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Litigators of the Week: Summary Judgment Win For COVID Test Maker in Securities Fraud Suit Targeting Accuracy Claims

By Ross Todd
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It's one of those archetypal pandemic business stories, but with a securities litigation twist.

Before the COVID-19 pandemic, Co-Diagnostics Inc., the maker of diagnostic tests for diseases including tuberculosis and HIV, faced the possibility of having its stock delisted by NASDAQ, with share prices hovering under a dollar per share.

After the company developed a PCR diagnostic test for COVID-19 and secured lucrative government contracts abroad and in the U.S., including with the testing programs in Utah, Iowa and Nebraska, share prices soared, reaching more than $23 by late spring 2020.

But then, after health officials cautioned against the prospects of any test being 100% accurate, the company was hit with securities fraud claims by investors who claimed the stock price had been inflated by the company's statements about the performance of its test.

After the case survived a motion to dismiss, Co-Diagnostics brought on **Doug Greene**, **Genevieve York-Erwin** and their team at **Baker & Hostetler**. U.S. District Judge Jill Parrish last week sided with them on summary judgment. After finding the plaintiff's economic expert failed to consider the company's mixed earning statement released around the same time as the alleged corrective statements, the judge found the plaintiffs couldn't show loss causation.

Courtesy photos

Doug Greene, left, and Genevieve York-Erwin, right, of Baker & Hostetler.

Lit Daily: Who is your client and what was at stake?

Doug Greene: Our clients are Co-Diagnostics Inc., a molecular diagnostics company headquartered in Salt Lake City, and several of its current and former directors and officers.

The lead plaintiff and class representative is Gelt Trading Ltd. At issue was Co-Diagnostics' May 1, 2020 press release that disclosed, among other things, that its Logix Smart COVID-19 test demonstrated "100% sensitivity and 100% specificity"—well-defined scientific metrics—across independent evaluations. Gelt Trading alleged that the press release was false and/or misleading because it conveyed to investors that the Logix Smart test was "100% accurate," allegedly inflating Co-Diagnostics' stock price. Gelt Trading claimed that this artificial inflation was removed, and investors suffered losses, when Co-Diagnostics' stock price dropped on May 15, 2020, following three disclosures that allegedly revealed the press release to be false. Gelt Trading asserted claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934.

How did this matter come to you and the firm?

Greene: Co-Diagnostics engaged us to defend a separate, later-filed securities class action in the Southern District of New York, on the recommendation of one of its D&O insurers. The court in *Gelt Trading* had recently denied Co-Diagnostics' motion to dismiss, and the litigation was in the early stages of discovery. After working with us for a while on the later-filed case, Co-Diagnostics and the individual defendants decided to engage us to defend the *Gelt Trading* case as well.

Who all is on your team and how did you divide the work?

Gen York-Erwin: We were lucky to have help from a variety of excellent colleagues on this matter, but the core group was as follows:

- Doug led and oversaw our team's work throughout the litigation, steered our strategic decisions, helped work through our toughest issues, shaped our summary judgment and *Daubert* arguments and kept our clients comfortable
- I drafted and argued our summary judgment motion and our opposition to plaintiff's motion for partial summary judgment, managed much of the team's day-to-day litigation efforts, worked with **Zach Taylor** and **Marissa Peirsol** to develop the economic and industry expert record and the *Daubert* motions and prepared and defended our industry experts at deposition
- Zach took the deposition of plaintiff's economic expert (Mr. Bettencourt), drafted and argued our *Daubert* motion to exclude that expert's testimony, prepared and defended our economic expert witness and other fact witnesses at deposition and managed much of the document discovery in the case
- Marissa drafted and argued our *Daubert* motion to exclude plaintiff's industry expert (Dr. Westgard), drafted and argued our opposition to plaintiff's motion to exclude one of defendants' industry experts (Dr. Bustin), helped develop our industry expert record and prepared and defended many of our fact witnesses at deposition
- Associates **Alex Karambelas** and **Kayla Prieto** worked hard at every turn to support the team's efforts, compiled the summary judgment record, conducted fact discovery, managed document review and productions and handled discovery disputes; and
- Associate **Juan Gascon**, a key member of our securities and governance team, supported various aspects of our work.

Most defendants are motivated to settle when securities cases survive a motion to dismiss and a class is certified. Why did your client press on to summary judgment here?

Greene: You're right: the vast majority of securities class actions settle soon after the denial of a motion to dismiss. This is a shame; the right cases can and should be litigated through summary judgment. The key is to pick the right cases, and this was one.

When we got into the facts, we determined that we had strong summary judgment arguments on each element: falsity, scienter, materiality, loss causation and reliance—we didn't oppose class certification on reliance grounds, and on summary judgment made a price-impact argument under the Supreme Court's decision in *Halliburton II*. Each of those was an independent basis for summary judgment, so mathematically, having strong arguments on five separate elements gave us a lot of comfort about prevailing on one or more. And none of the individual defendants sold any stock during the alleged class period or otherwise had any concrete personal motive to commit the alleged fraud.

Even if we hadn't prevailed on summary judgment, we felt it was a case we could take to trial and win. The merits would still be on our side, and our clients are honest people who do important, life-saving work and are excellent witnesses.

Tell me about the three alleged corrective disclosures at issue in this case. How did you make the case that they weren't actually corrective disclosures?

Greene: Plaintiff's theory of the case was that the Company's May 1 press release created a false impression that the Logix Smart test was 100% accurate, and that this impression was "corrected" by three third-party disclosures.

The first alleged corrective disclosure was a May 14 Salt Lake Tribune article stating that TestUtah—not Co-Diagnostics—declined to participate in a statewide validation study. We argued that the article was not corrective given it did not concern Co-Diagnostics, nor did it say anything about the accuracy of the Logix Smart test.

