP.

The case is Isaac Gordon v. Robinhood Financial LLC, case number 386236, in the Washington State Court of Appeals, Division III.

--Editing by Peter Rozovsky.



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Poland Springs Sued Over Microplastics In 'Natural' Water

By **Hailey Konnath**

Law360 (March 5, 2024, 10:49 PM EST) -- Poland Springs is being falsely marketed as "100% natural spring water," a description that isn't accurate thanks to the "dangerous levels of microplastics" found in the bottled water, according to a proposed class action filed Tuesday in New York federal court.

The consumers said in their complaint that Poland Spring manufacturer BlueTriton Brands Inc. touts the bottled water as "nothing but natural spring water." The company has profited greatly from this misrepresentation, as it's able to charge a price premium for Poland Spring because of its purported purity, per the complaint.

But every bottle of Poland Spring contains microplastics, which are fragments of plastic found in 90% of bottled water tested in studies, the consumers said. Microplastics could be toxic, leading to health problems like heart issues, chronic inflammation and endocrine disruption, they claimed.

On top of that, Poland Spring contains "alarming levels" of phthalates, a synthetic chemical used to increase the flexibility, transparency and durability of plastic products, they said. Phthalates, too, have been linked to health problems, including with the heart and hormone levels, according to the consumers.

"A reasonable consumer purchases Poland Spring believing they are getting a bottle of nothing but spring water from nature," the consumers said. "Reasonable consumers, however, would not deem Poland Spring to be 100% natural spring water if they knew that the water in each bottle contains phthalates and microplastics."

The suit was filed by named plaintiff Jennifer Moore, a New York resident who said she purchased bottles of Poland Spring based on labels' representations that they contained only natural spring water.

Moore is looking to represent a nationwide class of potentially millions of individuals who've purchased Poland Spring bottled water within the applicable statute of limitations. She's also looking to represent a New York subclass.

Moore is alleging breach of express warranty, unjust enrichment and violations of New York General Business Law. She's also hoping to secure unspecified damages, restitution, disgorgement of profits and an order forcing BlueTriton to put out a "corrective advertising campaign" to inform the public about the true contents of Poland Spring water, according to the complaint.

"While it is undeniable that Poland Spring is a leading brand in the bottled water space in the northeastern United States and a financial success, defendant's success has been the result of deceptive business practices in the marketing and sale of Poland Spring," Moore said.

Poland Spring is **already facing** allegations its manufacturer lied about the source of its spring water. That litigation was filed against Nestle Waters North America Inc., of which BlueTriton used to be a subsidiary.

Also on Monday, Nestle **was accused** of misleading consumers as to the purity of its Perrier mineral water. The consumers in that suit claim that the water actually comes from a contaminated spring that requires filtration and treatment.

BlueTriton and counsel for the consumers didn't immediately respond to requests for comment late Tuesday.

Moore is represented by Tina Wolfson and Bradley K. King of Ahdoot & Wolfson PC.

Counsel information for BlueTriton wasn't immediately available Tuesday.

The case is Jennifer Moore v. BlueTriton Brands Inc., case number 1:24-cv-01640, in the U.S. District Court for the Eastern District of New York.

--Editing by Jay Jackson Jr.

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Rail Giants Get Some Docs Kept Out Of Fuel Surcharge MDL

By **Bryan Koenig**

Law360 (March 5, 2024, 8:45 PM EST) -- A D.C. federal judge has kept more than two dozen key documents out of a long-running multidistrict litigation accusing the country's four largest railroad companies of a fuel surcharge price-fixing scheme while permitting at least portions of over a dozen others that didn't qualify for an exclusion afforded discussions about shared traffic.

U.S. District Judge Paul L. Friedman's Monday ruling is the culmination of a multiyear fight over Section 10706 of the U.S. Code, created in 1980 to prevent antitrust trials from hearing evidence based on conversations between rail carriers about interline shipping, provided those conversations by themselves would not constitute an antitrust violation.

