



AI Claims and Disclosures: Securities Law Risks from Development to Deployment

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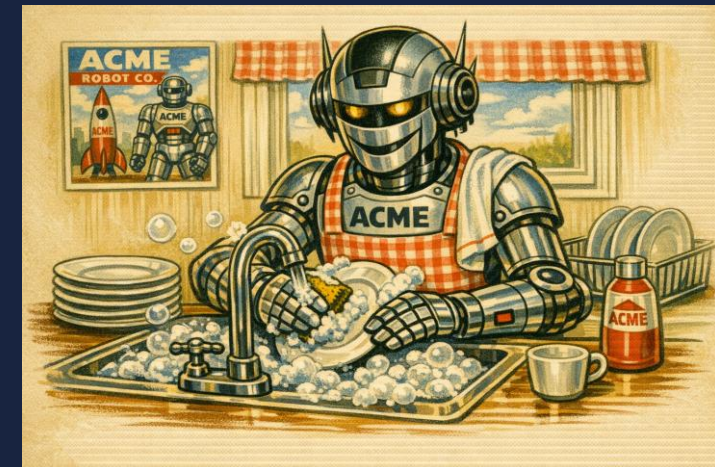
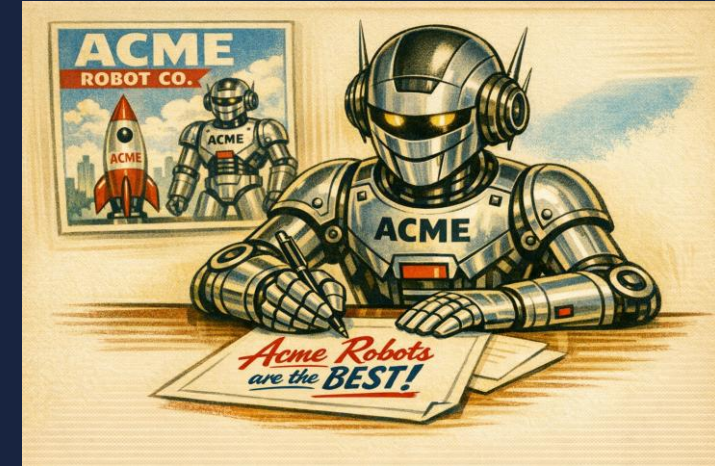
Overview of AI Washing and Other Challenged AI Claims

“AI Washing” and Other Challenged AI Claims

Investors, consumers, and regulators such as the FTC and SEC have brought many cases against companies for allegedly false or misleading claims about AI, using theories of liability from consumer protection, securities, and common law.

These cases can challenge company claims about AI-enabled products or services in a broad variety of ways, including:

- Exaggerated efficacy, accuracy, or performance claims
- Deceptive claims about revenue and customer demand
- Misleading comparisons (eg, to non-AI products)
- Lack of adequate substantiation
- False “scientifically proven” claims
- Overly broad (or unqualified) claims
- Deceptive illustrations or demonstrations
- Failure to (adequately) disclose limitations or risks
- Future performance claims that don’t come true
- Misstatements about the role of AI in the product
- Deceptive agency or agentic claims



Primer on Securities Class Actions

Antifraud Provisions of the Securities Laws

Overview

- Section 10(b) under the Securities Exchange Act of 1934 (Exchange Act) prohibits “manipulative or deceptive devices or contrivances in connection with the purchase or sale of any security.”
- Rule 10b-5 prohibits the “use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
 - To employ any device, scheme or artifice to defraud,
 - **To make any untrue statement of a material fact or to omit to state a material fact** necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or
 - To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.”
- In addition to enforcement action by the SEC, there is an implied **private right of action** against any person who makes an untrue statement of material fact or omits to state a material fact in connection with the purchase or sale of any security.

