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United States District Court  
Northern District of California

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF CALIFORNIA

VICTORIA SHAEV,  
Plaintiff,  
v.  
JOHN D. BAKER, et al.,  
Defendants.

Case No.16-cv-05541-JST

**ORDER GRANTING IN PART AND  
DENYING IN PART MOTION TO  
DISMISS**

Re: ECF No. 99

Before the Court is nominal Defendant Wells Fargo & Company’s (“Wells Fargo”) motion to dismiss the Consolidated Amended Verified Amended Stockholder Derivative Complaint (“the Complaint”) pursuant to Rules 12(b)(6) and 23.1 for failure to adequately plead demand futility.<sup>1</sup> The Court will grant the motion as to Plaintiff’s claim under California Corporations Code section 25403, and deny it in all other respects.

**I. BACKGROUND**

This is a shareholder derivative action on behalf of nominal party Wells Fargo against the company’s officers and directors. Compl. ECF No. 83 at 6, ¶ 64.<sup>2</sup> Plaintiffs allege that, “[f]rom at least January 1, 2011 to the present (‘the Relevant Period’), Defendants knew or consciously disregarded that Wells Fargo employees were illicitly creating millions of deposit and credit card accounts for their customers, without those customers’ knowledge or consent.” *Id.* ¶ 1.

**A. The Parties**

Wells Fargo is a financial and bank holding company that provides retail, commercial, and

<sup>1</sup> The Individual Director Defendants joined in Wells Fargo’s motion. See ECF Nos. 100-102, 107-08, 110.

<sup>2</sup> The Court refers to the pagination created by the electronic docketing system (ECF) throughout this Order.

1 corporate banking services. Id. ¶ 66. The company is incorporated in Delaware and  
2 headquartered in San Francisco, California. Id. Wells Fargo’s largest reportable operating  
3 segment<sup>3</sup> during the relevant period, the Community Banking division, “focuses on diversified  
4 financial products and services to customers and small businesses, including checking and savings  
5 accounts, credit and debit cards, as well as auto, student, and small-business lending.” Id. ¶ 69.

6 The Lead Plaintiffs are Fire and Police Pension Association of Colorado and the City of  
7 Birmingham Retirement and Relief System. Id. ¶¶ 61, 63. Plaintiffs have owned Wells Fargo  
8 common stock since at least January 1, 2011 and remain current stockholders of the company. Id.  
9 ¶ 1, 65.

10 The Individual Defendants were officers and directors of the company during the relevant  
11 period. Defendant John G. Stumpf served as Wells Fargo’s CEO from June 2007 until his  
12 resignation on October 12, 2016. Id. ¶ 70. He was also a director between June 2006 and January  
13 2010, when he became Chairman of the Board. Id. Following Stumpf’s resignation in October  
14 2016, Defendant Timothy J. Sloan became Wells Fargo’s CEO. Id. ¶ 71. Defendant Carrie  
15 Tolstedt served as Senior Executive Vice President of the Community Banking division from June  
16 2007 to July 2016. Id. ¶ 72. The Director Defendants during the relevant time period include:  
17 John D. Baker II (director since January 2010); Elaine L. Chao (director from July 2011 to January  
18 2017); John S. Chen (director since September 2006); Lloyd H. Dean (director since June 2005);  
19 Elizabeth A. Duke (director since January 2015); Susan E. Engel (director since May 1998);  
20 Enrique Hernandez (director since January 2003); Donald M. James (director since January 2009);  
21 Cynthia H. Milligan (director since July 1992); Enrique Peña (director since November 2011);  
22 James H. Quigley (director since October 2013); Judith M. Runstad (director from May 1998 to  
23 April 2016); Stephen W. Sanger (director since 2003); Susan G. Swenson (director since  
24 November 1998); Suzanne M. Vautrinot (director since February 2015). ¶¶ 76–91.

25

26

27 <sup>3</sup> An “operating segment” is a firm component for which discrete financial information is available  
28 and which meets other specified criteria. Statement of Fin. Accounting Standards No. 131, ¶ 10  
(Fin. Accounting Standards Bd. 1997). A segment becomes “reportable” when it has assets,  
revenues, or profits of at least 10 percent of all operating segments of the company. Id. ¶ 18.

1           **B.     Cross-Selling**

2           Throughout the relevant period, Wells Fargo’s financial condition and prospects were  
3 dependent upon cross-selling – i.e., the sale of new products and services to existing customers.

4           Id.

5           ¶ 3.

6           As explained in Wells Fargo’s 2006 Annual Report, “[s]elling more products to [its]  
7 customers – or “cross-selling” – is the foundation of [its] business model and key to [its] ability to  
8 grow revenue and earnings.” Id. ¶ 126. The 2007 Annual Report further explained that “the  
9 Bank’s ‘primary strategy to achieve [its] vision’ was ‘to increase the number of products our  
10 customers buy from us and to give them all of the financial products that fulfill their needs.’” Id.  
11 ¶ 127 (brackets added). The same 2007 Report went on to explain that the “cross-sell strategy and  
12 diversified business model . . . ‘facilitate growth in strong and weak economic cycles, as we can  
13 grow by expanding the number of product out current customers have with us.’” Id. That Report  
14 further noted that “Wells Fargo was ‘known across [its] industry as number one, second to none,  
15 for cross-sell and revenue growth.’” Id. (emphasis omitted). The 2010 Annual Report similarly  
16 touted Wells Fargo as “the king of cross-sell.” Id. ¶ 130. Likewise, the 2013 Annual Report  
17 stated that “cross-sell of our products is an important part of our strategy to achieve our vision to  
18 satisfy all our customers’ financial needs . . . . We believe there is more opportunity for cross-sell  
19 as we continue to earn more business from our customers.” Id. ¶ 134 (emphasis omitted). Wells  
20 Fargo’s 2013 SEC filings explained that cross-selling was critical to the company’s financial  
21 success:

22           Our “cross-selling” efforts to increase the number of products our customers buy from us  
23 . . . is a key part of our growth strategy, and our failure to execute this strategy effectively  
24 could have a material adverse effect on our revenue growth and financial results. Selling  
25 more products to our customers – “cross-selling” – is very important to our business model  
and key to our ability to grow revenue and earnings...

26           Id. ¶ 135.

27           The company tracked and reported yearly cross-sell numbers, and this “was often the first  
28 metric announced in the Annual Reports to shareholders.” Id. ¶ 142.

1 Cross-selling numbers progressively grew between 1998, “when the products per retail  
2 banking household was 3.2,” and 2010, when that number reached an average of 6.14 products per  
3 household. Id. ¶ 142. That number reached its zenith in 2014, at 6.17 products per household.  
4 Id. ¶ 144.

5 **C. Gr-Eight Initiative**

6 To achieve their cross-selling goals, “Defendants imposed strict quotas regulating the  
7 number of products Wells Fargo bankers must sell.” Id. ¶ 2.

8 As early as 1999, the bank established the “Great Eight” or “Gr-Eight” initiative, which set  
9 a goal of selling eight products per household. Id. ¶¶ 124–25.

10 “The number of accounts Wells Fargo employees opened were also closely tracked.  
11 Several former Wells Fargo employees have recounted they were required to open 15 new  
12 accounts for products each day.” Id. ¶ 146. Daily sales for each branch were reported to the  
13 district manager four times a day. Id. And “[e]mployees who were unable to meet their sales  
14 goals faced the prospect of termination.” Id.

15 Plaintiffs allege “[t]hose quotas translated into unrelenting pressure on bankers to open  
16 numerous accounts per customer.” Id. ¶ 2. “And because Wells Fargo’s success in cross-selling  
17 was central to its financial results and market participants’ assessment of the Company,  
18 Defendants were also highly motivated to foster, and perpetuate, those unlawful practices.” Id.

19 **D. Letter to Stumpf and the Audit and Examination Committee in September**  
20 **2007**

21 In September 2007, Stumpf and the Board’s Audit and Examination Committee received  
22 letters from an employee discussing how the Gr-Eight Initiative created a high pressure sales  
23 culture that resulted in unethical and illegal activity, including fraud. Id. ¶¶ 22, 484. The letter  
24 warned that, “[l]eft unchecked, the inevitable outcome shall be one of professional and  
25 reputational damage, consumer fraud and shareholder lawsuits, coupled with regulator sanctions.  
26 Id.

27 **E. EthicsLine**

28 Wells Fargo began tracking employee complaints regarding unethical sales practices

1 through EthicsLine – a service through which employees can report ethics and compliance  
2 concerns to Wells Fargo via a third party – in 2008. Id. ¶¶ 23, 159. Through this system,  
3 employees could report “gaming” – defined as “the manipulation and/or misrepresentation of  
4 product solutions or product solutions reporting in order to receive or attempt to receive  
5 compensation, or to meet or attempt to meet goals” and “sales incentives.” Id. ¶¶ 23, 158. After  
6 an employee reported an ethics or compliance concern through EthicsLine, the information was  
7 provided to Wells Fargo’s Office of Global Ethics. Id. ¶ 151.

8 Stumpf later confirmed in his written responses to questions posed by the Senate Banking  
9 Committee that “from at least 2011 forward, the Board’s Audit and Examination Committee  
10 received period reports on activities of Wells Fargo’s Internal Investigations group (which  
11 investigates issues involving team members), as well as information on EthicsLine and suspicious  
12 activity reporting. Among other things, several of those reports discussed increases in sales  
13 integrity issues or in notifications to law enforcement in part relating to the uptick in sales  
14 integrity issues.” Id. ¶ 155.

15 **F. Litigation between 2008 and 2013**

16 Between 2008 and 2013, several lawsuits against the company involved allegations of  
17 unauthorized account-creation practices. Id. ¶¶ 24–26, 33, 35, 212-219, 501.

18 In 2008 a former Wells Fargo employee won a whistleblower lawsuit against the company  
19 relating to the creation of fake brokerage accounts in 2008. Id. ¶ 24. “In the case, a division of the  
20 U.S. Department of Labor (“DOL”) found there was ‘reasonable cause to believe’ Wells Fargo  
21 violated whistleblower protection laws by transferring the employee after he flagged illegal  
22 activity.” Id.

