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UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

OAKLAND DIVISION

IN RE WAGEWORKS, INC. SECURITIES LITIGATION	CASE NO.: 4:18-CV-01523-JSW **DEFENDANT WAGEWORKS, INC.'S REPLY IN SUPPORT OF ITS MOTION TO DISMISS CONSOLIDATED AMENDED CLASS ACTION COMPLAINT FOR VIOLATION OF THE FEDERAL SECURITIES LAWS** Hearing Date: November 22, 2019 Hearing Time: 9:00 a.m. Courtroom: 5, 2d floor Judge: Hon. Jeffrey S. White

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SUMMARY OF ARGUMENT (STANDING ORDER, ¶ 7)

Plaintiffs' Opposition confirms that their Section 10(b) and Rule 10b-5 claim fails to plead particularized facts that give rise to a strong inference of scienter. *Zucco Partners, LLC v. Digimarc Corp*., 552 F.3d 981 (9th Cir. 2009). The Opposition does not defend Plaintiffs' failure to plead direct allegations of Defendants' scienter regarding any alleged fraud. Plaintiffs thus have abandoned, even conceded, such theories. *See Costabile v. Natus Med. Inc.*, 293 F. Supp. 3d 994, 1014 (N.D. Cal. 2018) (White, J.). Instead, their case is built on mere "conclusory allegations of law and unwarranted inferences [that] are insufficient to defeat a motion to dismiss." *In re Daou Sys., Inc.*, 411 F.3d 1006, 1013 (9th Cir. 2005) (citation omitted). The Court is not required to "assume the truth of legal conclusions merely because they are cast in the form of factual allegations." *Fayer v. Vaughn*, 649 F.3d 1061, 1064 (9th Cir. 2011) (citation omitted). Nor is the Court "required to indulge unwarranted inferences in order to save a complaint from dismissal." *Metzler Inv. GMBH v. Corinthian Colls., Inc.*, 540 F.3d 1049, 1064-65 (9th Cir. 2008). At bottom, Plaintiffs fail to plead particularized facts to support an inference of scienter that is at least as compelling as an inference of nonfraudulent intent – here, a mistaken contractual interpretation resulting in an accounting error consisting of the reversal of less than 1% of the total reported 2016 revenue. *Webb v. SolarCity Corp.*, 884 F.3d 844 (9th Cir. 2018).

Plaintiffs' Section 10(b) and Rule 10b-5 claim also should be dismissed for failure to plead loss causation. The Opposition does not defend Plaintiffs' original market revelation theory of loss causation. Their new theory – proximate causation – does not save the CAC because the CAC fails to sufficiently plead "a causal connection between the material misrepresentation and the loss." *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 342 (2005).

Finally, the Section 11 claim should be dismissed for lack of statutory standing. *In re Century Aluminum Co. Sec. Litig.*, 729 F.3d 1104 (9th Cir. 2013); *Thomas v. Magnachip Semiconductor Corp*., 167 F. Supp. 3d 1029 (N.D. Cal. 2016). Plaintiff Public Employees Retirement Association ("PERA") concedes this pleading deficiency by claiming it can, by amendment, cure it. Any amendment that fails to satisfy the principles enunciated in *Century Aluminum*, however, would be futile.

INTRODUCTION

The backbone of Plaintiffs' case has collapsed. This securities fraud case is based on the premise that certain services rendered by WageWorks, Inc. ("WageWorks" or the "Company") under a government contact would be at "no cost" to the government. Therefore, say Plaintiffs, Defendants intended to defraud investors when WageWorks recognized the associated revenue, amounting to less than one percent of the total 2016 revenue. In moving to dismiss the amended complaint, the Company submitted the contract for the Court's consideration.[1] The Contract does not contain a "no cost" provision. Plaintiffs' Opposition ("Opp.") fails to address this fatal defect. They simply ignore it.

In fact, the Opposition notably avoids many of the arguments made by WageWorks in its Memorandum in Support of the Motion to Dismiss (the "Opening Br."). Instead, Plaintiffs substitute rhetoric for specific facts in an effort to twist WageWorks' ongoing contract dispute with the government into a "classic case of accounting fraud." Opp. at 1. Despite Plaintiffs' rhetoric and avoidance, the deficiencies in the Consolidated Amended Complaint ("CAC") remain. By failing to respond to certain specific arguments in the Company's Opening Brief, Plaintiffs have conceded much, including but not limited to:

- The CAC fails to plead direct allegations of the Executive Defendants' contemporaneous knowledge of the Company's alleged non-entitlement to Base Year 1 revenue.
- The OPM Contract and Modification do *not* contain a "no cost" provision.
- The OPM Contract and Modification do *not* contain a provision excluding payment for "start-up" costs.
- The CAC lacks particularized facts showing the Executive Defendants had access to information regarding WageWorks's alleged non-entitlement to Base Year 1 revenue.
- The CAC fails to plead direct allegations of the Executive Defendants' contemporaneous knowledge of the KP Connector impairment.
- The CAC fails to plead direct allegations of the Executive Defendants' contemporaneous knowledge of the accounting treatment of the OPM revenue or KP Connector.

[1] *See* Ex. A (Dkt. No. 108-1). Plaintiffs have advised that they "do not object to this Court accepting as true the OPM Contract and its Modification 0001[.]" Dkt. No. 124 at 2.

Plaintiffs are left with their laundry list of inferences of scienter. Those suggested inferences are untethered to particularized facts and are unsupported (even rejected) by Ninth Circuit law. The numerous out-of-Circuit cases cited in the Opposition do not save the CAC in the face of on point law from the Ninth Circuit. Far from an "accounting fraud," the more plausible inference from a holistic view of the allegations, at most, involves a misinterpretation of the OPM Contract and resulting accounting error, which was corrected when discovered. In fact, Plaintiffs' proclamation of fraud defies common sense. Why would WageWorks risk a de-listing of its stock, a restatement of its financial statements, regulatory scrutiny, and time-consuming and expensive litigation – *all for revenue amounting to less than one percent of total 2016 revenue*?

In addition, Plaintiffs have abandoned their market revelation theory of loss causation and now advocate a proximate cause theory that falls short. And by requesting an amendment to its pleadings on standing, Plaintiff PERA acknowledges that it lacks statutory standing for the Section 11 claim as currently pleaded. The CAC should be dismissed.