One by one, Judge Friedman went through more than 40 documents, some of which are duplicates, including deposition transcripts, internal carrier communications, communications between at least two of the rail giants and meeting minutes, as he weighed what to permit for use by shippers suing Union Pacific Railroad Co., CSX Transportation Inc., Norfolk Southern Railway Corp. and BNSF Railway Co.

Guiding the ruling was a D.C. Circuit panel's **May 2022 decision** upholding the majority of a February 2021 order in which Judge Friedman said Section 10706 can't be used as **a blanket ban** on evidence against the rail companies just because the material covers discussions among them about so-called interline rail traffic where cargo is transported by more than one carrier. The U.S. Department of Justice also weighed in, saying a blanket ban would amount to **"a de facto immunity"** for allegedly anti-competitive conduct so long as it happened to include interline traffic.

Based on the appellate court's guidance, Judge Friedman on Monday excluded multiple exhibits he said were dominated by discussions, either internal or between carriers, on interline traffic. While some of the excluded material also discussed non-interline traffic, Judge Friedman said those instances didn't change the focus away from shared interline traffic, noting that the D.C. Circuit specifically said to exclude material where non-interline shipping discussions "did not change the focus of the discussion or agreement away from the participating railroads' shared, identifiable interline movements."

Conversely, Judge Friedman admitted deposition transcripts where the witnesses' discussion of interline traffic could be redacted. He also admitted other material containing "segregable" references to interline traffic with redactions, as well as segregable, non-interline portions of discussions about a June 2003 meeting between two railroads.

"The defendants assert that the meeting agenda and correspondence are protected under Section 10706 because the relationship between these two railroads was 'overwhelmingly one between interline connecting carriers,'" Judge Friedman said. "The court finds that the defendant railroads have not carried their burden."

"Although these railroads may have shared interline traffic, the mere fact that two railroads share interline traffic is insufficient. The meeting agenda suggests that the discussion primarily focused on general industry concerns, not on specific interline movements," he said. "The court is not persuaded that the meeting focused on interline movements, although the agenda indicates in a very few places that certain sub-discussions focused on interline movements (e.g., discussions about specific gateways or gateway performance)."

Union Pacific welcomed the ruling in a statement.

"We are pleased with the decision as it upholds the federal statute aimed at promoting discussions among railroads to facilitate transportation options for America's shippers reliant on two or more railroads for moving their goods across the country," Union Pacific said. "The ruling also fosters competition in the transportation industry, where railroads compete directly with trucks and other modes of transportation. Importantly, the ruling properly prohibits such legitimate discussions from being misused in a court of law."

Norfolk Southern and CSX declined to comment Tuesday. Representatives for BNSF and the plaintiffs did not immediately respond to requests for comment.

Monday's ruling could have important **implications** for the five cases in the current MDL, a joined case from Oxbow Carbon & Minerals LLC and will also affect nearly 100 cases in **a subsequent MDL**. An attorney for the rail companies previously said most, if not all, the plaintiffs' "substantial evidence" comes from meetings discussing interline shipping.

The centrality of the evidence has made the Section 10706 dispute hard-fought, and led the D.C. Circuit to hold that it's not enough for communications to simply mention interline shipping to qualify for exclusion, they must show "that the movements at issue are the participating rail carriers' shared interline traffic."

However, the appellate court also pushed back on Judge Friedman's insistence that to be excluded, evidence must speak to "a specific shipper, shipments or destinations."

Instead, "more general discussions or agreements may suffice," according to the appellate ruling.

The case concerns shippers' claims that the railway companies worked together for years to fix the price of fuel surcharges and agreed not to compete with one another on those prices to keep them high. The alleged scheme cost shippers that rely on railway transport billions of dollars, according to the suit.

The rail companies have been battling the claims since 2007 and has already resulted in two parallel multidistrict litigation proceedings before two different judges in D.C. federal court.

The older MDL, being overseen by Judge Friedman, won class certification in 2012 but lost it years later, following a U.S. Supreme Court precedent that raised the standard for showing antitrust damages in class actions.