23 In 2009, six former employees brought wrongful termination suits in which they alleged  
24 that they were fired for reordering debit cards without customer authorization after they had been  
25 instructed to do so by their manager. Id. ¶ 25, 213.

26 In 2010, two former Wells Fargo employees filed a discrimination lawsuit in which they  
27 pointed to unethical sales activities and unauthorized account openings at the Company. Id. ¶¶ 26,  
28 214.

1 In 2012, seven former Wells Fargo employees filed a complaint asserting similar  
2 allegations. Id. ¶¶ 33, 217.

3 In 2013, another former employee filed a lawsuit “alleging she was retaliated against and  
4 wrongfully terminated after her supervisor forced her to open accounts in the names of family  
5 members.” Id. ¶¶ 35, 218.

6 **G. Communications to Stumpf and Human Resources Executives in 2011**

7 In 2011, two branch managers – one in New Jersey and one in Arizona – emailed Stumpf  
8 warning him that employees were creating fake accounts to meet the company’s sales quotas. Id.  
9 ¶ 28. One of those branch managers, Rasheeda Kamar, stated in her email that she was fired after  
10 failing to meet sales quotas because she did not tolerate the creation of fake accounts. Id. ¶ 200.  
11 The other branch manager, Ricky Hansen, reported the fraudulent accounts to Human Resources  
12 and EthicsLine. Id. ¶ 201–02. He was fired a month later for improperly looking up the  
13 fraudulent account information, which he did at EthicsLine’s request. Id.

14 **H. Los Angeles Times Article in December 2013**

15 On December 21, 2013, the Los Angeles Times published an article reporting that, “[t]o  
16 meet quotas, [Wells Fargo] employees have opened unneeded accounts for customers, ordered  
17 credit cards without customers’ permission and forged client signatures on paperwork.” Id. ¶ 37.  
18 The article further noted “[t]he relentless pressure to sell [that] has battered employee morale and  
19 led to ethical breaches.” Id. The article’s conclusions were based on “a review of internal bank  
20 documents and court records, and from interviews with 28 former and seven current Wells Fargo  
21 employees who worked at bank branches in nine states, including California.” Id.

22 Stumpf later admitted during his testimony before the Senate Banking Committee in  
23 September 2016 that he discussed the December 2013 Los Angeles Times article with the Board.  
24 Id. ¶ 40.

25 **I. Communication to Stumpf and the Board in April 2015**

26 On April 3, 2015, a former Wells Fargo banker mailed and emailed a letter to Stumpf and  
27 the Board advising them of ‘unethical practices in sales due to the continuous management threat  
28 of negative consequences if they did not produce ‘solutions’ in double digits on daily basis, the

1 threat has come to ‘do whatever it takes to get this [sic] numbers.’” Id. ¶¶ 44, 205. “During the  
2 next several months, the former employee repeatedly emailed Wells Fargo representatives,  
3 copying the Board, asking for updates.” Id. ¶ 44, 207.

4 **J. Litigation in May 2015**

5 The December 2013 Los Angeles Times article prompted a year-long investigation into the  
6 illicit account-creation practices by L.A. City Attorney Michael Feuer, which led to the filing on  
7 May 4, 2015 of a civil enforcement action on behalf of California consumers. Id. ¶ 42. In that  
8 complaint, the L.A. City Attorney alleged “that . . . Wells Fargo employees opened banking and  
9 financial accounts, products, and services for California customers without their knowledge or  
10 consent . . .” Id. ¶¶ 499, 172-78, 42.

11 On May 14, 2015, a consumer class action challenging the illicit account-creation scheme  
12 was filed against Wells Fargo in this district. Id. ¶¶ 45, 179-82, 500.

13 **K. OCC Supervisory Letters between 2014 and 2016**

14 The Office of the Comptroller of the Currency (“OCC”) began supervising Wells Fargo’s  
15 governance and risk management practices in January 2012. Id. ¶ 31.

16 In 2014, “[t]he OCC specifically identified the need to assess cross-selling and sales  
17 practices as part of its upcoming examination of the Bank’s governance processes.” Id. ¶ 222.

18 In 2015, the OCC issued several Supervisory Letters “regarding required corrective action  
19 in the Bank’s enterprise-wide risk management and oversight of its sales practices,” among other  
20 issues. Id. ¶ 485, 220-238, 46. For example, the OCC issued a Supervisory Letter in June 2015  
21 highlighting the following “MRAs,” or “Matters Requiring Attention”: “the lack of an appropriate  
22 control or oversight structure given corporate emphasis on product sales and cross-selling,” “the  
23 lack of an enterprise-wide sales practices oversight program,” “the lack of a formalized  
24 governance process to oversee sales practices and effectively oversee and test branch sales  
25 practices,” and “the failure of the Bank’s audit services to identify the above issues or to aggregate  
26 sales practice issues into an enterprise view.” Id. ¶ 503.<sup>4</sup>

27 \_\_\_\_\_  
28 <sup>4</sup> “The OCC defines MRAs as practices that ‘[d]eviate from sound governance, internal control,  
and risk management principles, which may adversely impact the bank’s earnings or capital, risk

1           **L.       Consent Orders**

2           On September 8, 2016, the L.A. City Attorney, U.S. Consumer Financial Protection  
3 Bureau (CFPB) and the OCC issued separate consent orders and press releases disclosing  
4 widespread deficiencies and unsafe or unsound practices in Wells Fargo’s risk management and  
5 oversight of its sales practices. Id. ¶ 9.

6           The CFPB’s consent order stated “that from January 1, 2011 to September 8, 2016  
7 thousands of Wells Fargo employees engaged in improper sales practices ‘to satisfy sales goals  
8 and earn financial rewards under [the Company’s] incentive-compensation program,’ leading the  
9 Company to terminate approximately 5,300 employees for engaging in those practices.” Id. ¶ 10  
10 (quoting Wells Fargo Bank, N.A., 2016-CFPB-0015 (Consumer Financial Protection Bureau Sept.  
11 8, 2016)). “In all, the CFPB found that the Bank ‘opened hundreds of thousands of unauthorized  
12 deposit accounts and applied for tens of thousands of credit cards for consumers’ without their  
13 knowledge or consent.” Id.

14           **M.       Congressional Investigation**

15           In September 2016, Stumpf testified before the Senate Banking Committee and the House  
16 Financial Services Committee. ¶¶ 15–16.

17           At the hearing before the House Financial Services Committee, Stumpf testified that “the  
18 Board, from 2011 to 2013, would get reports at a Committee level, at a high level about ethics  
19 lines [EthicsLine], requests, or information at not a granular but maybe at the company level.” Id.  
20 ¶ 29. He further testified that “[t]he board was made aware, generally, of issues by – in  
21 committees, at high levels in the 2011, ’12 time frame. By 2013, we had talked about maybe in  
22 one – I can’t remember which committee it was, surely by 2014, and then when we finally  
23 connected the dots on customer harm in ’15, the board was very active on this.” Id. ¶ 260, 498.

24           In his written responses to questions posed by the Senate Banking Committee, Stumpf  
25 confirmed that, “[f]rom at least 2011 forward, the Board’s Audit and Examination Committee  
26 received periodic reports on the activities of Wells Fargo’s Internal Investigations group (which

27 \_\_\_\_\_  
28 profile, or reputation, if not addressed’; or ‘[r]esult in substantive noncompliance with laws and  
regulations, . . .” Id. ¶ 46.

1 investigates issues involving team members), as well as information on EthicsLine and suspicious  
2 activity reporting.” Id. ¶¶ 30, 261. Stumpf explained that, “[a]mong other things, several of those  
3 reports discussed increases in sales integrity issues or in notifications to law enforcement in part  
4 relating to the uptick in sales integrity issues.” Id. Stumpf stated that other committees –  
5 including the Risk Committee and the Human Resources Committee – also received reports  
6 regarding sales integrity issues. Id. Stumpf admitted that “[s]ales integrity issues were also  
7 discussed periodically with the Board.” Id.

8 Stumpf testified before the Senate Banking Committee that he learned of the fraud in 2013  
9 and that the Board learned of it “later [in] 2013 and then 2014 and on.” Id. ¶ 41. He further  
10 testified that he recalls learning of the increase in the number of reports of sales-practice issues in  
11 late 2013. Id. ¶ 169. He stated that the reports regarding the opening of fraudulent accounts “got  
12 to the board level – it got to the corporate level in 2013 because progress was not being made.” Id.  
13 ¶ 258. He further testified: “And I know in 2014, various committees of the Board were made  
14 aware of this. The risk committee, the audit and examination [committee], the corporate  
15 responsibility [committee].” Id.

16 **N. Procedural History**

17 Based on the misconduct alleged above, several entities filed shareholder derivative  
18 complaints in this district, which have since been consolidated into a single action. ECF Nos. 39,  
19 70. The Court appointed Lieff Cabraser Heimann & Bernstein and Saxena White as Co-Lead  
20 Counsel. ECF No. 70.

21 In the consolidated complaint, Plaintiffs assert the following causes of action: (1) breach of  
22 fiduciary duty (against all Defendants); (2) unjust enrichment (against all Defendants); (3) breach  
23 of fiduciary duty for insider selling and misappropriation of information (against the Insider  
24 Selling Defendants); (4) violation of Section 14(a) of the Exchange Act and SEC Rule 14a-9  
25 (against the Director Defendants); (5) violations of Section 10(b) of the Exchange Act and SEC  
26 Rule 10b-5 (against all Defendants); (6) violation of Section 20A of the Exchange Act (against  
27 Insider Selling Defendants); (7) violations of Section 29(b) of the Exchange Act (against all  
28 Defendants); (8) violation of Section 25402 of the California Corporations Code (against the

1 Insider Selling Defendants); (9) violation of Section 25403 of the California Corporations Code  
2 (against the Director Defendants); (10) corporate waste (against the Director Defendants); (11)  
3 contribution and indemnification (against Defendants Stumpf, Shrewsberry, Sloan, and Tolsted).  
4 Id., ¶¶ 524–596. Plaintiffs seek declaratory relief, damages, injunctive relief, restitution, and  
5 attorneys’ fees. Id. at 185–86.

