

Southern District of New York: Extensive and Reasonably Specific Warnings in Offering Materials Constituted a Real Warning to Investors (Securities Law Alert)

06.01.22



(Article from *Securities Law Alert*, May 2022)

For more information, please visit the [Securities Law Alert Resource Center](#)

On April 25, 2022, the Southern District of New York dismissed a putative securities fraud class action against a China-based, U.S.-listed technology company and certain of its employees and directors alleging that the company's offering materials contained false and misleading statements and omitted material facts in violation of Sections 11 and 15 of the Securities Act. [Yaroni v. Pintec Tech., 2022 WL 1215450 \(S.D.N.Y. 2022\) \(Furman, J.\)](#). The court held that plaintiff failed to allege that the offering materials contained misrepresentations and omissions as to the company's internal controls because the controls-related warnings were extensive and reasonably specific, not generic or boilerplate, such that they constituted a real warning to investors. The court further determined that plaintiff failed to allege facts suggesting that the company knew or should have known about the internal control weaknesses at the time of the IPO.

Within months of the company's IPO, the price of its American Depositary Shares ("ADSs") declined sharply. Subsequently, the company's ADS price also fell following both the delayed filing of its 2018 Annual Report on Form 20-F and negative company disclosures. Plaintiff sued claiming that defendants made material misstatements or omissions in the company's offering materials on various subjects,^[1] including the company's internal controls. Plaintiff alleged that the warnings in the offering materials on "the *potential* risk of ineffective internal controls over financial reporting and the *possible* restatement of prior financial statements were improper because these harms had already materialized as of the IPO."

The court concluded that each claim failed as a matter of law. As to the internal controls allegations, the court explained that under *In re ProShares Trust Sec. Litig.*, 728 F.3d 96 (2d Cir. 2013), "when a registration statement warns of the exact risk that later materialized, a section 11 claim will not lie as a matter of law." The court determined that the warnings in the offering materials about the company's internal controls constituted a real warning. The court pointed out that, at the time of the IPO, the company did state that: (i) it had limited accounting personnel and warned that management had not completed an assessment of the effectiveness of its internal controls; (ii) its auditor had not audited its internal controls; (iii) a limited audit identified a material weakness (the company lacked sufficient financial reporting and accounting personnel with appropriate knowledge of GAAP and SEC reporting requirements); and (iv) it might identify additional material weaknesses in the future and that it might be required to restate its financial statements.

The court observed that “critically, to the extent the Complaint alleges that the warned-of risks had materialized, it does not allege that [the company] knew or should have known of that fact at the time of the IPO.”

[1] Plaintiff claimed that defendants made material misstatements or omissions concerning: (1) the company’s internal controls, its audit committee, and auditor; (2) cash loans made to its former parent company outside the ordinary course of business; (3) a loan made to another company; (4) the company’s revenue recognition practices; and (5) certain line items in the company’s financial statements.

Authors and
Contacts

Meaghan Kelly
Partner
mkelly@stblaw.com
+1-202-636-5542

George Wang
Partner
gwang@stblaw.com
+1-212-455-2228

Cheryl Scarboro
Of Counsel
cscarboro@stblaw.com
+1-202-636-5529