Rule 10b-5

Elements of 10b-5 claim

- **Materiality**
 - Does the information significantly alter the total mix of information available to investors?
- **Scienter**
 - Intent to defraud or recklessness.
- **In connection with the purchase or sale of securities**
 - Because the investing public may rely on statements made by the company in making decisions to purchase or sell the company's securities, *virtually every public statement by the company may be deemed to be made in connection with the purchase or sale of the company's securities.*
- In addition to the above, **private plaintiffs** must establish the following:
 - **Reliance:** The plaintiff actually relied on the defendant's misstatement or omission when making their investment decision.
 - **Economic Loss:** Typically shown as declined value in Plaintiff's investment.
 - **Loss Causation:** The misstatement or omission must be the direct cause of the investment's decline in value.

Rule 10b-5

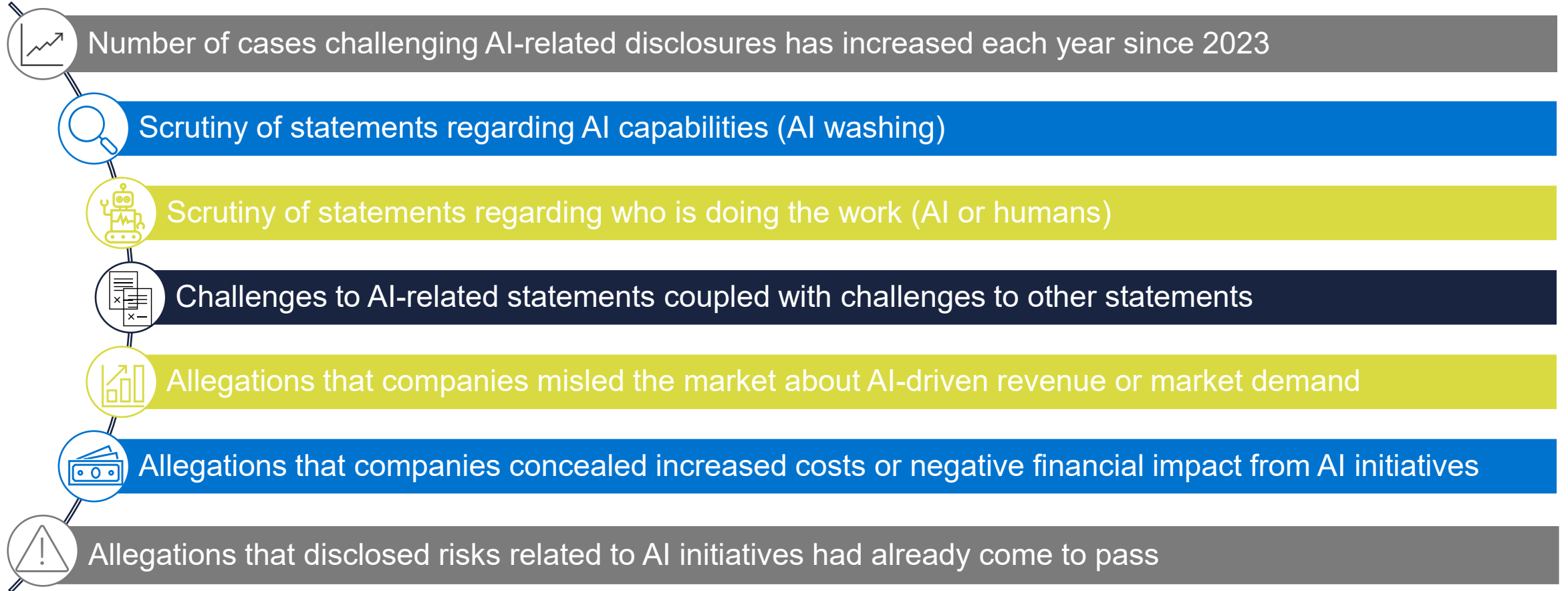
Duty to Correct and Update

- If the company publicly makes an inaccurate or misleading statement, the company has an obligation to correct that statement. If the company has publicly made a forward-looking statement that has subsequently become inaccurate or misleading due to changes and circumstances, the company **may have an obligation to update** that prior statement.
- Certain courts have imposed a “**duty to update**” on companies, while other courts, considering the issue, have held that while a company has a “**duty to correct**” the statement that was untrue or misleading, what made it does not have a “duty to update” statements that were true and not misleading when made. Whether it is necessary under applicable, legal requirements (or advisable for investor relations reasons) for the company to update prior statements will depend upon **the facts and circumstances** of the statement in question.