## 6 **II. LEGAL STANDARD**

7 Federal Rule of Civil Procedure 8(a)(2) requires that a complaint contain “a short and plain  
8 statement of the claim showing that the pleader is entitled to relief.” While a complaint need not  
9 contain detailed factual allegations, facts pleaded by a plaintiff must be “enough to raise a right to  
10 relief above the speculative level.” Bell Atl. Corp. v. Twombly, 550 U.S. 544, 555 (2007). To  
11 survive a Rule 12(b)(6) motion to dismiss, a complaint must contain sufficient factual matter that,  
12 when accepted as true, states a claim that is plausible on its face. Ashcroft v. Iqbal, 556 U.S. 662,  
13 678 (2009). “A claim has facial plausibility when the plaintiff pleads factual content that allows  
14 the court to draw the reasonable inference that the defendant is liable for the misconduct  
15 alleged.” Id. While this standard is not a probability requirement, “where a complaint pleads facts  
16 that are merely consistent with a defendant's liability, it stops short of the line between possibility  
17 and plausibility of entitlement to relief.” Id. (internal quotation marks omitted). In determining  
18 whether a plaintiff has met this plausibility standard, the Court must accept all factual allegations  
19 in the complaint as true and construe the pleadings in the light most favorable to the  
20 plaintiff. Knieval v. ESPN, 393 F.3d 1068, 1072 (9th Cir. 2005).

## 21 **III. ANALYSIS**

22 Nominal Defendant Wells Fargo moves to dismiss the Complaint pursuant to Rule  
23 12(b)(6) and Rule 23.1 on the ground that Plaintiffs have failed to adequately plead demand  
24 futility. ECF No. 99.

### 25 **A. Requests for Judicial Notice**

26 The Court first addresses Wells Fargo’s requests for judicial notice. ECF No. 99-2; ECF  
27 No. 116-2.

28 “As a general rule, we may not consider any material beyond the pleadings in ruling on a

1 Rule 12(b)(6) motion.” United States v. Corinthian Colleges, 655 F.3d 984, 998–99 (9th Cir.  
2 2011) (internal quotation marks and citations omitted). However, “[t]he court may judicially  
3 notice a fact that is not subject to reasonable dispute because it: (1) is generally known within the  
4 trial court’s territorial jurisdiction; or (2) can be accurately and readily determined from sources  
5 whose accuracy cannot reasonably be questioned.” Fed. R. Evid. 201(b). The Court “must take  
6 judicial notice if a party requests it and the court is supplied with the necessary information.” Fed.  
7 R. Evid. 201(c).

8 The Court takes judicial notice of the following documents under the incorporation by  
9 reference doctrine: Los Angeles Times Article from December 21, 2013 (Exhibit A); Office of the  
10 Comptroller Currency’s Consent Order in the Matter of Wells Fargo Bank, N.A. (Exhibit D);  
11 Stumpf’s testimony before the U.S. Senate Committee on Banking, Housing, and Urban Affairs on  
12 September 20, 2016 (Exhibit E). A court may “take into account documents ‘whose contents are  
13 alleged in a complaint and whose authenticity no party questions, but which are not physically  
14 attached the [plaintiff’s] pleading.” Knieval v. ESPN, 393 F.3d 1068, 1076 (9th Cir. 2005)  
15 (quoting In re Silicon Graphics Inc. Sec. Litig., 183 F.3d 970, 986 (9th Cir.1999)). Each of these  
16 exhibits is referenced in the complaint and Plaintiffs do not question the authenticity of these  
17 documents. Plaintiffs oppose this request on the ground that Wells Fargo relies on these exhibits  
18 to challenge factual assertions in the Plaintiffs’ complaint that could reasonably be disputed – for  
19 example, to show that Wells Fargo took adequate remedial actions. ECF No. 115-1 at 2-4. This  
20 argument fails. See Fecht v. Price Co., 70 F.3d 1078, 1083, n. 1 (9th Cir. 1995) (rejecting  
21 Plaintiffs’ argument that the district court improperly considered the full text of documents that  
22 were only partially pleaded in the complaint) (citing Branch v. Tunnell, 14 F.3d 449, 454 (9th  
23 Cir.), cert. denied, 512 U.S. 1219 (1994)). District courts are “entitled to take notice of the full  
24 contents of the published articles referenced in the complaint, from which the truncated quotations  
25 were drawn.” Bell Atl. Corp. v. Twombly, 550 U.S. 544, 569, n. 13 (2007) (citing Fed. Rule Evid.  
26 201). However, because the facts contained in the documents are subject to reasonable dispute,  
27 “the Court takes judicial notice only of the statements contained therein, but not for the purpose of  
28 determining the truth of those statements.” In re LDK Solar Sec. Litig., 584 F. Supp. 2d 1230,

1 1254 (N.D. Cal. 2008) (internal quotation marks and citations omitted).

2 Second, the Court takes judicial notice of several SEC filings (Motion Exhibits B, F-I,  
3 K-L, N-P, and Reply Exhibit C). These exhibits are properly subject to judicial notice.  
4 See Metzler Inv. GMBH v. Corinthian Colleges, Inc., 540 F.3d 1049, 1064 n. 7 (9th Cir. 2008)  
5 (holding that the district court properly took judicial notice of publicly available financial  
6 documents and SEC filings); Pirelli Armstrong Tire Corp. Retiree Med. Benefits Trust v. Stumpf,  
7 No. C 11-2369 SI, 2012 WL 424557, at \*4 (N.D. Cal. Feb. 9, 2012) (granting defendants’ request  
8 for judicial notice of documents that Wells Fargo filed with the SEC). Plaintiffs oppose judicial  
9 notice of the SEC filings to the extent the Court is inclined to accept the truth of the matters  
10 asserted therein. ECF No. 115-1 at 4-5; ECF No. 118. Again, the Court takes judicial notice of  
11 the statements in the SEC filings, but not for the purpose of determining the truth of those  
12 statements.

13 Third, Wells Fargo requests that the Court take judicial notice of documents from  
14 government websites, including the Bureau of Labor Statistics, the Federal Deposit Insurance  
15 Corporation, the U.S. Census Bureau, the Center for Disease Control, and PACER (Exhibits C,  
16 Q-T). Again, Plaintiffs oppose this request to the extent the documents are considered for the  
17 truth of the matters asserted therein. ECF No. 115-1 at 7. The population data, labor statistics,  
18 and public court docket information contained in these exhibits is not reasonably subject to  
19 dispute. Therefore, the Court takes judicial notice of these exhibits. See Daniels-Hall v. Nat'l  
20 Educ. Ass’n, 629 F.3d 992, 998–99 (9th Cir. 2010).

21 Fourth, the Court takes judicial notice of the news release titled “Wells Fargo Announces  
22 Actions Based on Retail Banking Sales Practices Investigation” (Exhibit M), which was released  
23 by Wells Fargo on February 21, 2017. The Court takes judicial notice of Exhibit M solely “to  
24 indicate what was in the public realm at the time, not whether the contents of those articles were in  
25 fact true.” Von Saher v. Norton Simon Museum of Art at Pasadena, 592 F.3d 954, 960 (9th Cir.  
26 2010) (quoting Premier Growth Fund v. Alliance Capital Mgmt., 435 F.3d 396, 401 n. 15 (3d  
27 Cir.2006)).

28 Fifth, the Court takes judicial notice of court filings in other cases and search results from

1 the PACER database (Motion Exhibits J and T, and Reply Exhibits A and B) because they are  
 2 matters of public record. See Reyn’s Pasta Bella, LLC v. Visa USA, Inc., 442 F.3d 741, 746 n. 6  
 3 (9th Cir. 2006) (“We may take judicial notice of court filings and other matters of public record”).  
 4 Again, the Court only takes judicial notice of the existence of these court filings, and does not  
 5 accept the matters asserted therein as true. Salas v. Gomez, No. 14-CV-01676-JST, 2016 WL  
 6 3971206, at \*5 (N.D. Cal. July 25, 2016) (“Although the Court ‘may take judicial notice of the  
 7 existence of unrelated court documents...it will not take judicial notice of such documents for the  
 8 truth of the matter asserted therein.’”) (quoting In re Bare Escentuals, Inc. Sec. Lit., 745 F. Supp.  
 9 2d 1052, 1067 (N.D. Cal. 2010) ).

10 Finally, the Court takes judicial notice of Wells Fargo’s stock price history between  
 11 December 20, 2013 and January 17, 2014 (Reply Exhibit D). Metzler Inv. GMBH v. Corinthian  
 12 Colleges, Inc., 540 F.3d 1049, 1064, n. 7 (9th Cir. 2008) (noting that judicial notice of “reported  
 13 stock price history and other publicly available financial documents” was proper).

14 The Court now turns to the merits of Defendants’ motion to dismiss.

15 **B. Pleading Standards under Rule 23.1**

16 “The derivative form of action permits an individual shareholder to bring ‘suit to enforce  
 17 a corporate cause of action against officers, directors, and third parties.’” Kamen v. Kemper Fin.  
 18 Servs., Inc., 500 U.S. 90, 95 (1991) (emphasis in original) (quoting Ross v. Bernhard, 396 U.S.  
 19 531, 534 (1970)).

20 However, “[a] shareholder seeking to vindicate the interests of a corporation through a  
 21 derivative suit must first demand action from the corporation’s directors or plead with particularity  
 22 the reasons why such demand would have been futile.” In re Silicon Graphics Inc. Sec. Litig., 183  
 23 F.3d 970, 989 (9th Cir. 1999), as amended (Aug. 4, 1999) (citing Fed.R.Civ.P. 23.1). “The  
 24 purpose of the demand requirement is to affor[d] the directors an opportunity to exercise their  
 25 reasonable business judgment and waive a legal right vested in the corporation in the belief that its  
 26 best interests will be promoted by not insisting on such right.” Kamen, 500 U.S. at 96 (internal  
 27 quotation marks omitted).