PLAINTIFFS MISREPRESENT THE STANDARD APPLICABLE TO THIS REFORM ACT CASE

There is no question that to survive a motion to dismiss, the CAC must "state with particularity the circumstances constituting fraud or mistake" (Fed. R. Civ. P. 9(b)) and, as mandated by the Reform Act, "plead with particularity both falsity and scienter." *Zucco Partners LLC v. Digimarc Corp.*, 552 F.3d 981, 990 (9th Cir. 2009) (citation omitted). Yet tellingly, Plaintiffs posit that "[a] complaint 'does not need detailed factual allegations,' but only needs to allege 'enough facts to state a claim to relief that is plausible on its face.'" Opp. at 3 (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007)). Plaintiffs are wrong. As a case cited in the Opposition explains, "because Plaintiffs' claims are predicated on securities fraud, more than just the *Twombly/Iqbal* standard must be met." *In re Leapfrog Enter., Inc. Sec. Litig.*, 237 F. Supp. 3d 943, 949-50 (N.D. Cal. 2017); *see Costabile v. Natus Med. Inc.*, 293 F. Supp. 3d 994, 1007 (N.D. Cal. 2018) (White, J.) (discussing *Twombly/Iqbal* standards and noting, "[a] heightened pleading standard, however, applies to this [securities fraud] case"). Because the Reform Act requires much more than the *Twombly/Iqbal* standard, the CAC should be dismissed.

ARGUMENT

I. THE CAC FAILS TO STATE A SECTION 10(B) CLAIM BECAUSE IT FAILS TO PLEAD A STRONG INFERENCE OF SCIENTER

A. Plaintiffs Effectively Concede They Do Not Allege Particularized Facts Showing Defendants' Knowledge of Any Misrepresentation

As demonstrated in the Opening Brief, the CAC fails to adequately show that the Executive Defendants believed the Company was not entitled to Base Year 1 revenue, or had contemporaneous knowledge of the KP Connector impairment or of the accounting for that impairment or OPM revenue. Opening Br. at 6, 8-9. Fatally, the Opposition does not point to allegations of such direct knowledge and thus, effectively concedes these points. *See Costabile,* 293 F. Supp. 3d at 1014 ("Plaintiff has abandoned this theory by failing to respond to Defendants' arguments regarding it in his opposition to the motion to dismiss."). Instead, Plaintiffs' leading argument is based on inferences they attempt to draw from certain terms of the OPM Contract (*see* Opp. at 16-17) but, as shown below, their argument fails because Plaintiffs either concede the key contractual terms discussed in the Opening Brief or outright ignore them. The following comparison makes that evident:

WageWorks' Opening Brief	Plaintiffs' Opposition
• "First, the Contract plainly shows a unit price for services provided in '*Base Year 1 (March 1, 2016 – Aug. 31, 2016)*.' Ex. A at 4 (emphasis added)." Opening Br. at 7.	The Opposition concedes that the Contract began in Base Year 1 as well as the definition of Base Year 1: • "During the first year of the contract, March 1, 2016 through August 31, 2016 ('Base Year 1'), WageWorks was required . . ." Opp. at 6.
• "Second, the Modification did not include a 'no cost' provision, as Plaintiffs insist. CAC ¶¶ 72, 88, 122, 163. It did not concern payments to the Company at all but simply added enhanced security and information technology requirements. *See* Ex. C." Opening Br. at 7.	The Opposition does not acknowledge this argument, ***does not point to any "no cost" provision*** in the Modification (or Contract) and does not dispute the nature of the Modification. Instead, Plaintiffs respond with the same conclusory and incorrect statements: • "WageWorks was required, **at no cost to OPM**, to develop and establish . . ." Opp. at 6. (emphasis in original). • "Given the 'no cost' Contract and MOD0001 . . ." Opp. at 8.
• "Third, Plaintiffs admit the Company *was* entitled to payment for Base Year 1 services	The Opposition concedes that WageWorks began administrating the program on

no later than September 1, 2016. *See* CAC ¶ 6 (the Company "was not entitled to be paid . . . until WageWorks began administering the OPM Contract . . . on its 'implementation date' of September 1, 2016"); *id.* ¶ 84 (noting the Company *met* the September 1 deadline)." Opening Br. at 7 (footnote omitted).	September 1, 2016: • "WageWorks would not begin administering the program until September 1, 2016." Opp. at 5-6.
• "Fourth, unable to dispute the Company's actual performance, Plaintiffs suggest that Base Year 1 services were for start-up services, not included in the Contract. CAC ¶ 87. Yet the Contract mentions 'start-up' costs only once, in the context of sharing ideas: 'we are interested in your innovative ideas and proposals on how to limit start-up costs.' Ex. A at 40." Opening Br. at 7 (footnote omitted).	The Opposition does not acknowledge this argument, ***does not point to any contractual provision excluding payment for "start up" services,*** and does not dispute the contractual reference to "start-up" costs. Instead, it repeats the CAC's conclusory allegation: • "OPM made clear that WageWorks was responsible for 'funding and accounting for its startup cost' . . . ¶ 87." Opp. at 8. ◦ The Opposition ignores that this purported OPM communication allegedly occurred sometime *after* the Company submitted its invoice in February *2017*, nearly a year after the Contract began. *See* CAC ¶¶ 86-87; *see also id.* ¶ 122 (OPM's final denial of WageWorks' certified claim was on December 22, 2017). Plaintiffs' allegations actually *support* the inference of the *lack* of scienter in *2016* as they imply that OPM did not inform the Company that the Company was responsible for "start-up" costs until sometime *after* February 2017 and as late as December 2017. • "WageWorks was not entitled to fees for 'start up' . . . *Id.*" Opp. at 8.
• "Finally, the Company's ongoing legal action against OPM for OPM's failure to pay (Ex. B at 28) demonstrates its then and now belief that it is legally entitled to such payment." Opening Br. at 7.	The Opposition does not dispute the existence and substance of the Company's ongoing legal action against OPM. It simply ignores it.

Plaintiffs' failure to respond to the absence of a "no cost" and "no start-up cost" provision, upon which their case is predicated, constitutes an abandonment of those theories of scienter. *See Costabile,* 293 F. Supp. 3d at 1014. But even without abandonment, Plaintiffs' scienter theories are without merit due to their failure to make the threshold showing of the existence of such provisions. *See id.* at 1018 (plaintiff's argument "that the fact that the Supply

Contract was not executed provided strong evidence of scienter . . . fails because Plaintiff has not adequately alleged that the Supply Contract was unexecuted.”).

With the collapse of their theory of the case, Plaintiffs shift to the theory that “WageWorks could not earn or realize revenue under the per participant, per month term of the OPM contract for ‘Contract Year 1’ – March 1, 2016 through August 31, 2016, *given that there were no participants yet, and plan administration would not commence . . . until September 1, 2016.*” Opp. at 7-8 (emphasis added); *see id.* at 19 (“**WageWorks had no ‘participants’ to administer**, and thus bill for, **prior to September 1, 2016**.”) (emphasis in original). To the extent this “participant” theory is coherent, it is a red-herring and leads to a dead end as well.

