

U.S. SEC ENFORCEMENT DIVISION PURSUES CORONAVIRUS-RELATED FRAUD CLAIMS

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Federal, state and local law enforcement and consumer protection agencies have been issuing alerts and investigating cases regarding efforts by fraudsters to exploit the coronavirus crisis for profit. The SEC is taking similar action, focused on the use of public securities markets to carry out fraud.

Since the onset of coronavirus, or COVID-19, the SEC has suspended trading in the stock of more than 30 companies in connection with coronavirus-related fraud, pursuant to its authority to suspend trading temporarily where it believes that information about a company is unreliable or inaccurate.

And the SEC's Enforcement Division in recent weeks has brought enforcement actions in several cases alleging fraudulent statements regarding coronavirus products designed to boost a company's share price. The actions were brought against smaller companies issuing releases with false claims about products and services likely to be in high demand because of the pandemic, such as virus tests, hand sanitizer and masks. The statements are alleged to cause rapid increases in stock price and volume, and are alleged to violate section 10(b) of the Securities Exchange Act of 1934 and rule 10b-5.

The SEC's latest coronavirus-related complaint, filed this week in the Southern District of Florida, involved a different fact pattern. It charged an investment adviser, E*Hedge Securities, Inc., and its CEO with violations of the Investment Advisers Act of 1940 for failure to produce books and records in the course of an SEC investment-adviser examination, and for failure to properly register under the Act. E*Hedge on March 22, 2020 began operating a new website, "Covid19invest.com," which "attempted to capitalize on potential investor interest in products and treatments for the recent coronavirus, Covid-19," the SEC alleged. While the charges did not involve the pandemic, the Enforcement Division's interest was likely enhanced by E*hedge's coronavirus-related marketing.

To coordinate efforts related to the pandemic, the Division has formed a steering committee, which seeks to identify key areas of potential market and investor risk. A central focus is on microcap companies, co-director of enforcement Steven Peikin stated in an address last month to the Securities Enforcement Forum. He recalled the fraudulent schemes that arose in the wake of

Hurricane Katrina in 2005 and the Ebola crisis of 2014, and added: “Sadly, but not surprisingly, we have seen an explosion of similar activity over the last few months.”

A release by the SEC’s Office of Investor Education and Advocacy, originally issued in February and updated on May 27, noted claims by publicly traded companies that their products “can prevent, detect or cure corona virus,” and also noted that “the stock of these companies will dramatically increase in value as a result.”

In addition to its emphasis on microcap companies, the Enforcement Division has developed a process to review public filings of companies in pandemic-related industries, “with a focus on identifying disclosures that appear to be significantly out of step with others in the same industry,” Peikin stated in his address.

The Enforcement Division’s recent cases illustrate the range of activities in connection with COVID-19 that may trigger Enforcement Division interest. The E*Hedge action referred to above charged an investment adviser, but other cases have been brought against public companies and sometimes their principals.

In an action brought in May in the Southern District of New York, the SEC contended that issuer Applied BioScience “sought to exploit the COVID-19 pandemic for profit,” by announcing in late March a shift from making cannabiniol-based products to pandemic-related products, including hand sanitizer. The SEC further alleged that the company falsely claimed to be offering a COVID-19 home test kit to the general public for private use.

In fact, the SEC contended, the company did not offer or intend to sell test kits for home or private use, but rather intended to screen potential purchasers, and only to allow purchase for use by nursing homes, schools, military and first responders. Further, it alleged, the FDA had not approved the company’s sale of at-home test kits.

Also in May, the SEC filed an action against Turbo Global Partners and its CEO in the Middle District of Florida. This action centered on press releases issued by the company in March touting its partnership with another company to sell thermal scanning equipment to detect individuals with fever.

The complaint alleges a series of misstatements in the releases. For example, it alleges that one release falsely stated that Turbo Global’s alleged partner company “is [the] front facing Partner in the multi-national public-private-partnership (PPP) for this innovation which simply stated, is the only scanning technology on the planet with non-contact intelligent human temperature screening and facial recognition.” In reality, according to the SEC’s complaint, the partner was not engaged in any such partnership involving a government entity, and the scanning equipment in question did not have facial recognition technology.

The SEC brought an action in April against Praxsyn Corp. and its CEO in the Southern District of Florida, also focused on alleged false and misleading press releases. These releases made claims that the company “was able to acquire and supply large quantities of N95 and similar masks to protect wearers from the COVID-19 virus.” The SEC charged that the company never had any masks in its possession, any orders for masks, or a contract with or supplier to obtain masks.

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- Securities & Corporate Governance

MEET THE TEAM



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