28 This demand requirement is articulated in Federal Rule of Civil Procedure 23.1, which

1 requires that a shareholder derivative complaint “state with particularity: . . . any effort by the  
2 plaintiff to obtain the desired action from the directors or comparable authority and, if necessary,  
3 from the shareholders or members; and . . . the reasons for not obtaining the action or not making  
4 the effort.” Fed. R. Civ. P. 23.1(b). Although “Rule 23.1 requires that a plaintiff allege specific  
5 facts,” a plaintiff is not required to plead particularized facts “sufficient to sustain a judicial  
6 finding,” nor is a plaintiff required to “plead evidence.” In re Ezc Corp Inc. Consulting Agreement  
7 Derivative Litig., No. CV 9962-VCL, 2016 WL 301245, at \*33 (Del. Ch. Jan. 25, 2016) (internal  
8 quotation marks and citations omitted).

9 **C. Demand Futility under Delaware Law**

10 Plaintiffs concede in the Complaint that they did not make a pre-suit demand on the Board  
11 before filing this action. ECF No. 83 ¶ 477. They allege that demand should be excused as futile.  
12 Id. ¶¶ 477-517.

13 “To show futility under Delaware law,<sup>5</sup> a plaintiff must allege particularized facts creating  
14 a reasonable doubt that (1) the directors are disinterested and independent, or (2) the challenged  
15 transaction was otherwise the product of a valid exercise of business judgment.” Silicon Graphics,  
16 183 F.3d at 990 (citing Aronson v. Lewis, 473 A.2d 805, 814 (Del. 1984), overruled on other  
17 grounds by Brehm v. Eisner, 746 A.2d 244 (Del. 2000)).

18 Plaintiffs allege that demand would have been futile for three reasons: (1) the Director  
19 Defendants’ conduct did not constitute a valid exercise of business judgment; (2) the Director  
20 Defendants face a substantial likelihood of liability due to their knowledge or conscious disregard  
21 of facts relating to the illicit account-creation scheme; and (3) the Board lacks independence from  
22 Stumpf because it repeatedly granted him excessive compensation. Id. ¶¶ 477-517.

23 The Court concludes that demand is futile because the allegations in the Complaint create a  
24 reasonable doubt as to whether a majority of the Director Defendants face a substantial likelihood  
25 of liability as to Plaintiffs’ claims.<sup>6</sup>

26 \_\_\_\_\_  
27 <sup>5</sup> Delaware law applies because Wells Fargo is a Delaware corporation. Kamen, 500 U.S. at 108–  
28 09 (“[A] court that is entertaining a derivative action under that statute must apply the demand  
futility exception as it is defined by the law of the State of incorporation.”).  
<sup>6</sup> Given this finding, the Court does not address the other demand futility theories.

1           **D.       Substantial Likelihood of Liability as to Plaintiffs’ Claims**

2           “[D]emand is excused if Plaintiffs’ particularized allegations create a reasonable doubt as  
3 to whether a majority of the board of directors faces a substantial likelihood of personal liability  
4 for breaching the duty of loyalty.” Rosenbloom v. Pyott, 765 F.3d 1137, 1150 (9th Cir. 2014).  
5 Because the Board contained fifteen directors at the time the first complaint was filed,<sup>7</sup> Plaintiffs  
6 must establish a reasonable doubt as to whether at least eight of those Directors could exercise  
7 disinterested and independent business judgment in responding to a demand. See Rales v.  
8 Blasband, 634 A.2d 927, 930 (Del. 1993).

9           “Demand will be excused only if the plaintiff’s allegations show the defendants’ actions  
10 ‘were so egregious that a substantial likelihood of director liability exists.’” Silicon Graphics, 183  
11 F.3d at 990 (quoting Aronson, 473 A.2d at 815). “[T]he mere threat of personal liability for  
12 approving a questioned transaction, standing alone, is insufficient to challenge either the  
13 independence or disinterestedness of directors.” Id. Neither are allegations that simply  
14 “describ[e] the calamity and alleg[e] that it occurred on the directors’ watch.” South v. Baker, 62  
15 A.3d 1, 14 (Del. Ch. 2012) (internal quotation marks omitted). Rather, a shareholder plaintiff  
16 “must plead facts establishing a sufficient connection between the corporate trauma and the board  
17 . . .” Id.

18           **1.       Breach of Fiduciary Duty Claims**

19           Plaintiffs allege that all fifteen Director Defendants face a substantial risk of personal  
20 liability “given their awareness or conscious disregard of significant red flags relating to the illicit  
21 account-creation scheme.” ECF No. 83 ¶¶ 483, 494. Plaintiffs further allege that the Board as a  
22 whole failed to fulfill its “duty to ensure wells Fargo’s systems were sufficiently well-designed to  
23 detect suspicious activity at the customer level,” and that “the Board either deliberately or  
24 recklessly failed to take remedial action to stop the illicit account-creation scheme.” Id. ¶¶

25 \_\_\_\_\_  
26 <sup>7</sup> Baker, Chao, Chen, Dean, Duke, Engel, Hernandez, James, Milligan, Peña, Quigley, Sanger,  
27 Stumpf, Swenson, and Vautrinot. ECF No. 83 ¶ 91. Although Stumpf resigned after the filing of  
28 the action, courts assess demand futility “as of the time the complaint is filed” because the relevant  
question is “whether the board that would be addressing the demand can impartially consider its  
merits without being influenced by improper considerations.” Rales v. Blasband, 634 A.2d 927,  
934 (Del. 1993).

1 495-96. As a result, Plaintiffs allege that “the Board is incapable or unwilling to take the actions  
2 required to seek the relief requested in this Complaint.” Id. ¶ 497.

3 To prevail on this theory of director oversight liability, Plaintiffs “must show that the  
4 directors knew they were not discharging their fiduciary obligations or that the directors  
5 demonstrated a conscious disregard for their responsibilities . . .” In re Citigroup Inc. S’holder  
6 Derivative Litig., 964 A.2d 106, 122–23 (Del. Ch. 2009) (emphases in original). This “scienter-  
7 based standard” is rooted in the Delaware Supreme Court’s decision in In re Caremark Int’l Inc.  
8 Derivative Litig., 698 A.2d 959 (Del. Ch. 1996). Desimone v. Barrows, 924 A.2d 908, 935–36  
9 (Del. Ch. 2007). In that case, the Delaware Supreme Court held that, “where a claim of directorial  
10 liability for corporate loss is predicated upon ignorance of liability creating activities within the  
11 corporation, . . . only a sustained or systematic failure of the board to exercise oversight – such as  
12 an utter failure to attempt to assure a reasonable information and reporting system exists – will  
13 establish the lack of good faith that is a necessary condition to liability.” Caremark, 698 A.2d at  
14 971. “Such a test of liability . . . is quite high.” Id. (describing breach of fiduciary duty claims  
15 asserted against the directors as “extremely weak” because the record “does not support the  
16 conclusion that the defendants either lacked good faith in the exercise of their monitoring  
17 responsibilities or conscientiously permitted a known violation of law by the corporation to  
18 occur”). The Delaware Supreme Court “reinforc[ed]” the Caremark decision in Stone ex rel.  
19 AmSouth Bancorporation v. Ritter, 911 A.2d 362 (Del. 2006). Desimone, 924 A.2d at 935.  
20 There, the Delaware Supreme Court held “that Caremark articulates the necessary conditions  
21 predicate for director oversight liability: (a) the directors utterly failed to implement any reporting  
22 or information system or controls; or (b) having implemented such a system or controls,  
23 consciously failed to monitor or oversee its operations thus disabling themselves from being  
24 informed of risks or problems requiring their attention.” Stone, 911 A.2d at 370 (citing Guttman  
25 v. Huang, 823 A.2d 492, 506 (Del. Ch. 2003)). “In either case, imposition of liability requires a  
26 showing that the directors knew that they were not discharging their fiduciary obligations.” Id.

27 Plaintiffs must allege scienter here for an additional reason: Wells Fargo’s charter  
28 exculpates its Directors from liability unless the directors breached their duty of loyalty or the

1 conduct involved bad faith, intentional misconduct, or a knowing violation of the law. See ECF  
2 No. 99-1 at 409, Ex. P. Section 102(b)(7) of the Delaware General Corporation Law permits a  
3 corporation to include such an exculpatory clause in a certificate of incorporation. In re Midway  
4 Games Inc., 428 B.R. 303, 316 (Bankr. D. Del. 2010), on reconsideration in part (Mar. 19, 2010)  
5 (citing 8 Del. C. § 102(b)(7)). Therefore, under both the standard for director oversight liability  
6 and the standard for director liability for breach of the duty of care when the company has adopted  
7 an exculpatory provision, Plaintiffs must “alleg[e] particularized facts that show that a director  
8 consciously disregarded an obligation to be reasonably informed about the business and its risks or  
9 consciously disregarded the duty to monitor and oversee the business.” Citigroup, 964 A.2d at  
10 125.

11 The extensive and detailed allegations in the complaint plausibly suggest that a majority of  
12 the Director Defendants did precisely that.<sup>8</sup>

13 First, Plaintiffs point to Stumpf’s admissions to both the Senate Banking Committee and  
14 the House Financial Services Committee regarding the Board’s monitoring of sales integrity  
15 issues. Where a complaint contains particularized allegations “that the Board continued to closely  
16 and regularly monitor [the realm where the illegal activity occurred],” a court “can – and at [the  
17 motion to dismiss] stage must – reasonably infer that the Board’s discussion of these matters  
18 afforded its members a view of [the company’s] illegal conduct.” Rosenbloom, 765 F.3d at 1152.

19 The Complaint includes such allegations. Specifically, the Complaint points to the following  
20 testimony that Stumpf gave to the House Financial Services Committee on September 29, 2016:  
21 “The board was made aware, generally, of issues by – in committees, at high levels in the 2011,  
22 ’12 time frame. By 2013, we had talked about maybe in one – I can’t remember which committee

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23  
24 <sup>8</sup> Because Plaintiffs allege that the Board as a whole or specific committees within the Board had  
25 knowledge of the illegal account-creation scheme, the Court does not evaluate demand futility on  
26 a director-by-director basis. Rosenbloom v. Pyott, 765 F.3d 1137, 1159, n. 13 (9th Cir. 2014)  
27 (“Although in many cases involving demand futility the parties go director by director to  
28 determine whether demand is excused, the parties here do not do so, mainly because Plaintiffs  
repeatedly allege that a majority of the Board was involved in all (or nearly all) of the programs  
and decisions at issue. When appropriate, courts may evaluate demand futility by looking to the  
whole board of directors rather than by going one by one through its ranks.”) (citing Pfizer, 722  
F.Supp.2d at 461).