Plaintiffs’ own pleading refutes the assertion of “no ‘participants’” in the program prior to September 1, 2016. *See* CAC ¶ 71 (incumbent administrator processed claims through August 23, 2016). This error aside, Plaintiffs apparently are saying the *effect* of the fixed price and the September 1 implementation date somehow precluded payment for services rendered prior to September 1 (the date that WageWorks’ platform went live and WageWorks took over the processing of claims from the incumbent administrator). *Id.* ¶¶ 60, 88. The suggested inferential leap from the lone fixed price term to a wholesale forfeiture of payment for an entire Base Year is not supported by any facts and is contrary to other key contractual terms, such as the clear definition of “Base Year 1,” the broad definition of “FSAFEDS Administration,” and the provision explicitly stating that the contract price “includes all costs associated with providing the services *for the Program*”– not just for processing participants’ claims.[2] Ex. A at 4-9 (emphasis added). Plaintiffs also read too much into the September 1 date. They point to no contractual provision stating that payment for Base Year 1 would not be paid until the implementation date, and in any event, it is undisputed that WageWorks met the implementation date. Thus, the Company would be entitled to payment even under Plaintiffs’ theory.

The Opposition effectively concedes the following key contractual terms (or absence thereof): (1) the OPM Contract commenced on March 1, 2016; (2) Base Year 1 was March 1, 2016 through August 31, 2016; (3) WageWorks was to perform “FSAFEDS Administration”

[2] Plaintiffs do not contend that the Base Year 1 services provided by WageWorks were *not* “for the Program.”

services during Base Year 1 (and all Base Years); (4) the term "FSAFEDS Administration" was defined in the Contract; (5) the Contract provided a fixed price for Base Year 1 (and all Base Years); (6) the price "includes all costs associated with providing the services for the Program" (Ex. A at 9); (7) the Contract and Modification did not contain a "no-cost" provision; (8) the Contract and Modification did not state that "start-up" costs were not compensable; (9) the Contract contained a September 1, 2016 implementation date, which WageWorks satisfied; and (10) WageWorks performed under the Contract. These facts, at a minimum, refute any notions that the Company's belief in 2016 of entitlement to Base Year 1 revenue was "highly unreasonable . . . involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care." *Zucco*, 552 F.3d at 991 (citation omitted).

As mentioned, Plaintiffs' silence also concedes the absence of facts showing what the Executive Defendants knew about the accounting treatment of the OPM revenue or KP Connector and when. Instead, Plaintiffs rely heavily on the Restatement's "admission" that OPM revenue "should not have been recognized." Opp. at 13 (citing CAC ¶ 153); *see id*. at 19. In rejecting a similar argument, this Court held "Plaintiff cannot rely on that fact [defendants' acknowledgement in the Restatement of their incorrect interpretation of accounting rule] alone to establish scienter and must allege facts to show that 'the defendants knew specific facts at the time that rendered their accounting determinations fraudulent.'" *In re Taleo Corp. Sec. Lit.*, 2010 WL 597987, at *8 (N.D. Cal. Feb. 17, 2010) (White, J.) (citation omitted).[3]

In lieu of specific facts, Plaintiffs offer up the "straight-forward" calculation of OPM revenue due to the fixed contract price, and the size of the KP impairment write-off. *See* Opp. at 18-20. That does not salvage their allegations. For example, in *Zamir v. Bridgepoint Educ., Inc.*, 2018 WL 1258108, at *4 (S.D. Cal. Mar. 12, 2018), the complaint alleged in support of its scienter allegations that "the measurement of the revenue [that] should have been recognized is capable of precise measure." The court held that the complaint did not sufficiently plead scienter. *Id.* at *19. Moreover, as shown above, the fixed contract price does not render Base

[3] Plaintiffs cite confirming authority elsewhere in the Opposition. *See Curry v. Hansen Med., Inc.*, 2011 WL 3741238, at *7 (N.D. Cal. Aug. 25, 2011) ("The fact that Defendants acknowledged in the Restatement that certain revenue should have been deferred does not indicate that they were withholding this information from investors.").

Year 1 services non-compensable and therefore, makes the allegedly "straight-forward" nature of the calculation irrelevant. *See* p. 5, *supra*. The size of the KP impairment also is insufficient. The Ninth Circuit, in affirming the dismissal of large restatement cases, has consistently held that a mere restatement or GAAP violation, even an obvious or large one, is insufficient to show scienter.[4] Lower courts have repeatedly so held too.[5] As one court recently explained, "[v]iolations of GAAP, 'even significant ones or ones requiring large or multiple restatements, must be augmented by other specific allegations that defendants possessed the requisite mental state." *Zamir*, 2018 WL 1258108, at *7 (dismissing restatement case based on improper revenue recognition) (citation omitted).

Plaintiffs' cases to the contrary are inapposite because they involved "widespread" and "significant" inflation of revenue that were pleaded with "particularity" and that were *in addition to* well-pleaded allegations of *direct* evidence of scienter. For example, the complaint in *In re McKesson HBOC, Inc. Sec. Litig.*, 126 F. Supp. 2d 1248 (N.D. Cal. 2000), alleged "with particularity" "significant" GAAP violations in addition to "substantial evidence" of "widespread" improper revenue recognition and other "much more direct evidence" of scienter. *Id*. at 1273.[6] Here, the accounting error was insignificant (less than 1% of the total 2016 revenue), is not pleaded with particularity, is limited to a small portion of just one contract, and

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[4] *See Webb v. SolarCity Corp.*, 884 F.3d 844, 855 (9th Cir. 2018) ("the magnitude and duration of the GAAP violations," among other allegations, did not sufficiently plead scienter); *DSAM Global Value Fund v. Altris Software, Inc.*, 288 F.3d 385, 387, 390 (9th Cir. 2002) (refusing to find scienter based on the alleged "fail[ure] to see the obvious" GAAP violations relating to revenue recognition; "the mere publication of inaccurate accounting figures, or a failure to follow GAAP, without more, does not establish scienter") (citation omitted); *see also Metzler Inv. GMBH v. Corinthian Colls., Inc.*, 540 F.3d 1049 (9th Cir. 2008) (affirming dismissal of restatement case based on improper revenue recognition).

[5] *See, e.g., Taleo*, 2010 WL 597987, at *9, 13 (dismissing restatement case where the restatement spanned more than four fiscal years); *Plichta v. SunPower Corp.*, 790 F. Supp. 2d 1012, 1018 (N.D. Cal. 2011) (alleged "magnitude, duration, manner and simplicity" of alleged accounting fraud, combined with other allegations, were insufficient to plead scienter); *In re U.S. Aggregates, Inc. Sec. Litig.*, 235 F. Supp. 2d 1063, 1072-73 (N.D. Cal. 2002) (alleged "nature, duration and magnitude" of restatement were insufficient to plead scienter; "even an obvious failure to follow GAAP does not give rise to an inference of scienter").