After the D.C. Circuit refused to recertify the class, new cases started cropping up, and were eventually consolidated into an MDL before another judge.

Oxbow is represented by Robins Kaplan LLP.

The shippers are represented by Hausfeld LLP, Quinn Emanuel Urquhart & Sullivan LLP and Vinson & Elkins LLP, among others.

Union Pacific is represented by Latham & Watkins LLP, Jones Day and Massey & Gail LLP.

BNSF is represented by Munger Tolles & Olson LLP, Steptoe & Johnson LLP, Wilson Sonsini Goodrich & Rosati PC and Gibson Dunn & Crutcher LLP.

CSX is represented by Crowell & Moring LLP.

Norfolk Southern is represented by Skadden Arps Slate Meagher & Flom LLP and Arnold & Porter.

The MDL case is In re: Rail Freight Fuel Surcharge Antitrust Litigation — MDL 1689, case number 1:07-mc-00489, in the U.S. District Court for the District of Columbia. The joined case is Oxbow Carbon & Minerals LLC et al. v. Union Pacific Railroad Co. et al., case number 1:11-cv-01049, in the U.S. District Court for the District of Columbia.



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Terraform Says Creditors Sabotaging Dentons Retention

By **Emily Lever**

Law360 (March 5, 2024, 9:25 PM EST) -- A Delaware bankruptcy judge on Tuesday allowed Terraform Labs unsecured creditors time to catch up on a dispute over the debtor's Denton's retention, a request Terraform dubbed "sabotage" of its defense in an upcoming \$40 billion securities fraud trial.

In a virtual hearing, U.S. Bankruptcy Judge Brendan L. Shannon approved the newly-appointed committee of unsecured creditors' request for an adjournment so that it would have time to get up to speed on a dispute with the U.S. Trustee and the U.S. Securities and Exchange Commission over Terraform's retention of Dentons, which is now set to be duked out next week. The judge overruled Terraform's objection to the adjournment, which it said would be ruinous to its preparation for the start of its securities fraud trial on March 25—deliberately so, Terraform's counsel argued.

"This is a committee of unsecured unliquidated claimants whose only chance at recovery is if the debtor loses an existential securities fraud case," Terraform counsel Ronit J. Berkovich of Weil Gotshal & Manges LLP told the court. "Their incentive is to do all they can to sabotage the debtor's defense and that's what you see in action now."

Because Terraform's arguments in the hearing were new to the committee and the trustee and different from the briefs it had filed, Judge Shannon said it would be improper to rule on them that day.

"At this time I am not prepared to ascribe ill intentions to the committee's request for an adjournment," Judge Shannon said. "As a matter of fact, I regard it as pretty routine."

Judge Shannon asked the parties to return to court in a week's time to make their arguments about the SEC's concerns over the \$70 million retainer the crypto project wants to set aside for legal defense. In a **response** filed Monday, Terraform called the objection — which was joined by the U.S. Trustee — a "troubling example of government overreach" and an attempt to disadvantage it ahead of a fast-approaching trial.

The SEC brought that suit in February 2023, accusing Terraform and founder Do Kwon of extensive securities fraud. The suit stems from Terraform's woes in May 2022. The company used an algorithm to adjust supply and demand between stablecoin TerraUSD and its Luna token. When Terra lost its dollar peg as investors dumped both the stablecoin and Luna, the Terraform ecosystem crashed, embroiling a number of cryptocurrency ventures in the chaos.

The \$70 million Dentons retainer is necessary, and pushing off arguments about the issue would further distract the team from the round-the-clock work it must do to prepare for trial, argued Berkovich, saying, "Sabotaging the litigation is what an adjournment would do."

Counsel for the committee — which also objected to the Dentons retention agreement — argued their client's request for an adjournment was only natural given that it needed to get up to speed on a complex case and had been appointed mere days ago, and that its questioning was not meant to undermine the debtor but to conduct necessary due diligence.