1 it was, surely by 2014, and then when we finally connected the dots on customer harm in '15, the  
2 board was very active on this.” Id. ¶ 260, 498. Stumpf confirmed in written responses to  
3 questions posed by the Senate Banking Committee that, “[f]rom at least 2011 forward, the Board’s  
4 Audit and Examination Committee received periodic reports on the activities of Wells Fargo’s  
5 Internal Investigations group (which investigates issues involving team members), as well as  
6 information on EthicsLine and suspicious activity reporting.” Id. ¶ 261. Notably, Stumpf  
7 explained that, “[a]mong other things, several of those reports discussed increases in sales  
8 integrity issues or in notifications to law enforcement in part relating to the uptick in sales  
9 integrity issues.” Id. (emphasis added). Stumpf stated that other committees – including the Risk  
10 Committee and the Human Resources Committee – also received reports regarding sales integrity  
11 issues. Id. Stumpf admitted that “[s]ales integrity issues were also discussed periodically with the  
12 Board.” Id. In his testimony before the Senate Banking Committee, Stumpf testified that reports  
13 regarding the opening of fraudulent accounts “got to the board level – it got to the corporate level  
14 in 2013 because progress was not being made.” Id. ¶ 258. He further testified: “And I know in  
15 2014, various committees of the Board were made aware of this. The risk committee, the audit and  
16 examination [committee], the corporate responsibility [committee].” Id. Collectively, those three  
17 committees contain twelve out of the fifteen Directors who were on the Board at the time this  
18 complaint was filed. Id. ¶¶ 484, 490, 491. Therefore, these allegations plausibly suggest that a  
19 majority of the Director Defendants knew about the widespread illegal activity by 2014 at the  
20 latest, and perhaps as early as 2011, but nonetheless failed to take action, thereby consciously  
21 disregarding their fiduciary duty to monitor and oversee the business.

22 Second, Plaintiffs point to direct communications from a former Wells Fargo employee to  
23 the Board in 2015.<sup>9</sup> Specifically, Plaintiffs allege that, “[o]n April 3, 2015, a former Wells Fargo

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24  
25 <sup>9</sup> Plaintiffs also allege that the Audit and Examination Committee “failed to act when the  
26 Committee and Stumpf received a letter in September 2007 from an employee discussing how the  
27 Gr-Eight Initiative created a high pressure sales culture that resulted in ‘unethical and illegal  
28 activity,’ including ‘routine deception and fraudulent exploitation of [Wells Fargo’s] clients.” Id.  
¶¶ 22, 484. However, Plaintiffs do not allege that any of the current Director Defendants were on  
the Audit and Examination Committee in September 2007. See id. ¶¶ 484. Rather, according to  
other allegations in the complaint, it appears that those Director Defendants did not join the Audit

1 banker . . . mailed and emailed a letter to Stumpf and the Board advising them of ‘unethical  
2 practices in sales due to the continuous management threat of negative consequences if they did  
3 not produce solutions.’” Id. ¶¶ 44, 205. “During the next several months, the former employee  
4 repeatedly emailed Wells Fargo representatives, copying the Board, asking for updates.” Id.  
5 (emphasis added). Defendants’ only response to this allegation is that these communications “are  
6 not alleged to have been sent to the individual Board members but to an email address of  
7 unalleged ownership (BoardCommunications@wellsfargo.com).” ECF No. 99 at 18. But  
8 Delaware law does not require the Plaintiffs to plead “facts sufficient to sustain a ‘judicial finding’  
9 either of director interest or lack of director independence” or “to plead evidence” at this stage of  
10 the litigation. Ezcorp, 2016 WL 301245, at \*33; Brehm v. Eisner, 746 A.2d 244, 254 (Del. 2000).  
11 And a communication to an email address that is clearly associated with the Board and which  
12 warns of precisely the misconduct at issue here, especially when viewed in conjunction with the  
13 plethora of other allegations in the complaint regarding the Board’s knowledge, further supports  
14 the inference that the Director Defendants consciously disregarded their duties to the company.

15 Third, Plaintiffs point to several lawsuits between 2008 and 2013 which involved  
16 allegations of unauthorized account-creation practices at the company. ECF No. 83 ¶¶ 212-219,  
17 501. For example, Plaintiffs allege that a former Wells Fargo employee won a whistleblower  
18 lawsuit against the company relating to the creation of fake brokerage accounts in 2008. Id. ¶ 24.  
19 “In the case, a division of the U.S. Department of Labor (“DOL”) found there was ‘reasonable  
20 cause to believe’ Wells Fargo violated whistleblower protection laws by transferring the employee  
21 after he flagged illegal activity.” Id. Plaintiffs further allege that six former employees brought  
22 wrongful termination suits in 2009, in which they alleged that they were fired for reordering debit  
23 cards without customer authorization after they had been instructed to do so by their manager, and

24  
25 and Examination Committee until March 2010. See id. ¶¶ 76, 79, 82, 84, 85, 86, 89, 90.

26 Plaintiffs further allege that two branch managers emailed Stumpf regarding the creation of fake  
27 accounts in 2011, but they do not allege that these emails were sent to the Board, and “Delaware  
28 law does not permit the wholesale imputation of one director’s knowledge to every other for  
demand excusal purposes.” Id. ¶ 28; Desimone v. Barrows, 924 A.2d 908, 943 (Del. Ch. 2007).

1 that two former employees brought a discrimination lawsuit in 2010, in which they pointed to  
 2 unethical sales activities and unauthorized account openings at the Company. Id. ¶¶ 25-26,  
 3 213-14. In 2012, seven former Wells Fargo employees filed a complaint asserting similar  
 4 allegations. Id. ¶ 217. In 2013, another former employee filed a lawsuit “alleging she was  
 5 retaliated against and wrongfully terminated after her supervisor forced her to open accounts in the  
 6 names of family members.” Id. ¶ 218. In a complaint filed in May 2015, the L.A. City Attorney  
 7 alleged “that . . . Wells Fargo employees opened banking and financial accounts, products, and  
 8 services for California customers without their knowledge or consent . . .” Id. ¶¶ 499, 172-78, 42.  
 9 In the same month, a consumer class action challenging the same practices was filed in this  
 10 district. Id. ¶¶ 500, 179-82, 45.

11 Defendants respond that the Court should disregard these lawsuits because they involve  
 12 “unproven allegations in other litigations.” ECF No. 99 at 19, 21. However, Plaintiffs do not rely  
 13 on those lawsuits to show that the allegations asserted in them are factually true; rather, they rely  
 14 on the plain existence of those lawsuits to show that the Board was aware of yet another red flag.  
 15 Cf. Maine State Ret. Sys. v. Countrywide Fin. Corp., No. 2:10-CV-0302 MRP, 2011 WL  
 16 4389689, at \*19-21 (C.D. Cal. May 5, 2011) (striking portions of the complaint that “quote[d] and  
 17 cite[d] to unproven, untested allegations in complaints filed in separate lawsuits, as if they were  
 18 facts” because plaintiffs did “not reasonably investigate the allegations they copied from  
 19 complaints in other cases”). And, although Plaintiffs do not specifically allege that the Board  
 20 knew about these lawsuits, it is reasonable to infer at this stage of the litigation that the Board  
 21 would be aware of lawsuits stemming from sales practices that were essential to its cross-selling  
 22 strategy. In re Intuitive Surgical S'holder Derivative Litig., 146 F. Supp. 3d 1106, 1117 (N.D.  
 23 Cal. 2015) (“While Plaintiff does not specifically allege that information regarding the . . .  
 24 products liability lawsuits were brought to the board’s attention, . . . it is . . . reasonable to infer  
 25 that the board would have been aware of any product liability lawsuits arising from the da Vinci  
 26 system.”).

27 Fourth, Plaintiffs point to an article published by the Los Angeles Times on December 21,  
 28 2013 that described in detail how the intense pressure to meet cross-selling quotas drove

1 employees to open unauthorized customer accounts. Id. ¶ 37. This article is directly relevant to  
 2 Board knowledge because “Stumpf admitted during his testimony before the House Financial  
 3 Services Committee that he discussed the December 2013 L.A. Times article with the Board.” Id.  
 4 ¶¶ 40, 169. The article itself was based on “a review of internal bank documents and court  
 5 records, and [] interviews with 28 former and seven current Wells Fargo employees who worked  
 6 at bank branches in nine states, including California.”<sup>10</sup> Id. Plaintiffs allege that this article  
 7 “unquestionably alerted Defendants that [unlawful account-creation] activities were pervasive and  
 8 stemmed from the culture – directed by management and supported by the Board – of pressuring  
 9 Bank employees to grow accounts by any means necessary.” Id. ¶ 40.