[6] Similarly, *In re Daou Sys., Inc.*, 411 F.3d 1006 (9th Cir. 2005), involved allegations of "systematic" improper revenue recognition as well as "specific allegations of direct involvement in the production of false account statements and reports." *Id.* at 1017, 1023. Plaintiffs' handful of out-of-state cases (Opp. at 18) are irrelevant in the face of the well-developed relevant law within the Ninth Circuit. *See* nn. 4 & 5, *supra*.

stands alone, without any direct allegation of scienter. Even the *McKesson* court observed that "courts have rejected attempts to bootstrap conclusory allegations of GAAP violations into proof of intentional or reckless misconduct." *Id.* Bootstrapping is precisely what Plaintiffs have done.

Plaintiffs turn to the KP Connector, emphasizing "the magnitude of the impairment was 100% of the value of the asset[.]" Opp. at 19. Yet the very case they cite refused to find an inference of scienter simply because "Defendants wrote off 100% of goodwill[.]" *Leapfrog*, 237 F. Supp. 3d at 951. Thus, even Plaintiffs' own legal authority shows that a 100% impairment of an asset's value is not indicative of scienter.[7] Likewise, the Ninth Circuit has refused to find scienter based on, *inter alia*, a 100% write down of an asset (goodwill). *See City of Dearborn Heights Act 345 Police & Fire Ret. Sys. v. Align Tech., Inc.*, 856 F.3d 605, 612, 620-21 (9th Cir. 2017) ("the more compelling inference is that Defendants made a good faith but mistaken determination in its goodwill valuations"). Plaintiffs further argue that "Defendants knew" the KP Connector "was valueless as far back as 2016" (Opp. at 19) because the Restatement disclosed "the client notified the Company that it no longer required the services provided by the Company" in 2Q 2016. *Id.* at 7. But the CAC provides no factual details about the notification, the Executive Defendants' alleged awareness of it, or the factors relevant to the assessment of the value of the KP Connector. In essence, "Plaintiff argues that the Court should find a strong inference of scienter based simply on the contention that Defendants should have known better . . . That alone is insufficient." *Rentech*, 2018 WL 4802058, at *9.[8]

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[7] While the *Leapfrog* court found "specific allegations" regarding a 96% write-off of long-lived assets sufficient to allege scienter (237 F. Supp. 3d at 954-55), it did so based on a flaw in the defendants' reason for the write-off: "as Defendants justified the long-lived impairment write-off in 4Q based on an obvious stock decline, but that stock decline was obvious as of 3Q or shortly thereafter." *Id.* at 954. That is, "the corporate defendants there offered an explanation that on its face was nonsensical[.]" *Cheng Jiangchen v. Rentech, Inc.*, 2018 WL 4802058, at *9 (C.D. Cal. June 7, 2018) (distinguishing *Leapfrog*). Here, the reason for the write-off – the discontinuation of the customer using the KP Connector – is not "nonsensical."

[8] Plaintiffs also rely on *In re Ibis Tech. Sec. Litig.*, 422 F. Supp. 294, 316 (D. Mass. 2005), where the Court found that the delay in an impairment write-down contributed to defendants' alleged motive and was sufficient to plead scienter. *Ibis* is irrelevant because under First Circuit precedent, allegations of motive and opportunity may be sufficient to plead scienter (*id.* at 316) whereas the Ninth Circuit has rejected such allegations to support a strong inference of scienter. *See Zucco*, 552 F.3d at 991 ("motive to commit fraud and opportunity to do so . . . are not sufficient to establish a *strong* inference of deliberate recklessness") (quoting *In re Silicon Graphics Sec. Litig.*, 183 F.3d 970, 974 (9th Cir. 1999)) (emphasis in original).

B. Inadequate Internal Controls and "Tone at the Top" Do Not Support Scienter

The Opening Brief demonstrated that a "Restatement's admissions of material weaknesses in [company's] internal controls, including its admission of an 'inappropriate tone at the top,' do not weigh in favor of inferring scienter." *In re Hertz Glob. Holdings, Inc.*, 905 F.3d 106, 118 (3d Cir. 2018); *see* Opening Br. at 9-10.[9] Effectively conceding this point, Plaintiffs argue that their internal controls and tone at the top allegations "when viewed in combination with other revelations and facts" result in a strong inference of scienter. Opp. at 21. The "other revelations" and "facts," however, are nothing more than conclusions unsupported by specific facts. *See id.* at 21-22 (internal controls were "exploited" by Jackson and Callan, the corporate culture "lacked ethics or integrity," "they manipulated the numbers," "issued false invoices," etc.). The Court, however, is not required to "assume the truth of legal conclusions merely because they are cast in the form of factual allegations." *Fayer v. Vaughn*, 649 F.3d 1061, 1064 (9th Cir. 2011) (citation omitted); *see Daou*, 411 F.3d at 1013 ("conclusory allegations of law and unwarranted inferences are insufficient to defeat a motion to dismiss") (citation omitted).

In addition, Plaintiffs' authority suggesting that faulty internal controls are sufficient to raise a strong inference of scienter has been consistently rejected within the Ninth Circuit. *See* Opening Br. at 9-10.[10] As one court explained, "[p]resumably every company that issues a financial restatement because of GAAP errors will cite as a reason lack of effective controls." *In re Hansen Natural Corp. Sec. Litig.*, 527 F. Supp. 2d 1142, 1158 (C.D. Cal. 2007).[11] Finally,

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[9] Also, what Plaintiffs characterized as "damning admissions" in the Restatement (Opp. at 21) is impermissible pleading by hindsight. *See, e.g., Alaska Elec. Pension Fund v. Asar*, 768 F. App'x 175, 185 (5th Cir. 2019) ("Without knowing what Kirk and McHenry said or did, it is equally credible that they realized that the tone at the top was inappropriate only with hindsight.").

[10] *See also Karpov v. Insight Enter., Inc.*, 2010 WL 2105448, at *10 (D. Ariz. Apr. 30, 2010) ("Allegations that Insight had material weaknesses in its internal controls do not, standing alone, give rise to a strong inference of scienter on the part of the company or its executives."); *In re Hypercom Corp. Sec. Litig.*, 2006 WL 1836181, at *9 (D. Ariz. July 5, 2006) ("the fact that Hypercom issued a press release recognizing a lack of effective internal controls, is not overly probative as to whether Smolak intentionally misclassified the leases.").

[11] In addition, in the case plaintiffs cite, *In re Akorn, Inc. Sec. Litig.*, 240 F. Supp. 3d 802 (N.D. Ill. 2017), the complaint sufficiently alleged facts showing the executive defendants' direct knowledge of the inadequacies. *Id.* at 819. Here, all the CAC pleads is the existence of internal control deficiencies and the blanket assertion that the Executive Defendants "exploit[ed]" those

Plaintiffs fail to link the deficient "internal controls" and "tone at top" allegations to the purported OPM revenue or KP Connector fraud.[12] Even allegations sourced from so-called "confidential witnesses" fail to do so.