"Our three members were appointed by the U.S. Trustee to serve as fiduciaries for unsecured creditors, and they're questioning the debtor's business judgment in pursuing bet-the-company litigation," said Aaron Colodny of White & Case. "They don't know what the wager is, they don't know

what the return is after the bet: they seem content to make a \$70 million retainer and proceed down a no-holds-barred litigation path."

Berkovich disputed the idea that Terraform was blowing all its resources on "pursuing" high-stakes litigation, saying it had no choice.

"We are the defendant," Berkovich said. "If we lose, there will be no enterprise value, because the SEC will take it all."

Berkovich also said the proposed counsel for the committee would bring too much "firepower" to what she described as "our simple case, which doesn't have sexy crypto issues like FTX," noting that White & Case and McDermott represent the unsecured creditors' committees in several high-profile bankruptcies — Celsius and Voyager, respectively — and that the debtor did not want to be embroiled in the wider crypto collapse. Furthermore, Celsius has possible claims against Terraform's estate, according to Berkovich.

As for the unsecured creditors' committee itself, it includes securities fraud claimants who are current or potential plaintiffs in the SEC case, meaning they only get paid if Terraform loses the \$40 billion suit — a loss that would be to the detriment of general unsecured creditors since it would wipe out the estate, Berkovich contended.

"These claimants' only chance at a recovery is if the debtor loses," Berkovich said. "The unsecured creditors' committee's interests are diametrically opposed to the interest of general unsecured claimants."

Linda Richenderfer, counsel for the U.S. Trustee's Office, said she was "flabbergasted" by the debtor's arguments and had received no prior indication that they would be aired.

"Litigation by ambush is not what I thought was going to be the course of this bankruptcy case," Richenderfer said.

The trustee counsel also pushed back against Terraform's argument that all the securities holders' claims would necessarily be subordinated, as Berkovich claimed in her argument that the securities holders had no hope of getting paid through a reorganization and thus could only see a recovery by sinking the company. The securities holders took losses as a result of Terraform's crash and therefore can try to bring claims in the normal course of bankruptcy, the trustee's counsel said.

"When the de-pegging occurred there was a huge loss of money by many, many people," Richenderfer said. "They are subordinated because they bought securities? I can't get my head around that."

The U.S. Trustee previously expressed doubts about whether Terraform actually qualified for bankruptcy, citing a Third Circuit decision in the bankruptcy case of Johnson & Johnson's talc unit to question whether Terraform is in fact facing immediate financial distress. In that appeals case, the circuit court dismissed LTL Management's first bankruptcy on the basis its lack of financial problems meant it couldn't file for Chapter 11 protection in good faith.

In late December, U.S. District Judge Jed S. Rakoff sided with the SEC in ruling that Terraform sold unregistered securities. Judge Rakoff denied both parties' motions for summary judgment on the SEC's fraud claims, which will be argued in the trial set to start March 25.

Terraform **filed for Chapter 11 bankruptcy protection** on Jan. 21. After the collapse, Terraform began focusing on software development. The company currently holds \$28 million of bitcoin, \$7 million of other cryptocurrencies and about 155 million in Luna with an estimated value of about \$87 million, according to its bankruptcy declaration.

Terraform is represented by Ronit Berkovich, Jessica Liou and F. Gavin Andrews of Weil Gotshal & Manges LLP and Paul N. Heath, Zachary I. Shapiro and Matthew P. Milana of Richards Layton & Finger PA.

The official committee of unsecured creditors is represented by White & Case LLP and McDermott Will

& Emery LLP.

The bankruptcy case is In re: Terraform Labs Pte. Ltd., case number 1:24-bk-10070, in the U.S. Bankruptcy Court for the District of Delaware.

The SEC case is Securities and Exchange Commission v. Kwon et al., case number 1:23-cv-01346, in the U.S. District Court for the Southern District of New York.

--Additional reporting by Vince Sullivan, Aislinn Keely, Lauren Berg and Alex Wittenberg. Editing by Alex Hubbard.

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