10 Fifth, Plaintiffs point to significant regulatory interventions between 2012 and 2016.  
 11 Specifically, Plaintiffs allege that the Audit and Examination Committee “failed to act when it  
 12 received information” about several OCC Supervisory Letters between in 2015 “regarding  
 13 required corrective action in the Bank’s enterprise-wide risk management and oversight of its sales  
 14 practices,” among other issues. Id. ¶ 485, 220-238, 46. For example, the OCC issued a  
 15 Supervisory Letter in June 2015 highlighting the following “MRAs,” or “Matters Requiring  
 16 Attention”: “the lack of an appropriate control or oversight structure given corporate emphasis on  
 17 product sales and cross-selling,” “the lack of an enterprise-wide sales practices oversight  
 18 program,” “the lack of a formalized governance process to oversee sales practices and effectively  
 19 oversee and test branch sales practices,” and “the failure of the Bank’s audit services to identify  
 20 the above issues or to aggregate sales practice issues into an enterprise view.” Id. ¶ 503. Earlier,  
 21 in 2014, “[t]he OCC specifically identified the need to assess cross-selling and sales practices as  
 22 part of its upcoming examination of the Bank’s governance processes.” Id. ¶ 222.<sup>11</sup>

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23  
 24 <sup>10</sup> Wells Fargo’s gloss on the L.A. Times article – that it “informed the reader that the problem  
 was localized to Los Angeles,” ECF No. 116 at 11 – is flatly inconsistent with the article’s text.  
 25 <sup>11</sup> Defendants argue that these OCC supervisory letters were directed to Wells Fargo’s subsidiary,  
 Wells Fargo Bank, N.A., and only seven of the members of the Bank’s board were also members  
 26 of the Wells Fargo board. ECF No. 99 at 23-24. Although seven directors does not constitute a  
 majority of the Board, the Plaintiffs elsewhere allege, by way of Stumpf’s testimony and written  
 27 responses to Congressional committees, that the entire Board and several committees that  
 collectively make up a majority of the Board knew about these issues through other means –  
 28 namely, regular reporting on sales integrity issues and the opening of fraudulent accounts.

1 Sixth, Plaintiffs cite widespread employee terminations due to unauthorized account  
2 creation between 2011 and September 2016 as another red flag. According to the Consumer  
3 Financial Protection Bureau’s consent order from, “more than 5,300 Wells Fargo employees” were  
4 terminated during a five-year period “for conduct relating to the illicit account-creation scheme.”  
5 Id. ¶ 246, 505 (emphasis omitted). Plaintiffs further allege that “Wells Fargo terminated nearly  
6 1,000 employees in the retail banking sector for improper sales practices” in 2011 alone, but  
7 “Defendants took no action at that time.” Id. ¶ 247.

8 Seventh, because cross-selling was so essential to Wells Fargo’s financial growth and  
9 success during the relevant time period, it is reasonable to infer “that the Board was intensely  
10 interested in” the success of its cross-selling initiative, that the Board saw cross-selling “as a  
11 critical driver of growth” for the company, and that the Board “planned on very closely  
12 monitoring” cross-selling numbers. Rosenbloom, 765 F.3d at 1151-52. Indeed, “[y]early cross-  
13 sell numbers were also tracked and reported” and this “was often the first metric announced in the  
14 Annual Reports to shareholders.” ECF No. 83, ¶ 142. As noted above, the complaint further  
15 alleges that various committees of the Board did, in fact, “receiv[e] periodic reports on  
16 investigations into sales integrity issues and information from EthicsLine,” as confirmed by  
17 Stumpf’s testimony and written responses to Congress that the Board as a whole and several  
18 specific committees on the Board. See id. ¶¶ 159, 261. The rise in cross-selling numbers, which  
19 reached its peak in 2014, coincides with the rise in sales integrity issues: Stumpf told the Senate  
20 Banking Committee that he recalls learning of the increase in the number of reports of sales-  
21 practice issues in late 2013. Id. ¶¶ 144, 169. This further suggests that the Director Defendants  
22 knew about the illicit account-creation scheme.

23 Of course, these allegations regarding the importance of cross-selling and the simultaneous  
24 rise in cross-selling and sales integrity issues would not be sufficient on their own to establish  
25 conscious inaction on the part of the Board. See Rosenbloom, 765 F.3d at 1152 (noting that,  
26 although “the bare facts of the Board’s hunger for higher off-label sales and an ultimate increase in  
27

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28 Therefore, the regulatory interventions, though not sufficient on their own, bolster the Court’s  
conclusion that the Director Defendants consciously disregarded their duties to the company.

1 those sales do not suffice to show conscious inaction on the part of the Board,” the plaintiffs  
2 presented several other allegations that strongly supported an inference of conscious inaction).  
3 Rather, these allegations are just one piece of a much larger puzzle, as demonstrated by the  
4 numerous other allegations outlined above. Importantly, though, these allegations provide a  
5 reason why the Director Defendants might have chosen to consciously disregard their fiduciary  
6 duties and allow widespread illegal account creation practices to continue: Wells Fargo’s success  
7 was dependent upon cross-selling, which was in turn dependent upon the same strict sales quotas  
8 that drove employees to create fake accounts. Therefore, these allegations further bolster the  
9 Court’s conclusion that the Director Defendants consciously disregarded their fiduciary duties to  
10 the company.

11 Defendants respond that these red flags are insignificant when viewed in their larger  
12 context. For example, Defendants argue that the termination of 5,300 employees over the span of  
13 five years is minimal when viewed in light of the bank’s size and layoffs in the financial services  
14 sector during this time. ECF No. 99 at 17-18, n. 9. Defendants similarly argue that “[t]he  
15 existence of four employee complaints over a nine-year period in an organization as large as Wells  
16 Fargo hardly evidences the sort of systemic failure of controls that Plaintiffs must plead to support  
17 a failure of oversight claim.” *Id.* at 18. Defendants also contend that, “[i]f Wells Fargo’s  
18 Directors undertook to read all of those complaints [in which it is a named defendant], they would  
19 do nothing else.” *Id.* at 19.

20 As a preliminary matter, no one would expect the Director Defendants to read every  
21 complaint naming Wells Fargo as a defendant, it is not unreasonable to expect them to be aware of  
22 a large-scale lawsuit tied to the company’s central business strategy. *See, e.g., In re Biopure Corp.*  
23 *Derivative Litig.*, 424 F. Supp. 2d 305, 307–08 (D. Mass. 2006) (imputing knowledge of an FDA  
24 clinical hold to director defendants because the “company’s primary product or service [was] in  
25 jeopardy”) (citing *In re Keyspan Corp. Sec. Litig.*, 383 F. Supp. 2d 358, 387-88 (D.N.Y. 2003)).  
26 The action filed by the Los Angeles City Attorney in May 2015 certainly falls into that category.  
27 So does the consumer class action filed in this district, which Wells Fargo recently settled for \$110  
28 million. *See Jabbari v. Wells Fargo, N.A., et al.*, Case No. 15-cv-02159-VC, ECF No. 96 (N.D.

1 Cal. March 28, 2017). Moreover, all of these lawsuits raised the same issue – the creation of  
2 unauthorized accounts by employees – thereby pointing to a widespread problem within the  
3 company. Therefore, these allegations go to the heart of the Director Defendants’ duty to monitor  
4 and oversee operations after controls have been implemented in order to stay “informed of risks or  
5 problems requiring their attention.” Stone, 911 A.2d at 370 (citing Guttman v. Huang, 823 A.2d  
6 492, 506 (Del. Ch. 2003)).

7 More importantly, though, Defendants ignore the bigger picture by addressing each of  
8 these red flags in piecemeal fashion. While any of these red flags might appear relatively  
9 insignificant to a large company like Wells Fargo when viewed in isolation, when viewed  
10 collectively they support an inference that a majority of the Director Defendants consciously  
11 disregarded their fiduciary duties despite knowledge regarding widespread illegal account-creation  
12 activities, and therefore, that there is a substantial likelihood of director oversight liability. See  
13 Delaware Cty. Employees Ret. Fund v. Sanchez, 124 A.3d 1017, 1019 (Del. 2015) (“[I]t is  
14 important that the trial court consider all the particularized facts pled by the plaintiffs . . . in their  
15 totality and not in isolation from each other, and draw all reasonable inferences from the totality of  
16 those facts in favor of the plaintiffs.”). Like in Rosenbloom, the Plaintiffs have pointed to a  
17 “battery of particularized factual allegations that strongly support an inference at this stage of the  
18 litigation that the Board knew of and did nothing about illegal activity.” Rosenbloom, 765 F.3d at  
19 1152. Such allegations “that the board consciously failed to act after learning about evidence of  
20 illegality – the proverbial ‘red flag’” – are sufficient at the motion to dismiss stage. South v.  
21 Baker, 62 A.3d at 15 (citing “[a] claim that an audit committee or board had notice of serious  
22 misconduct and simply failed to investigate” as an example of a case that “would survive a motion  
23 to dismiss, even if the committee or board was well constituted and was otherwise functioning”)  
24 (quoting David B. Shaev Profit Sharing Account v. Armstrong, 2006 WL 391931, at \*5 (Del. Ch.  
25 Feb. 13, 2006)). “A board that fails to act in the face of such information makes a conscious  
26 decision, and the decision not to act is just as much of a decision as a decision to act.” Id. (citing  
27 Aronson, 473 A.2d at 813).

28 Defendants further argue that, if anything, these allegations would have led the Board to

1 conclude that Wells Fargo’s oversight system and controls were working as they were supposed  
2 to. For example, with respect to the Board’s apparent inaction in response to communications  
3 from and litigation involving current and former employees, Defendants argue that “[a] more  
4 appropriate inference is that the Board leaves individual ethics and related employment cases to  
5 management and counsel, who are equipped to handle those individual issues in a manner that the  
6 Board is not.” ECF No. 99 at 20. Regarding the Los Angeles Times article, Defendants argue that  
7 “the article indicates that management had detected and had dealt with [the problem] in the most  
8 serious way that a company can discipline employees: dismissal.” Id. at 21. Defendants place  
9 particular focus on the complaint’s allegation that, “in 2011, one group (the Sales and Service  
10 Conduct Oversight Team) ‘began to engage in proactive monitoring of data analytics, specifically  
11 for the purpose of rooting out sales practice violations’” and that those controls “identified  
12 simulated funding activity in the Los Angeles and Orange County markets, and terminated Wells  
13 Fargo employees for that conduct.” Id. at 19; ECF No. 83 ¶ 27. With respect to the employee  
14 terminations, Defendants similarly argue that the terminations “might well have communicated to  
15 the Directors that the controls in place were functioning properly and that the Company was taking  
16 misconduct seriously when it discovered it.” ECF No. 99 at 17-18.