Trends in AI-Related Securities Class Actions

Exemplar Cases

Trends in Securities Class Actions Related to AI



So far, AI-related cases do not appear more likely to survive a motion to dismiss than average

Nolff et al. v Aterian, Inc., et al., S.D.N.Y.

Case settled before ruling on motion to dismiss

Challenged Statements

“We believe we are reinventing how to rapidly and successfully identify new product and market opportunities, and to launch, autonomously market and sell products in the rapidly growing global e-commerce market by leveraging our proprietary software technology platform, known as AIMEE. AIMEE combines large quantities of data, AI, machine learning, and other automation algorithms at scale to allow rapid opportunity identification and automated online sales and marketing of consumer products.

AIMEE sources data from various e-commerce platforms, the internet and publicly available data, allowing us to estimate and determine trends, performance, and consumer sentiment on products and searches within e-commerce platforms. This functionality allows us to help determine which products to market, manufacture through contract manufacturers, import, and sell on e-commerce marketplaces. AIMEE is also connected, through APIs, to multiple e-commerce platforms. **This allows us to automate the purchase of marketing, automate various parts of our fulfillment and logistics operations and to automate the pricing changes on product listings.”**

Nolff et al. v Aterian, Inc., et al., S.D.N.Y.

Case settled before ruling on motion to dismiss

Falsity Allegations

Relying heavily on statements from former employees, plaintiffs alleged this statement was false and misleading because defendants allegedly failed to disclose that:

- (i) AIMEE was not artificial intelligence;
- (ii) AIMEE was unable to identify new product and market opportunities, but rather required human beings to manually analyze data that was stored in AIMEE to identify new product opportunities;
- (iii) AIMEE was unable to launch or autonomously market products, but rather it required human beings to initiate the launch and manually market the products;
- (iv) AIMEE did not automate the purchase of marketing, or various parts of Aterian's fulfillment and logistics operations, but rather Aterian input information manually, including when adding new products to the system or changing prices.

Alich v Opendoor Technologies, Inc. (D. Ariz.)

Motion to dismiss granted in part and denied in part; case settled thereafter

Challenged Statements Dismissed For Failure Adequately to Allege Falsity

Plaintiffs challenged statements regarding the Opendoor's pricing algorithm, including:

- **The algorithm uses “machine learning to drive pricing decisions.”**
- **Opendoor’s “proprietary, machine learning-based pricing models are key to its ability to acquire and resell thousands of homes per month accurately, profitably, and with increasing levels of automation.”**

Plaintiffs alleged these statements were misleading because the algorithm could not accurately price homes and as such Opendoor's pricing decisions were based on a human-driven process.

Defendants argued they disclosed the existence of human involvement. eg, “After all the data has been collected and incorporated, each offer is reviewed and finalized by members of our pricing team, allowing us to marry the best of algorithmic insights with human judgment.”

Court agreed with defendants the statements would not lead a reasonable investor to believe the entire process was driven by the algorithm.

Alich v Opendoor Technologies, Inc. (D. Ariz.)

Motion to dismiss granted in part and denied in part; case settled thereafter

Challenged Statements Sustained

On a motion for reconsideration, the Court found that plaintiffs adequately alleged the following statement was false or misleading:

The algorithm can “dynamically adjust to leading market indicators and react to real-time macro- and micro-economic conditions.”

Pointing to analyst commentary, the Court held this statement created “an impression that Opendoor’s algorithm was, at the very least, generating roughly accurate offers at the time the statements were made.”