C. The Confidential Witness Allegations are Insufficient and Do Not Supply the Missing Support for Plaintiffs' Scienter Allegations

WageWorks demonstrated that Plaintiffs' "confidential witnesses" are fundamentally *un*reliable because they lack personal knowledge and their proffered vague and conclusory statements are themselves not indicative of scienter. Opening Br. at 10-11. In fact, the infirmities afflicting Plaintiffs' CWs also doomed the CWs in *U.S. Aggregates*. In that case, Judge Wilken rejected the proffered CW allegations, finding that (1) "many of the [CW] allegations are not linked to the GAAP violations," (2) allegations that "numbers were 'manipulated,'" that the company was a "dirty company" and that the CEO "managed by intimidated" were "too generalized and vague," and (3) "none of the confidential witnesses have any first-hand knowledge of [company's] accounting decisions." *U.S. Aggregrates*, 235 F. Supp. 2d at 1074. Plaintiffs fail to address these and other deficiencies identified by WageWorks, do not refute the numerous cases cited by WageWorks, and merely regurgitate the same conclusory and defective CW allegations of the CAC – all without citing a single supporting legal authority.[13] *See* Opp. at 23-24. At bottom, Plaintiffs' CW allegations "say[] nothing about the Defendants' knowledge of the improprieties, their intentions, or their participation in accounting fraud." *Rok I*, 2017 WL 35496, at *15.

D. The Other Allegations Do Not Rectify Plaintiffs' Failure to Plead Particularized Facts Supporting Scienter

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deficiencies. *See, e.g.*, CAC ¶¶ 178-79. That is not enough. *See McGee v. Am. Oriental Bioengineering, Inc.*, 2014 WL 12586107, at *12 (C.D. Cal. Sept. 23, 2014) ("Plaintiffs do not point to any fact to establish [executive defendant's] intent to exploit (unidentified) control weaknesses other than the fact that . . . it happened") (citation omitted).

[12] *See Rok v. Identiv, Inc.*, 2017 WL 35496, at *11 (N.D. Cal. Jan. 4, 2017) ("*Rok I*") (rejecting hands-on management allegations as indicative of scienter where "there are no allegations here that Hart or Nelson were directly involved in producing false accounting statements."), *aff'd sub nom. Cunningham v. Identiv, Inc.*, 716 F. App'x 663 (9th Cir. 2018).

[13] Plaintiffs actually cite authority elsewhere in the Opposition that supports some of WageWorks' arguments regarding the unreliability of the CWs. *See In re Silicon Storage Tech., Inc. Sec. Litig.*, 2007 WL 760535, at *32 (N.D. Cal. Mar. 9, 2007) (finding "irrelevant" "allegations from information obtained from 'confidential informants' who left their employment at SST long before the commencement of the proposed class period"; dismissing complaint).

Core Operations Theory. In an attempt to transform the OPM Contract into an intent to defraud, Plaintiffs argue the "OPM Contract was a key contract" and therefore "Jackson and Callan had to have been aware" of the contractual terms by virtue of their corporate positions. Opp. at 16 (emphasis omitted). As previously shown, the core operations theory is inapplicable because, *inter alia*, the CAC fails to plead particularized facts regarding the Executive Defendants' actual access to the disputed information. Opening Br. at 13. By failing to respond to this argument, Plaintiffs have abandoned this avenue of the core operations theory. *See Costabile*, 293 F. Supp. 3d at 1014. Plaintiffs thus concede that the CAC lacks facts showing that any Executive Defendant had actual access to information regarding the Company's alleged non-entitlement to Base Year 1 revenue.

Instead, Plaintiffs rest their entire argument on the second avenue of the core operations theory: "in rare circumstances where the nature of the relevant fact is of such prominence that it would be 'absurd' to suggest that management was without knowledge of the matter." *Webb*, 884 F.3d at 854 (quoting *S. Ferry LP, No. 2 v. Killinger*, 542 F.3d 776, 785-86 (9th Cir. 2008)); *see* Opp. at 17 ("It would be both illogical and absurd for Jackson and Callan not to have known the essential OPM Contract terms"). But the CAC pleads no "unusual circumstances" (*S. Ferry*, 542 F.3d at 785) showing that it would be "absurd" for the Executive Defendants to believe the Company was entitled to Base Year 1 revenue. Even assuming *arguendo* the Executive Defendants' knowledge of the "essential OPM Contract terms," such terms support the conclusion of a right to payment. *See* Section I.A., *supra*. The plain language of the Contract, Plaintiffs' failure to refute that language, and the absence of any allegation of non-performance by WageWorks dispels any notion of absurdity. Moreover, Plaintiffs fail to explain how the amount of revenue reversed in the Restatement – *less than one percent* of the previously reported total revenue for fiscal 2016 – was "of such prominence" to support a finding of "absurdity."[14]

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[14] *Compare In re Immersion Corp. Sec. Litig.*, 2011 WL 871650, at *5 (N.D. Cal. Mar. 11, 2011) (restatement of reported revenue by 15.3%, *inter alia*, is "not of such 'unusual' nature as to give rise to an inference of scienter") *with Berson v. Applied Signal Tech., Inc.*, 527 F.3d 982 (9th Cir. 2008) (core operations theory applied; complaint alleged defendants knew about stop-work orders on government contracts that made up 80% of the company's revenue).

Far from "unusual circumstances," the contested OPM revenue is really an ordinary breach of contract dispute. The core operations theory is inapplicable.

Allegations Based on Motive. Plaintiffs repeatedly argue that WageWorks improperly recognized OPM revenue to inflate the stock price in advance of the Secondary Offering. Opp. at viii, 1, 3, 5, 8-9, 20, 23, 28, 32. But such motive has been rejected by the Ninth Circuit as insufficient to provide an inference of scienter. *See Webb*, 884 F.3d at 856; *see also Anderson v. Peregrine Pharms., Inc.*, 654 F. App'x 281, 281 (9th Cir. 2016) ("we decline, as we have in the past, to find the Defendants' attempts at securing capital during the putative Class Period to support an inference of scienter.") (citation omitted). Even the Opposition cites confirming legal authority: "It is clear that in the Ninth Circuit private securities plaintiffs cannot aver intent in general terms of mere 'motive and opportunity.'" *Curry*, 2011 WL 3741238, at *7 (citation omitted) (allegations of two public equity offerings during the class period, one just months before the announcement of a restatement, "do not establish scienter.").[15] As the Ninth Circuit explained, "[s]urely every company that goes public wants to maximize its apparent profitability prior to its IPO and to maintain a high share price afterward[.]" *Webb*, 884 F.3d at 856.

SOX Certifications. The Ninth Circuit also routinely rejects allegations of scienter based on the defendants' signatures on SOX Certifications. Opening Br. at 14-15; *see also In re Lifelock, Inc. Sec. Litig.*, 690 F. App'x 947, 954 (9th Cir. 2017). Plaintiffs fail to show otherwise. In fact, they respond with citations to two cases, both of which held that SOX certifications did *not* support a strong inference of scienter.[16]

[15] Plaintiffs cite to *Daou* and a case from Virginia (*see* Opp. at 28), but neither is applicable. Unlike the allegations here, the allegations in *Daou* "present[ed] *more than* mere evidence of a motive and opportunity to commit fraud." 411 F.3d at 1024 (emphasis added). And the Virginia case appears to have relied primarily on Second Circuit law, which, unlike the Ninth Circuit, allows scienter to be pleaded by mere motive. *See In re MicroStrategy, Inc. Sec. Litig.*, 115 F. Supp. 2d 620, 642-43 (E.D. Va. 2000).

