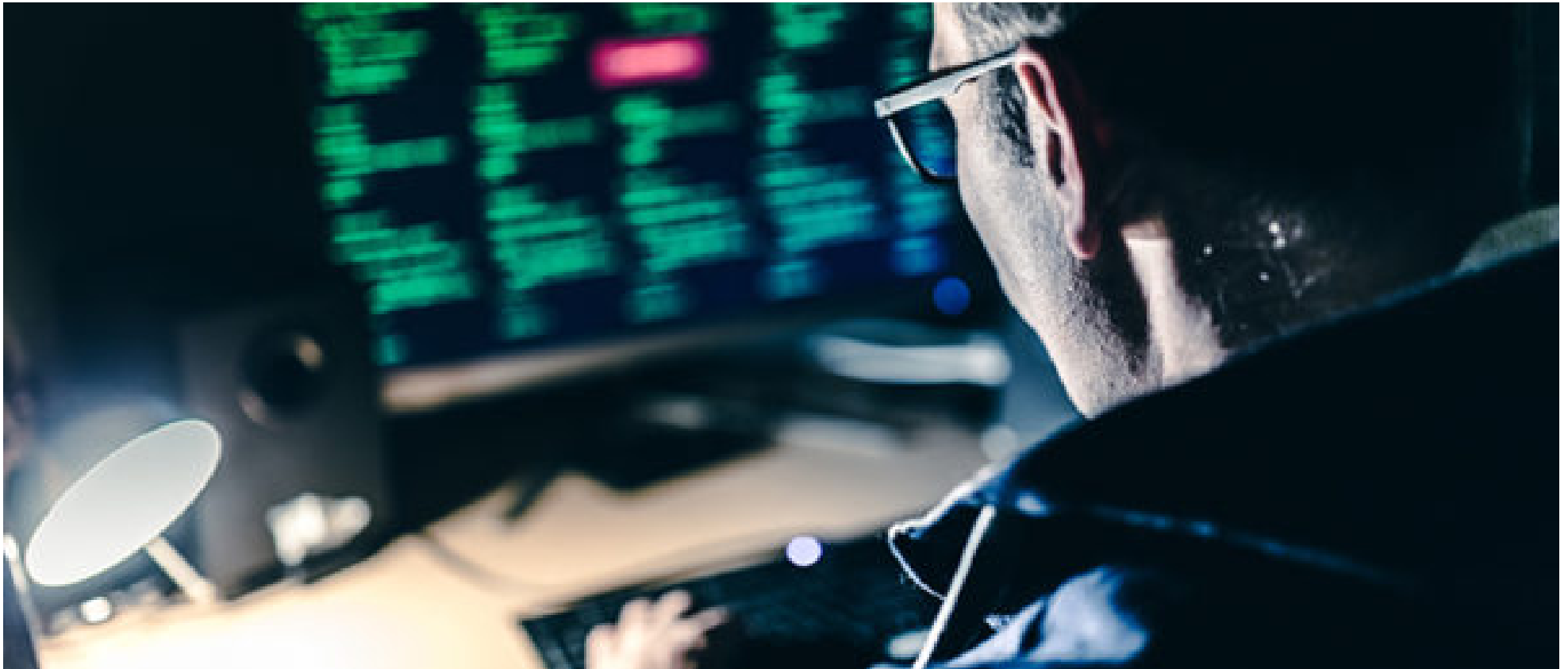




Securities Litigation and Regulatory Enforcement

Resources for Broker Dealers, Investment Advisers, General Counsels, and Directors & Officers

Fraud in the Time of Covid-19



Computer hacker

By Winstead on April 6, 2020

By **Toby M. Galloway**, **Matthias Kleinsasser**, **Joe Wielebinski**

In sports, it is often said that “winning cures everything.” The same concept applies to uncovering fraud. When the economy is strong and most investors are making money, there is little incentive to ask difficult questions about a company’s performance. Once the economy craters, however, investors begin demanding answers and harsh truths are often revealed. As Warren Buffett has said, “only when the tide goes out do you discover who’s been swimming naked.”

This may already be occurring in the current economic environment. On April 2, 2020, the Chinese coffee chain Luckin Coffee announced in a regulatory filing that an internal investigation had concluded that its Chief Operating Officer fabricated 2019 sale numbers by approximately 2.2 billion yuan (\$310 million). Unfortunately for investors, the announcement was not a belated April Fool's Day joke. Luckin's IPO in May 2019 priced stock at \$17 per share. Shares shot to \$51.38 per share in January 2020 before crashing due to the Covid-19 outbreak, and, more recently, the announcement of the internal investigation's findings.

If history is any guide, financial fraud experts are about to become very busy. The recession that began in 2008 resulted in a significant increase in lawsuits based on fraudulent loss. See, e.g., Adam Smith, **"The Reasons Fraud Spikes in a Recession," Time, May 20, 2009.** A key reason for this is that when companies' values plummet and investors cry foul, firms begin evaluating management's decisions with a much sharper eye. In addition, fraudsters try to take advantage of people's fears. Finally, ongoing frauds are more susceptible to discovery when investors seek to liquidate their holdings en masse. There is every reason to believe this will happen in the current economic climate, given the global economic damage done by Covid-19.

Toby M. Galloway is Co-Chair of Winstead's Securities Litigation & Enforcement Practice Group. He also practices in the areas of white-collar defense, governmental & internal investigations, and business litigation. Before developing his private practice, he served as an attorney with the United States Securities and Exchange Commission, in roles of increasing responsibility, for more than 11 years

Matthias Kleinsasser is a member of Winstead's Business Litigation, White-Collar Defense and Business Restructuring/Bankruptcy Practice Groups. His practice encompasses all aspects of commercial litigation in state and federal court, with an emphasis on bankruptcy-related litigation, securities litigation, securities enforcement proceeding defense and white-collar defense.

Joe Wielebinski is a member of Winstead's Business Restructuring/ Bankruptcy Practice Group. For more than 30 years, his practice has concentrated on bankruptcy, creditors' rights and financial restructuring, and he is active throughout the United States in a variety of complex restructuring, insolvency and bankruptcy matters and related litigation. Joe has represented numerous victims in matters involving complex financial fraud, theft, money laundering and other white collar crimes. He has also served as a Federal District Court receiver at the request of the SEC in cases involving national and cross-border fraud schemes.

Securities Litigation and Regulatory Enforcement



Copyright © 2020, Winstead PC. All Rights Reserved.