The Court found the complaint adequately alleged that impression was false based on Confidential Witness statements that the algorithm was “never accurate,” “corrupt,” and “dramatically overpricing homes.” According to the CWs, pricing analysts were instructed to ignore the algorithm-generated initial price in setting a final price.

Notably, the Court found the complaint failed adequately to allege scienter. The case went forward on this statement because it was made in Opendoor’s IPO offering documents.

In re Qutoutiao, Inc. Securities Litig. (S.D.N.Y.)

Motion to Dismiss Granted

Challenged Statements Not False When Read in Context

- Plaintiff alleged that QTT misled investors by stating in its IPO Offering Documents that QTT used “artificial intelligence” and “deep learning methods” to “monitor and identify objectionable visual content with a high degree of accuracy” and flag “suspicious content for manual review.”
- According to plaintiff, these claims were misleading because the content screening did not prevent illegal *advertisements* from appearing on the app.
- The court agreed with the defendants that, read in context, the references to “artificial intelligence” to the screening of QTT’s core content for consumers (ie, news articles), not advertisements.
 - The challenged statements appeared under the heading “Content Screening Technology,” not in a separate section titled “Advertisements.”

Takeaways

Traditional tools for challenging the adequacy of securities class action complaints work equally well for AI cases

- Courts apply the same exacting standards in cases involving AI
- Courts consider context in which statements are made, whether statements are forward looking, and whether they are general statements of corporate optimism (puffery)
- Plaintiffs still must allege particularized facts to show falsity and scienter

Companies should continue to apply established standards for accuracy, transparency, and the use of cautionary language and risk disclosures

- Ensure public statements about AI capabilities and performance can be substantiated
- Clarify the role of human labor
- More recent complaints avoid buzzwords such as “AI” and “machine learning” and focus on company-specific technology

Companies are not required to accurately predict the future

SEC Enforcement Trends

SEC Enforcement Examples: Delphia (USA) Inc.

- In March 2024, the SEC settled charges against Delphia (USA) Inc. for allegedly making false and misleading statements regarding its use of AI and machine-learning capabilities.
- According to the SEC, Delphia represented that it "used artificial intelligence and machine learning to analyze its retail clients' spending and social media data to inform its investment advice." The company's brochures promised that its investment advice was "powered by the insights it makes when individuals ... connect their social media, banking, and other accounts," which was fed into "a predictive algorithmic model" for the selection of "stocks, ETFs and options[.]"
- Additionally, a later press release stated that Delphia was "the first investment adviser to convert personal data into a renewable source of investable capital ... that will allow consumers to invest in the stock market using their personal data."
- Finally, Delphia's website claimed that it "put collective data to work to make our artificial intelligence smarter so it can predict which companies and trends are about to make it big and invest in them before everyone else."
- The SEC found that these statements were false and misleading because Delphia did not, in fact, have the claimed AI and machine-learning capabilities.
- In addition, the SEC found the firm also violated the Marketing Rule, which prohibits a registered investment adviser from distributing any advertisement that includes any untrue statement of material fact.
- Delphia ultimately agreed to cease and desist from any further violations, was censured, and pay a civil penalty of \$225,000.

SEC Enforcement Examples:

Albert Saniger

- In April 2025, the SEC filed an action against Albert Saniger, the founder and former CEO of Nate, Inc. (Nate) for allegedly making false and misleading statements regarding Nate's use of AI and machine-learning capabilities.
- According to the SEC, Saniger raised over \$42 million from private market investors by falsely claiming that Nate's mobile shopping software used AI to complete users' purchases across a variety of retail platforms.
- Specifically, Saniger misrepresented through presentations, marketing materials, and emails that Nate utilized "machine learning" and "neural networks" to autonomously process transactions – when in fact Saniger knew that virtually all of the purchases were being completed manually by contract workers.
- Additionally, Saniger went so far as to conduct product demonstrations for investors that falsely made it appear that software was automatically completing orders, when in reality, Nate's employees manually processed the orders at Saniger's direction.

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