[16] *Curry*, 2011 WL 3741238, at *7 ("The facts alleged in the SCAC do not demonstrate that Defendants were aware of improper revenue recognition at the time the SOX certifications were made."); *Welgus v. TriNet Grp., Inc.*, 2017 WL 167708, at *9 (N.D. Cal. Jan. 17, 2017) ("Plaintiff does not . . . plead facts demonstrating that Goldfield and/or Porter signed the SOX certifications while aware of any error.").

E. The Post-Class Period Events Do Not Support Scienter

Executive Resignations. As previously shown, mere executive resignations cannot support a strong inference of scienter under Ninth Circuit law. Opening Br. at 15. Many of Plaintiffs' legal authorities, once again, come from outside the Ninth Circuit (Opp. at 27 n.30), and thus are irrelevant in the face of controlling Ninth Circuit precedent. *See* Opening Br. at 15; *see also Rentech*, 2018 WL 4802058, at *10 ("Resignations or terminations also do not support a strong inference of scienter."); *Rok I*, 2017 WL 35496, at *16 ("even if [CEO] was removed in connection with [company] announcing" alleged fraud, that "does not say that [CEO] committed fraud, much less that he had any particular intent in 2013 and 2014.").[17]

The Opening Brief also showed that "Plaintiffs have failed to plead facts regarding the Executive Defendants' alleged knowing or reckless involvement in a fraud" (Opening Br. at 15), sufficient to "refut[e] the reasonable assumption that the resignation occurred as a result of restatement's issuance itself[.]" *Zucco*, 552 F.3d at 1002. Plaintiffs respond with *no facts*, offering instead their naked incredulity. Say Plaintiffs, "It simply does not make sense that a company would terminate its CEO, CFO . . . absent a determination of fraudulent or illegal conduct or, at a minimum, deliberately reckless conduct relating to accounting fraud." Opp. at 27-28. This attempt to equate resignations with fraud has repeatedly been rejected. "Changes in leadership are only to be expected when leadership fails. That is not, in itself, a symbol of fraud." *Hertz*, 905 F.3d at 119; *see* Opening Br. at 15.[18]

Independent Auditors. Plaintiffs spill much ink on the concerns raised by KPMG in August 2018 (*see* Opp. at 24-27), yet cite not a single case to support the finding that KPMG's

[17] To the extent Plaintiffs rely on legal authority within the Ninth Circuit, the facts of those cases are not comparable to those at bar. For example, the firing of the CEO in *Luna v. Marvell Tech. Grp.*, 2017 WL 2171273 (N.D. Cal. May 17, 2017), supported a strong inference of scienter because it tended to refute defendants' theory that the alleged fraud was the result of sole decisions of a lower-level accountant. *Id.* at *4-5. So such allegations are present here.

[18] *See also In re Int'l Rectificer Corp. Sec. Litig.*, 2008 WL 4555794, at *16 (C.D. Cal. May 23, 2008) ("After [corporation] announced that investors could no longer rely on multiple financial statements, it is unremarkable that [corporation] would seek to change its management team to reassure investors."); *U.S. Aggregates*, 235 F. Supp. 2d at 1074 ("Plaintiff can point to no particularized allegation refuting the reasonable assumption that Defendant Stone was fired simply because the errors that lead to the restatement occurred on his watch or because he failed adequately to supervise his department.").

post-class period concerns *regarding the Audit Committee's interaction with KPMG during its 2018 independent investigation* is probative of what the Executive Defendants *knew in 2016 regarding the OPM Contract, the KP Connector and the related accounting*. They are not.

Rok I is instructive. There, the company disclosed that its independent auditor had (1) resigned and was "unwilling to be associated with the consolidated financial statements prepared by management," (2) advised the board of its expressed disagreement with the scope and remediation of the Special Committee's investigation, and (3) identified a material weakness with respect to "entity level controls," which concerned the results of the investigation undertaken by the Special Committee during 2015, senior management leadership and operating style, and the lack of an "open flow of information and communication." *Rok I*, 2017 WL 35496, at *3 (citations omitted). Judge Breyer rejected plaintiffs' argument that the auditor's resignation and concerns supported an inference of scienter, explaining that "[b]ecause the BDO resignation was tied to the Special Committee's 2015 investigation . . . the BDO resignation did not reflect a finding by BDO that Defendants made false statements in 2013 and 2014 about either an Entity Level Controls Weakness or Hart's compensation." *Id.* at *14.[19] In affirming that decision, the Ninth Circuit "adopt[ed] the detailed and well-reasoned analysis" of the District Court. *Cunningham*, 716 F. App'x at 664. *Rok I*'s conclusion and "well-reasoned analysis" applies equally here.

In lieu of legal authority and specific facts, the Opposition offers only unsupported conclusions wrapped in inflammatory language. *See* Opp. at 25 (Executive Defendants "fooled KPMG" by issuing a "false invoice" to OPM); *id.* ("KPMG obviously found illegal or fraudulent conduct."); *id.* at 26-27 ("to fool the auditors"). Plaintiffs' rhetoric of "fooling KPMG" rings hollow where the Company implemented all of KPMG's recommendations. *See, e.g.,* CAC ¶¶

[19] Judge Breyer reaffirmed this holding after the plaintiff moved for relief under Rule 60(b) based on alleged "new evidence" of the actual resignation letter. *See Rok v. Identiv, Inc.*, 2018 WL 807147, at *5 (N.D. Cal. Feb. 9, 2018) ("*Rok II*") ("The new evidence still does not address the relevant intent. That BDO resigned in November of 2015 because it believed that some of [CEO's] expenses were improper and that the Special Committee and the Board were not adequately investigating the Ruggiero complaint *does not mean that Defendants had a contemporaneous intent to defraud investors* when they made the challenged executive compensation statements in the three proxy statements *in 2013 and 2014*.") (emphasis added).

67, 149; Opening Br. at 16. And, Plaintiffs' bare claim of "false invoice" is not supported by any facts and is belied by the Company's action against OPM to collect on that invoice. Ex. B at 28.