17 This is one inference that could be drawn from the allegations. But at this stage of the  
18 litigation the Court must construe all reasonable inferences in Plaintiffs’ favor. See Brehm v.  
19 Eisner, 746 A.2d 244, 255 (Del. 2000) (“Plaintiffs are entitled to all reasonable factual inferences  
20 that logically flow from the particularized facts alleged . . .”); see also, e.g., Rosenbloom, 765 F.3d  
21 at 1153 (“Whereas Allergan argues that the Board could have viewed the increase in off-label  
22 Botox sales as the natural operation of the medical community, at this stage of the case we must  
23 make reasonable inferences for Plaintiffs, not against them – and it is reasonable to infer that the  
24 data repeatedly presented to Allergan’s board linking Allergan programs to fluctuations in off-  
25 label sales support a finding of scienter.”). And it is just as reasonable to infer from Plaintiffs’  
26 allegations as a whole that the Director Defendants knew that (1) unauthorized account-creation  
27 practices were not confined to a few employees and sufficiently dealt with on a one-off basis  
28 through termination, but rather a systemic issue that was rampant in branches across the country,

1 and (2) that the company’s oversight systems and controls for sales integrity issues were  
2 inadequate at detecting, preventing, and rooting out this problem. McCall v. Scott, 239 F.3d 808,  
3 821 (6th Cir.), amended on denial of reh’g, 250 F.3d 997 (6th Cir. 2001). In sum, by “focus[ing]  
4 on other hypothetical explanations for the [their] conduct,” the Defendants “improperly ignore[]  
5 the rule that any inferences reasonably drawn from the factual allegations of the complaint must be  
6 viewed in the light most favorable to the plaintiffs.” Westmoreland Cty. Employee Ret. Sys. v.  
7 Parkinson, 727 F.3d 719, 729 (7th Cir. 2013) (internal quotation marks and citations omitted).

8           Throughout their briefing, Defendants seem to suggest that the mere presence of control  
9 systems is sufficient on its own to satisfy the fiduciary duty to monitor. By way of example, this  
10 position is demonstrated in the following passage in Defendants’ motion:

11                           Even if the Wells Fargo Directors had been made aware of the  
12                           June 2015 letter containing MRAs, that correspondence would not  
13                           have communicated an utter lack of control systems. To be sure,  
14                           the June 2015 correspondence called upon Wells Fargo Bank, N.A.  
15                           to . . . “improv[e] processes.” But the instruction to ‘improve  
16                           processes’ presupposes processes.  
17           ECF No. 99 at 24 (emphasis added). But the Delaware Supreme Court has clearly explained that a  
18           director can be held liable for a failure to monitor even if control systems were in place. As that  
19           court explained in Stone, director oversight liability can result in one of two ways: “(a) the  
20           directors utterly failed to implement any reporting or information system or controls; or (b) having  
21           implemented such a system or controls, consciously failed to monitor or oversee its operations  
22           thus disabling themselves from being informed of risks or problems requiring their attention.”  
23           Stone, 911 A.2d at 370 (citing Guttman, 823 A.2d at 506) (emphasis in original). Given the  
24           court’s use of the disjunctive “or” in that sentence, Defendants’ singular focus on the presence of  
25           control systems is misplaced. In other words, a director cannot simply implement control systems,  
26           consciously fail to oversee its operations, and then claim to have satisfied its fiduciary duty to  
27           monitor.

28           The allegations in the complaint plausibly suggest that that is what occurred here. For  
          example, Plaintiffs allege that, despite multiple lawsuits brought by former employees related to  
          the unlawful account creation practices between 2008 and 2013, “[t]he only response . . . was to

1 include a new entry code on its EthicsLine ethics complaint forms for ‘gaming’ and ‘sales  
2 incentives,’ to track those specific types of complaints.” ECF No. 83. ¶ 219. But implementation  
3 of a reporting system is not sufficient on its own to preclude director oversight liability. As  
4 explained above, Stumpf admitted that the Board and several committees within the Board learned  
5 of an uptick in sales integrity issues, based partially on EthicsLine reporting, between the 2011 to  
6 2014 time period. But, despite having “knowledge that the company controls [were] inadequate,”  
7 the allegations plausibly suggest that the Director Defendants “knowingly failed to stop further  
8 problems from occurring,” thus breaching their fiduciary duties to the company. Rich ex rel. Fuqi  
9 Int'l, Inc. v. Yu Kwai Chong, 66 A.3d 963, 984 (Del. Ch. 2013) (“When faced with knowledge  
10 that the company controls are inadequate, the directors must act, i.e., they must prevent further  
11 wrongdoing from occurring.”). Where, as here, Plaintiffs allege that directors “failed to exercise  
12 reasonable oversight over pervasive fraudulent and criminal conduct,” the directors’ conscious  
13 inaction is not protected by the business judgment rule. In re Citigroup Inc. S'holder Derivative  
14 Litig., 964 A.2d 106, 130-131 (Del. Ch. 2009) (emphasis in original).

15 In sum, the abundance of particularized allegations in the Consolidated Amended  
16 Complaint support an inference that a majority of the Director Defendants – and in particular those  
17 Director Defendants who were on the risk committee, audit and examination committee, and  
18 corporate responsibility committee – knew about widespread illegal activity and consciously  
19 disregarded their fiduciary duties to oversee and monitor the company. As a result, they face a  
20 substantial likelihood of liability for Plaintiffs’ breach of fiduciary duty claims.

## 21 2. Section 14(a) Claims

22 The Director Defendants also face a substantial likelihood of liability on Plaintiffs’ claims  
23 under Section 14(a) of the Exchange Act and SEC Rule 14a-9.

24 Section 14(a) of the Securities Exchange Act makes it unlawful to solicit shareholder  
25 approval by use of a proxy statement that does not comply with the rules and regulations of the  
26 Securities Exchange Commission. 15 U.S.C. § 78n. In turn, regulation 14a-9 prohibits proxy  
27 statements that are false or misleading with regard to any material facts at the time they are issued  
28 and in light of the circumstances under which they are made. 17 C.F.R. § 240.14a-9.

1 Collectively, these provisions “disallow the solicitation of a proxy by a statement that contains  
2 either (1) a false or misleading declaration of material fact, or (2) an omission of material fact that  
3 makes any portion of the statement misleading.” Desaigouadar v. Meyercord, 223 F.3d 1020, 1022  
4 (9th Cir. 2000).

5 “[A] Section 14(a), Rule 14a–9 plaintiff must demonstrate that the misstatement or  
6 omission was made with the requisite level of culpability and that it was an essential link in the  
7 accomplishment of the proposed transaction.” Desaigouadar v. Meyercord, 223 F.3d 1020, 1022–  
8 23 (9th Cir. 2000). Where, as here, the claim “sounds in fraud,” both Federal Rule of Civil  
9 Procedure 9(b) and the heightened pleading standard of the Private Securities Litigation Reform  
10 Act (PSLRA) apply, and the plaintiff must “identify: (1) each statement alleged to have been  
11 misleading; (2) the reason or reasons why the statement is misleading; and (3) all facts on which  
12 that belief is formed.” Id.; In re Countrywide Fin. Corp. Derivative Litig., 554 F. Supp. 2d 1044,  
13 1076 (C.D. Cal. 2008).

14 As with the breach of fiduciary duty claims, “to establish a threat of director liability based  
15 on a disclosure violation, plaintiffs must plead facts that show that the violation was made  
16 knowingly or in bad faith.” In re Citigroup Inc. S’holder Derivative Litig., 964 A.2d 106, 133–34  
17 (Del. Ch. 2009).

18 Contrary to Defendants’ contention, Plaintiffs’ allegations meet the heightened pleading  
19 requirements of the PSLRA. See ECF No. 116 at 16, n. 13. Plaintiffs allege that “[t]he Director  
20 Defendants . . . caus[ed] Wells Fargo to issue proxy statements that failed to disclose the illicit  
21 account-creation scheme or the seriously deficient internal and disclosure controls that allowed the  
22 scheme to begin and helped perpetuate it.” ECF No. 83 ¶¶ 272-311. Specifically, Plaintiffs allege  
23 that the 2014, 2015, and 2016 Proxy Statements omitted several material facts, including  
24 disclosures regarding “ineffective internal and disclosure controls”; “reporting failures that failed  
25 to appropriately address rampant illegal sales practices and retaliatory terminations against those  
26 reporting improper account-creation practices”; “Board-approved compensation programs that  
27 incentivized fraudulent account openings for years”; and “known pending investigations by the  
28 U.S. Department of Justice (‘DOJ’), DOL, congressional committees, the SEC, California state

1 prosecutors, and attorneys general into the fraudulent account openings.” Id. ¶¶ 278, 290, 302. In  
2 addition, Plaintiffs allege that the Proxy Statements “omitted the fact that certain of the cross-  
3 selling metrics reported by Defendants were based on false, illegally-generated cross-sell  
4 numbers.” Id. ¶¶ 284, 296. Plaintiffs also explain in detail why the proxy statements were  
5 misleading – for example, the disclosures “suggested that Wells Fargo’s strong financial  
6 performance was attributable to a purportedly effective governance structure, while improperly  
7 omitting that such financial performance stemmed, in material part, from the illicit account-  
8 creation scheme.” Id. ¶¶ 310, 281, 293, 296. In addition, Plaintiffs identify specific statements in  
9 the proxy statements that they allege are affirmatively false and misleading. Id. ¶¶ 272-311.  
10 Absent these false or misleading statements and omissions in the Proxy Statements, Plaintiffs  
11 contend that shareholders would not have voted to re-elect Board members, approve executive  
12 compensation packages (including approval of an incentive compensation award for Officer  
13 Defendant Tolstedt based on “record cross-sell and deposit levels”), and reject an independent  
14 Board chairman. Id. ¶¶ 116-22, 273-311.<sup>12</sup>

15 In light of the extensive and detailed allegations suggesting that the Director Defendants  
16 knew about the illegal account-creation scheme by 2014 at the latest, the Court can also  
17 reasonably infer that the Director Defendants knew that these disclosures were false or misleading  
18 at the time they were issued. Therefore, Plaintiffs have adequately alleged scienter on the part of  
19 the Director Defendants for the reasons already discussed.

