Ninth Circuit Affirms Dismissal of Securities Class Action Against Tesla, Inc.

February 3, 2021

On January 26, 2021, the Ninth Circuit issued a decision in *Friedman v. Tesla, Inc.*, *et al.*, No. 19-15672, affirming the dismissal of a putative securities fraud class action. The lawsuit accused Tesla and two of its officers of misleading investors in 2017 regarding the company's production goals for its first mass-market electric vehicle, the Model 3. The Court held that the plaintiffs had failed to identify any actionable misrepresentation, finding that most of the relevant statements were simply "optimistic projections" regarding production capabilities that qualified for protection under the Private Securities Litigation Reform Act's (PSLRA) safe harbor for forward-looking statements. The decision highlights the important distinction between statements of present fact and statements of opinion or future aspirations. It also confirms that the safe harbor applies to mixed statements: i.e. statements that are forward-looking but that incorporate underlying assumptions concerning past or present facts. Finally, the decision demonstrates that to state a viable claim for securities fraud, plaintiffs cannot merely rely on evidence of internal *disagreement* over a company's stated goals; instead, they must show that a speaker *did not believe* that a forward-looking statement was true.

The plaintiffs alleged that Tesla misled investors by (1) communicating production goals for the Model 3 that the company knew was unattainable, and (2) reaffirming that the company was "on track" to meet those targets. The plaintiffs alleged that the defendants repeatedly stated that they expected to reach the goal of producing 5,000 cars per week by the end of 2017, despite knowing that Tesla would not be able to do so. Op. at 5. Ultimately, Tesla did not meet this goal. *Id.* at 8. Plaintiffs brought suit under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5, in addition to asserting claims against the individual defendants for control person liability under Section 20 of the Exchange Act. *Id.* at 9.

In affirming the district court's dismissal of the complaint, the Ninth Circuit held that most of the alleged misstatements were "unquestionably" forward-looking and were accompanied by meaningful cautionary language, meaning that they were not actionable under the PSLRA. *Id.* at 19. The Court rejected the plaintiffs' argument that statements representing that Tesla was "on track" to meet its stated production goals were not forward-looking because they contained "embedded assertions concerning *present* facts." *Id.* at 18. The Court explained that the PSLRA's definition of "forward-looking statements" expressly encompasses "statement[s] of the *plans and objectives* of management for future operations," as well as "'statement[s] of the *assumptions* underlying or relating to' those plans and objectives." *Id.* (citing 15 U.S.C. § 78u-5(i)(1)(B), (D)). The Court further explained that to demonstrate that a statement concerning plans for future operations is *not* protected by the PSLRA's safe harbor, a plaintiff must show that the challenged statement goes beyond the mere articulation of plans, objectives, or assumptions, and instead "contains an express or implied 'concrete' assertion concerning a specific 'current or past fact[].'" *Id.* at 18-19 (citing *In re Quality Sys., Inc. Sec. Litig.*, 865 F.3d 1130, 1142-44 (9th Cir. 2017)).

Applying these principles, the Court concluded that the defendants' statements indicating that Tesla was "on track" to meet its goal of producing 5,000 Model 3s per week by the end of 2017 *were* forward-looking. The Court found that those statements did not include "the sort of 'concrete description' about the facts concerning the 'past and present state' of production" that might otherwise remove such a statement from the protection of the PSLRA's safe harbor. *Id.* at 27-28 (quoting *Quality Sys.,* 865 F.3d at

1142-44). Instead, they were simply "generic" reaffirmations of the company's previously communicated goals.

While the Court concluded that part of one of the alleged misstatements was *not* forward-looking—namely, the company's announcement that it had commenced "installation of Model 3 manufacturing equipment" at one of its factories—the Court held that this statement was nonactionable because the plaintiffs had failed to plead any facts demonstrating that the statement was "materially false or misleading." *Id.* at 21.

Notably, the Court dismissed the claims notwithstanding that the complaint included allegations from several alleged former Tesla confidential witnesses suggesting that they had expressly informed Musk that it would be impossible in 2017 to meet the stated target of producing 5,000 cars per week. *Id.* at 6. Plaintiffs argued that these accounts demonstrated that the defendants knew it would be impossible to achieve this production goal within the stated timeframe, and that this "known impossibility" negated the relevance of any cautionary language accompanying Tesla's forward-looking statements. *Id.* at 6, 22-23.

The Court rejected this theory, explaining that the mere fact that certain employees may have believed that the 5,000 car/week goal was unattainable did not mean that the defendants concurred. *Id.* at 22-23. Because these confidential witness accounts did not suffice to establish that the defendants "accepted those employees' views" and *knew* that the stated target would be impossible to achieve, they did not provide any basis for concluding that the defendants' statements fell outside of the PSLRA's safe harbor. *Id.* at 23.

Thus, the decision also confirms that to state a securities fraud claim, plaintiffs must do more than simply show internal disagreement over a stated corporate goal. Rather, plaintiffs must adduce evidence that the speaker in fact *disbelieved* what he or she was communicating to investors.

The panel included Circuit Judge J. Clifford Wallace, Circuit Judge Susan P. Graber, and Circuit Judge Daniel P. Collins.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your usual Davis Polk contact.

Catherine Kennedy	+1 650 752 2090	**catherine.kennedy@davispolk.com**
Edmund Polubinski III	+1 212 450 4695	**edmund.polubinski@davispolk.com**
Neal A. Potischman	+1 650 752 2021	**neal.potischman@davispolk.com**
James P. Rouhandeh	+1 212 450 4835	**rouhandeh@davispolk.com**
Dana M. Seshens	+1 212 450 4855	**dana.seshens@davispolk.com**
Andrew Yaphe	+1 650 752 2088	**andrew.yaphe@davispolk.com**