EPS Guidance. Lastly, while the CAC does not denote guidance as an indicia of scienter (*see* CAC, § V), the Opposition repeatedly suggests that scienter should be inferred because the Company allegedly would not have met EPS guidance for 2Q 2016, 3Q 2016 and FY 2016 but for the improper accounting for the OPM revenue and KP Connector. *See* Opp. at viii, 1, 4, 8-9, 16, 20, 23, 30. This theory of scienter also is insufficient. As Judge Freeman explained, allegations that defendants manipulated an accounting formula to "portray the illusion of profitability" that caused an overstatement of sales gross margins for seven consecutive quarters, which enabled the company to raise $94 million in IPO and $396 million in subsequent stock and note offerings and to acquire companies, were insufficient to plead a strong inference of scienter. *Bao v. Solarcity Corp.*, 2016 WL 4192177, at *1, 7-8 (N.D. Cal. Aug. 9, 2016) (citation omitted), *aff'd sub nom. Webb v. Solarcity Corp.*, 884 F.3d 844 (9th Cir. 2018); *see also DSAM*, 288 F.3d at 388, 391 (affirming dismissal for lack of scienter where a restatement due to improper revenue recognition caused financial statement to change from a $2.4 million in net income to a $2.5 million *loss*).[20] Accordingly, Plaintiffs' new theory of scienter based on guidance is insufficient to raise the required strong inference of scienter.

F. Considered Holistically, the More Plausible Inference is the Defendants Acted in Good Faith

The Ninth Circuit has counseled that "[i]n assessing the allegations holistically as required by *Tellabs*," the district courts may view the allegations "with a practical and common-sense perspective." *S. Ferry*, 542 F.3d at 784. From a practical point of view, **it defies common sense that the Company would risk a de-listing of its stock, a restatement of its financial statements, regulatory scrutiny, and time-consuming and expensive litigation – all for a**

[20] Plaintiffs suggest scienter was found in *Stocke v. Shuffle Master, Inc.*, 615 F. Supp. 2d 1180, 1190 n.3 (D. Nev. 2009), because "'but for the accounting errors,' defendant would have 'missed its earnings guidance/consensus estimates' by $0.05 per share." Opp. at 20. Plaintiffs, however, merely quote *an allegation* in the complaint. In reality, scienter was based on the fact that defendants had improperly accounted for revenue one year after they had acknowledged and disclosed a similar error. *Stocke,* 615 F. Supp. 2d at 1188-89. The court found that "the similar circumstances" contributed to an overall inference of scienter. *Id.* at 1190.

revenue that amount to *less than one percent* of the total 2016 revenue. The more plausible inference from Plaintiffs' allegations is the Company reasonably interpreted the Contract as providing for payment for Base Year 1 services and, as a result of that interpretation, recorded revenue. *See* Opening Br. at 16-17. Plaintiffs fail to show otherwise. Moreover, "[e]ven if a set of allegations may create an inference of scienter greater than the sum of its parts, it must still be at least as compelling as an alternative innocent explanation." *Zucco*, 552 F.3d at 1006. Here, Plaintiffs' conclusory allegations, taken as a whole, do "not demonstrate[] that the 'malicious inference is at least as compelling as any opposing innocent inference.'" *Costabile*, 293 F. Supp. 3d at 1020 (citation omitted).

II. THE CAC DOES NOT STATE A SECTION 10(B) CLAIM BECAUSE IT FAILS TO SUFFICIENTLY ALLEGE LOSS CAUSATION

A. Plaintiffs Concede They Have Failed to Plead to Plead Loss Causation Based on a Revelation-Of-Fraud Theory

Plaintiffs do not refute the argument that their loss causation theory – based solely on market revelation of the fraud[21] – fails because none of the alleged corrective disclosures revealed the alleged KP Connector fraud and the March 1-2 and September 12 disclosures did not reveal the alleged revenue recognition fraud. *See* Opening Br. at 17-18. The Opposition points to *no* revelatory language in any alleged corrective disclosure, arguing instead that "express disclosure of the fraud is not required." Opp. at 36. Plaintiffs thus have abandoned the market revelation theory of loss causation. *See Costabile*, 293 F. Supp. 3d at 1014.

Plaintiffs now seek to escape dismissal by proffering another theory. *See* Section II.B., *infra*. But the Ninth Circuit has counseled, "[w]hen plaintiffs plead a causation theory based on market revelation of the fraud, this court naturally evaluates whether plaintiffs have pleaded or prove the facts relevant to their theory." *Mineworkers' Pension Scheme v. First Solar, Inc.*, 881 F.3d 750, 754 (9th Cir. 2018). Plaintiffs have failed to plead loss causation "*relevant to their theory*." Under these circumstances, Plaintiffs' new theory does not save their deficient pleading. *See Rok II*, 2018 WL 807147, at *8 (upholding initial ruling that the complaint failed to plead loss causation under plaintiffs' original market revelation theory after plaintiffs offered a

[21] CAC ¶ 3 (investors "suffer[ed] significant economic harm when the truth was revealed and the Company's stock price dropped as a result."); *see id.* ¶¶ 23, 255, 257.

1 proximate cause theory under *First Solar*, and finding the "Court's analysis was consistent with,
2 and is unchanged by [*First Solar*]"); *Eng v. Edison Int'l*, 2018 WL 1367419, at *2, 4 (S.D. Cal.
3 Mar. 16, 2018) (similar). Whether by abandonment or inadequate allegations, Plaintiffs have
4 failed to plead loss causation based on market revelations of the alleged truth.

5 **B. Plaintiffs Have Failed to Plead Loss Causation Based on a General**
6 **Proximate Cause Theory**

7 Nor is Plaintiffs' new loss causation theory of avail. Plaintiff relies on *First Solar* (Opp.
8 at 33), which adhered to a general proximate cause theory of loss causation. *First Solar*, 881
9 F.3d at 753. Yet even under this theory, Plaintiffs still must sufficiently plead "a causal
10 connection between the material misrepresentation and the loss." *Dura Pharms., Inc. v. Broudo*,
11 544 U.S. 336, 342 (2005). As the Supreme Court emphasized, the alleged fraud must not merely
12 "'touch upon' a loss," it must actually "*cause* a loss." *Id*. at 343 (emphasis in original) (citing 15
13 U.S.C. § 78u-4(b)(4)). The Supreme Court has explained that proximate cause "demand[s] . . .
14 some *direct* relation between the injury asserted and the injurious conduct alleged." *Holmes v.*
15 *Sec. Inv'r Prot. Corp.*, 503 U.S. 258, 268 (1992) (emphasis added); *see also Nuveen Mun. High*
16 *Income Opportunity Fund v. City of Alameda*, 730 F.3d 1111, 1120 (9th Cir. 2013) (loss
17 causation is shown when defendants' misrepresentation "was *directly* related to the actual
18 economic loss") (emphasis added). "Put another way," the direct relation requirement means
19 that the "very facts" misrepresented or omitted must be "a substantial factor" in causing the loss.
20 *Nuveen*, 730 F.3d at 1120. In short, "[i]t is the exposure of the fraudulent representation that is
21 the critical component of loss causation." *In re Bofi Holding, Inc. Sec. Litig.*, 302 F. Supp. 2d
22 1128, 1136 (S.D. Cal. 2018) (citation omitted). The CAC fails to satisfy these standards of
23 proximate cause and to sufficiently plead facts adequate to support this theory, as required by
24 Rule 9(b). *See Oregon Pub. Emps. Ret. Fund v. Apollo Grp. Inc.*, 774 F.3d 598 (9th Cir. 2014).
25 To the extent Plaintiffs offer any coherent theory of proximate causation, it is too remote
26 and speculative to survive dismissal. For example, the first alleged corrective disclosure (March
27 1, 2018) revealed the Company was "delaying its Annual Report on Form 10-K for the year
28 ended December 31, 2017 and its financial results and associated conference call for the fourth

