

Theranos and Startup Culture: Vision or Fraud?

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As ravaged startup giant, Theranos, begins dissolution after a series of [lawsuits alleging “massive fraud”](#) and a default on its last \$65 million loan, spectators all seem to be asking the same question: how did a company fraudulently raise \$700 million before finally being unmasked?

Theranos promised to revolutionize the diagnostic-lab industry by delivering one innovation: finger prick blood tests. Health care companies, venture capitalists, and even government officials poured huge investments into the company – [on one occasion, \\$100 million was sent over a single wire transfer](#). As investors waited for years for Holmes to deliver, she was raking in money for a product that never even existed. Whenever investors would try to peek behind the curtains to find out more about her company’s “secret sauce,” she shrouded herself behind flagrantly [vague and often outright untruthful statements](#).

In many ways, Theranos is the embodiment of Silicon Valley startup culture. The startup entrepreneurial spirit is selling a vision of a fictional product – a product that does not yet exist. This is how Theranos’s huge valuation was birthed and where a critical legal problem lies. With the advent of [Sarbanes-Oxley Act](#) in 2002 that promised to safeguard investors against fraud like in the Enron scandal, startup companies have purposefully opted to stay private due to the myriad of regulations imposed by the Act, such as disclosure of financial statements. The problem is, companies like Theranos, [Uber](#), [WrkRiot](#), and more, have often construed this to mean that they are exempt from the rules that public companies play by and thus often cross the delicate line between merely selling a visionary product and committing massive fraud.

In many ways, Theranos was exactly the case the SEC was looking for. The SEC exists in an opportune moment to not only establish a clearer distinction of that oft-straddled line while also sending a strong signal that startup companies will have to play by the rules. While investment and fraud more generally will likely always be a feature in the magical Valley, the SEC must ensure that these fictional visions are kept honest through litigation.