The second disclosure was a May 14 announcement by the Iowa Governor that TestIowa's validation study—which involved the Logix Smart test—showed 95% sensitivity. We argued that even if this announcement somehow "corrected" the impression that the Logix Smart test was 100% accurate, the same exact information was disclosed three days earlier when the governor of Nebraska announced that TestNebraska's validation, which also used the Logix Test, had shown 95% accuracy. This meant that the allegedly corrective information was already known to the market and baked into the company's stock price prior to May 14. Notably, after the Nebraska governor's announcement, the company's stock increased nearly 10%, demonstrating that the market did not perceive the information as negative or corrective of the May 1 press release.

The last disclosure was a May 14 FDA press release concerning a different company's COVID test, and which stated, generically, that "[n]o diagnostic test will be 100% accurate." We argued this disclosure was not corrective because it did not concern Co-Diagnostics, and because it was already common knowledge that no diagnostic test and no COVID test could be 100% accurate (particularly in the first months of the pandemic). This fact was also widely reported in the media prior to the class period, meaning that it was baked into the company's stock price at all times and could not have caused any investor losses.

You were able to win a *Daubert* motion to exclude the expert the plaintiffs were relying on to prove up loss causation. What was your approach in challenging that witness?

York-Erwin: Our general approach was to show that the expert ignored obvious market evidence that attributed the company's stock price drop on May 15 to the company's earnings announcement—totally unrelated to the Logix Smart test. Plaintiff's expert did not even consider these analyst reports when preparing his expert reports, and failure to consider this obvious alternative explanation for the May 15 stock price drop rendered his testimony unreliable under Federal Rule of Evidence 702, *Daubert* and Tenth Circuit precedent. We also argued that the expert failed to seriously examine whether the alleged corrective disclosures were actually corrective and that he improperly applied a two-day event window, but it was the expert's failure to consider obvious alternative explanations for the May 15 stock price drop that drove the court's decision.

I hear the court held five hours of argument on the summary judgment and expert motions. How much of that argument focused on loss causation—the issue she ultimately found the case turned on? Are there any moments from the argument that stand out?

York-Erwin: Yes, it was a very long argument! We had strong arguments on five different elements (falsity, materiality, scienter, reliance and loss causation, plus a standing argument), so there was a lot of ground to cover. The first three hours or so were devoted to the parties' cross-motions for summary judgment. At our suggestion, the court heard argument on each element separately and in turn: Plaintiff made its case on falsity first, we responded, and each side had time for a short rebuttal, then we repeated the same sequence for scienter, and so on, finishing with loss causation. Once the parties had finished argument on the motions for summary judgment, the court turned to the parties' cross-motions to exclude one another's industry-experts, followed by our motion to exclude plaintiff's economic expert.

The loss causation argument itself only lasted maybe 20 or 30 minutes, but related issues came up repeatedly throughout the argument—it was clearly on Judge Parrish's mind from the beginning. One of the moments from the argument that stands out most came very early, during my argument on falsity, when I noted that it was widely discussed in news articles prior to May 1, 2020, that no test can be 100% perfect, and I read language from a few examples. I recall Judge Parrish stopping me there and asking how those statements were any different than the statement in the final alleged corrective disclosure (the after-hours FDA press release) that "no diagnostic test will be 100% accurate." I said she was right, there was no difference, and that this was critical to both falsity and loss causation: it was already widely known, when the challenged statements were made, that no test can be 100% accurate, so the challenged statements could not have misled a reasonable investor in that regard and the FDA press release's statement could not have been "corrective." She asked about similar loss causation issues again and again throughout the argument.

What can other defendants take from how you and your team litigated this case once you took over?

Greene: I really hope that other defendants will decide to defend the right securities class actions through summary judgment. Picking the right ones requires several essential steps.

The first step comes right at the beginning of the litigation: companies should choose defense counsel who are not just good at winning motions to dismiss, which is essential, but also have the ability to litigate effectively and efficiently through the subsequent stages of the litigation.

The second step is careful analysis by defense counsel of the chances of winning on summary judgment, element by element. The right cases for summary judgment are ones with strong summary judgment arguments on multiple grounds; more chances to win makes everyone more comfortable. And the lack of a concrete personal motive is important. In my experience, a motive-less securities class action rarely is meritorious.

The third step is analysis of the economics of litigating through summary judgment: How much will it cost? How much cost certainty can defense counsel give? What are realistic aggregate damages? Will there be enough D&O insurance left to settle if summary judgment is denied?

The final step is critical: excellent communication about the merits and economics among defense counsel, the defendants and their D&O insurers and brokers. The better the defendants and their D&O insurers know and trust the chances of winning on summary judgment (and class certification) and at what cost, the more comfortable they will be about defending the case beyond the motion to dismiss.

What will you remember most about this matter?

Greene: I'll remember how satisfying it was to win for this wonderful company. Their COVID test was successful and saved countless lives, and this litigation unfairly criticized their disclosure about the test. Our clients believed they told the truth and had the courage of their convictions to defend the case through discovery and summary judgment.

I'll also remember our tremendously talented team. We divided the work in a smart way, including having the lawyers who wrote a summary judgment or *Daubert* brief argue the motion, and each team member defended our clients with great skill, dedication, and passion.

York-Erwin: I think I'll most remember the fun I had working closely with our team on strategic issues, and the deep satisfaction of winning this important victory for such a worthy client. Co-Diagnostics is a great, small company doing important work to make quality diagnostic testing more affordable and accessible to everyone. It's very gratifying to secure this win for them.