quarter of 2017." CAC ¶ 132. The disclosure provided *no reason for the delay*. From this brief one-sentence disclosure, Plaintiffs make the inferential leap – without any supporting facts – that somehow, "[t]his announcement signaled to the market" a series of specific news: (1) "the Company's financial results were unreliable"; (2) the Company "was not able to secure a much needed opinion from its auditor"; (3) the Company had "financial irregularities"; and (4) there was "false accounting." *Id.*; *see also* Opp. at 34. This conjecture of what investors understood from the March 1 disclosure is precisely the kind of indirect and speculative theory that cannot satisfy proximate cause requirements. *See Metzler*, 540 F.3d at 1064-65 (the court "is not required to indulge unwarranted inferences in order to save a complaint from dismissal"). After all, "a plaintiff will always be able to contend that the market 'understood' a defendant's statement precipitating a loss as a coded message revealing the fraud." *Id.* at 1064. But Plaintiffs fail to plead a single fact (let alone one that satisfies Rule 9(b)) to support the conclusion that the market perceived the delay in filing to be related to the KP Connector impairment, OPM revenue, or fraud. *See Inchen Huang v. Higgins*, 2019 WL 1245136, at *17 (N.D. Cal. Mar. 18, 2019) (no loss causation pleaded where plaintiffs failed to plead specific facts connecting the risks of the alleged off-label marketing to a subsequent decreased in prescriptions underlying the negative financial news disclosures).[22] Plaintiffs thus have failed to adequately plead a causal connection between the alleged misrepresentations and any loss due to the March 1, 2018 stock price decline. *See Daou*, 411 F.3d at 1027 (finding no proximate causation for losses suffered prior to August 1998 "because before the revelations began in August 1998, the true nature of Daou's financial condition had not yet been disclosed.").

The same is true of the March 2 disclosure of a material weakness in internal controls and the Audit Committee investigation. While Plaintiffs mouth the magic words of "causally connected" (Opp. at 35), they fail to explain how the "very facts" of the undisclosed KP Connector impairment or the OPM revenue proximately caused the loss, particularly where the stock price *increased* 8.9% following that disclosure. Ex. E at 11. The September 12 disclosure

[22] *Compare Lloyd v. CVB Fin. Corp.*, 811 F. 3d 1200, 1204, 1210-11 (9th Cir. 2016) (loss causation was pleaded where the market and analysts perceived the government subpoena to be related to defendant bank's alleged misstatements of a specific borrower's ability to repay loan).

of the Special Committee investigation also was not a corrective disclosure. "More investigations might mean more smoke, but that does not authorize the Court to speculate as to the likelihood of fire, absent 'an express disclosure of actual wrongdoing' within the announcement of the investigation, or 'a subsequent corrective disclosure.'" *Inchen Huang*, 2019 WL 1245136, at *17 (citations omitted). Here, that announcement did not disclose actual wrongdoing and no subsequent corrective disclosure is alleged or exists. And, to the extent Plaintiffs relies on the filing of the Restatement on March 18, 2019 (Opp. at 34), that filing did not disclose anything new and thus, is not a corrective disclosure.[23] Also, the stock price *rose* from $37.72 on March 15 (previous business day) to close at $39.58 on March 18. Ex. E at 16.

In sum, the Section 10(b) claim should be dismissed for failure to plead loss causation.

III. THE CAC DOES NOT STATE A SECTION 11 CLAIM BECAUSE, AS PLAINTIFF PERA ACKNOWLEDGES, IT LACKS STANDING

Plaintiff PERA lacks statutory standing to pursue a Section 11 claim because it has not sufficiently pleaded that its stock was issued in the Secondary Offering. Opening Br. at 18-20. In response, PERA argues it has pleaded standing because "the 'certification,' filed by PERA . . . confirms that PERA purchased 8,500 shares on the date of the Offering at $69.25 (the Offering price)." Opp. at 40. But as previously shown, allegations that shares were purchased "on the day of" the offering and "for the same offering price" are insufficient to establish Section 11 standing, which is consistent with Ninth Circuit precedent. Opening Br. at 20 (citing *Thomas v. Magnachip Semiconductor Corp.*, 167 F. Supp. 3d 1029, 1055 (N.D. Cal. 2016), and *In re Century Aluminum Co. Sec. Litig.*, 729 F.3d 1104, 1108 (9th Cir. 2013)). PERA fails to show otherwise. All three cases cited (Opp. at 40) are out-of-date, preceding *Century Aluminum* by as much as seventeen years.[24]

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[23] *See Bofi*, 302 F. Supp. 3d at 1136 ("If the alleged disclosure is duplicative of public information, the market will already have incorporated that information into the stock price"); *In re Maxim Integrated Prods., Inc. Secs. Litig.*, 639 F. Supp. 2d 1038, 1048 (N.D. Cal. 2009) ("a disclosure that does not reveal anything new to the market is, by definition, not corrective").

[24] Plaintiff PERA's attempt to distinguish *Century Aluminum* on the ground that it involved tracing of shares is unavailing where (1) the CAC claims that PERA purchased its shares "pursuant and traceable to" the Secondary Offering (*see* Opp. at 39-40), and (2) the opinion, by its own terms, set forth the legal principles applicable to statutory standing under Section 11

No doubt recognizing the inadequacies of its pleadings under current Ninth Circuit law, Plaintiff PERA claims it can cure its standing deficiency by amending its pleading to include transaction data purportedly showing that it purchased directly from the lead underwriter. Opp. at 41 n.46. PERA's proffer, however, may still fall short because the data could "also [be] consistent with [the underwriter] having filled the order with previously issued shares it was holding." *Century Aluminum*, 729 F.3d at 1109. "Something more is needed." *Id.* at 1108. The Ninth Circuit requires that PERA "exclude the possibility that [its WageWorks] shares came from the pool of previously issued shares" that the underwriter might have possessed. *Id.* The CAC fails to do so and therefore, the Section 11 claim should be dismissed. And any amendment that fails to sufficiently plead the required exclusion would be futile.

CONCLUSION

For the foregoing reasons and for the reasons stated in WageWorks' Opening Brief, the Court should dismiss the CAC.

Dated: November 8, 2019

Respectfully submitted,

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where, as here, there has been more than one offering of a company's stock. *See Century Aluminum*, 729 F.3d at 1109.