20 Defendants argue that the complaint does not allege sufficient Board involvement in the  
21 preparation of the disclosures such that the Director Defendants face a substantial likelihood of  
22 liability. ECF No. 116 at 15. To the contrary, Plaintiffs allege that “Defendants Stumpf, Baker,  
23 Chao, Chen, Dean, Engel, Hernandez, James, Milligan, Peña, Quigley, Runstad, and Sanger  
24 caused Wells Fargo to file the 2014 Proxy Statement in connection with the 2014 annual

25 \_\_\_\_\_  
26 <sup>12</sup> Defendants do not argue that these allegedly false or misleading disclosures would have been  
27 immaterial to a reasonable investor. In any event, it is clear that “[s]hareholders would reasonably  
28 consider the Company’s financial performance in deciding whether to reelect the directors” and  
“would be interested in knowing whether the directors would use deceptive methods to achieve the  
performance measures that were the benchmarks of the . . . compensation plans.” Countrywide,  
554 F. Supp. 2d at 1077.

1 stockholders meeting to be held on April 29, 2014.” ECF No. 83 ¶ 273. Because all but Runstad  
 2 were on the Board at the time the first complaint was filed, the allegations in the complaint  
 3 suggest that a majority of the Director Defendants knowingly participated in the issuance of the  
 4 allegedly false or misleading disclosures. ECF No. 83 ¶ 91. Plaintiffs similarly allege with  
 5 particularity that the Director Defendants were involved in the preparation of the 2015 and 2016  
 6 Proxy Statements. Id. ¶¶ 286, 298.

7 The Court therefore concludes that the Director Defendants face a substantial likelihood of  
 8 liability on Plaintiffs’ claims under Section 14(a) of the Exchange Act.<sup>13</sup>

9 **3. Section 10(b) Claims**

10 “A § 10(b) claim requires the following elements: (1) a material misrepresentation or  
 11 omission; (2) scienter; (3) reliance; (4) economic loss; and (5) loss causation, which is ‘a causal  
 12 connection between the material misrepresentation and the loss.’” Countrywide, 554 F. Supp. 2d  
 13 at 1057 (quoting Dura Pharm. v. Broudo, 544 U.S. 336, 341–42 (2005)); 15 U.S.C. § 78u–  
 14 4(b)(4)).

15 Plaintiffs allege that the Defendants violated Section 10(b) by “caus[ing] the Company to  
 16 issue statements that, in light of the illicit account-creation scheme detailed above, were materially  
 17 false or misleading when made.” ECF No. 83 ¶ 312. In turn, Plaintiffs allege that these  
 18 statements “artificially inflated the price of Wells Fargo’s shares, causing the Company to  
 19 purchase shares at artificially inflated prices, through its significant stock repurchase program.”  
 20 Id. Plaintiffs allege that the stock repurchase program “signaled to investors . . . that Wells Fargo  
 21 shares were trading at a discount, which caused investors to purchase shares and thereby drive the  
 22 price up.” Id. ¶ 313. In addition, “the Company’s repurchasing of shares artificially inflated its  
 23 financial metrics such as earnings per share, as the repurchases resulted in fewer outstanding  
 24

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25 <sup>13</sup> Based on this alleged misconduct, the Director Defendants also face a substantial likelihood of  
 26 liability for breach of their fiduciary duty of loyalty, which “requires honesty from corporate  
 27 directors in their communications with the public and shareholders about corporate matters.”  
 28 Pirelli Armstrong Tire Corp. Retiree Med. Benefits Trust v. Stumpf, No. C 11-2369 SI, 2012 WL  
 424557, at \*6-\*7 (N.D. Cal. Feb. 9, 2012) (holding that director defendants faced a substantial  
 likelihood of liability for breach of their duty of loyalty by omitting material information in a  
 proxy statement).

1 shares.” Id. “The artificial inflation of Wells Fargo shares was both financially beneficial to  
2 Defendants, as numerous Defendants’ compensation was tied to the Company’s financial  
3 performance, and helped mask the illicit account-creation scheme (and thus helped perpetuate it).”  
4 Id. Moreover, “as a result of the artificial inflation of the price of Wells Fargo shares, the Insider  
5 Selling Defendants sold shares at higher prices, and in some instances sold them to the Company –  
6 and thus reaped greater proceeds – than they would have absent the artificial inflation.” Id.

7 Defendants’ argue that the directors do not face a substantial likelihood of liability under  
8 Section 10(b) because Plaintiffs have failed to allege scienter and reliance. ECF No. 99 at 27;  
9 ECF No. 116 at 16-17.

10 The Court has already concluded that the allegations in the complaint create a strong  
11 inference of scienter on the part of a majority of the Director Defendants, particularly the twelve  
12 Director Defendants who were members of the risk committee, the audit and examination  
13 committee, and the corporate responsibility committee. For the same reasons, the Court concludes  
14 that the Plaintiffs have successfully pleaded facts giving rise to a strong inference of scienter for  
15 purposes of their 10(b) claims. Countrywide, 554 F. Supp. 2d at 1056 (applying a “scienter-based  
16 standard” to Plaintiffs’ 10(b) claims and Plaintiffs’ Caremark claims).

17 With respect to reliance, Defendants argue that “Wells Fargo could never plead or prove,  
18 as it would have to, that it had reasonably relied on either its own misstatements or on the market  
19 price that reflected those misstatements given that the knowledge of the people who allegedly  
20 knowingly made those misstatements *is Wells Fargo’s knowledge*.” ECF No. 99 at 27 (emphasis  
21 in original). In other words, Defendants argue that the Director Defendants and Wells Fargo are  
22 one and the same, and therefore Wells Fargo could not possibly rely on misstatements that the  
23 Director Defendants knowingly made. Defendants contend that this “is merely the logical  
24 application of the long-standing corporate law proposition that corporations operate through their  
25 senior officers, whose knowledge is the corporation’s knowledge.” ECF No. 116 at 16. To  
26 support this argument, Defendants rely on In re Verisign, Inc. Deriv. Litig., 531 F. Supp. 2d 1173,  
27 1209 (N.D. Cal. 2007).

28 In Verisign, the plaintiffs similarly alleged that the director defendants made false or

1 misleading statements that “artificially inflated the value of VeriSign’s stock” and then caused  
2 VeriSign to repurchase its own stock at those inflated prices. VeriSign, 531 F. Supp. 2d at 1203.  
3 The court held that plaintiffs could not plead reliance under such a theory because the corporate  
4 decision-maker for the repurchase of shares also had knowledge of the alleged fraud. See id. at  
5 1209.

6           However, several courts have rejected VeriSign’s reasoning as flawed, and have  
7 accordingly declined to follow it. See In re Finisar Corp. Derivative Litig., No. C-06-07660  
8 RMW, 2012 WL 2873844, at \*17 (N.D. Cal. July 12, 2012); In re Fossil, Inc., 713 F. Supp. 2d  
9 644, 654 (N.D. Tex. 2010); Countrywide, 554 F. Supp. 2d at 1073. For example, another court in  
10 this district concluded that “the Verisign court ‘extended too far the legal fiction that the company  
11 is the same as its leadership.’” Finisar, 2012 WL 2873844, at \*17 (quoting In re Fossil, Inc., 713  
12 F.Supp.2d at 653). The Finisar court further explained that, “if Finisar issues or purchases stock at  
13 a loss, it does not do so recklessly – it is a puppet whose strings are pulled by the very directors  
14 and officers responsible for the fraud.” Id. Courts have also noted that VeriSign’s holding leads  
15 to an absurd result: “[I]t requires dismissal of a fraud claim where all of the directors are in on the  
16 scheme, but allows the claim to proceed if the corruption is less widespread.” Id. (emphasis in  
17 original); see also Fossil, 713 F. Supp 2d at 654 (“This Court declines to hold that in order to  
18 sufficiently plead reliance a derivative plaintiff must allege that some directors or officers acted  
19 with the alleged scienter and material misrepresentations but that some did not and that the  
20 company’s justifiable reliance on its Board exists only because of those who did not take part in  
21 the alleged fraud.”).

22           Moreover, the only authority upon which the VeriSign court relied in reaching its  
23 conclusion – the Ninth Circuit’s decision in Atari Corp. v. Ernst & Whinney, 981 F.2d 1025 (9th  
24 Cir. 1992) – was entirely inapplicable because Atari was not a derivative action and therefore did  
25 not involve allegations brought by a company against its own directors. See Atari, 981 F.2d at  
26 1027 (describing securities fraud claims brought by one company against the auditors and officers  
27 of another company with which the first company had entered into a merger); Fossil, 713 F. Supp.  
28 2d at 653 (“The key distinction between the statement in Atari and the allegations in this case and

1 Verisign is that Plaintiffs here allege that certain directors and officers misled the company, and  
2 Plaintiffs bring their claim derivatively on the company's behalf.”).

3 Defendants argue that the courts that have declined to follow VeriSign improperly relied,  
4 either directly or indirectly, on the Second Circuit’s decision in Ruckle v. Roto Am. Corp., 339  
5 F.3d 24 (2d Cir. 1964). ECF No. 116 at 17. Defendants contend that Ruckle is no longer good  
6 law because it was overruled in O’Neill v. Maytag, 339 F.2d 764. Id. Defendants are wrong.  
7 Although a Second Circuit panel declined to follow Ruckle a month after that decision was issued  
8 in 1964, the Second Circuit explained more than a decade later that “[t]he future, both in this  
9 circuit and in others, lay with the Ruckle dictum rather than with O’Neill.” Goldberg v. Meridor,  
10 567 F.2d 209, 215 (2d Cir. 1977) (explaining that the Second Circuit’s decision in Schoenbaum  
11 “effectively overrul[ed] any requirement of O’Neill that there must be one virtuous or ignorant  
12 lamb among the directors in order for liability to arise under s 10(b) . . .”).

13 The Court respectfully disagrees with the reasoning in VeriSign because it “exalts form  
14 over substance” and “restricts the application of [10(b) liability] in a way which is at odds with its  
15 basic purpose.” Pappas v. Moss, 393 F.2d 865, 869 (3d Cir. 1968). As the Second Circuit  
16 explained in Goldberg v. Meridor:

17 If . . . the board defrauded the corporation into issuing shares either  
18 to its members or others, we can think of no reason to say that  
19 redress under Rule 10B-5 is precluded, though it would have been  
20 available had anyone else committed the fraud. There can be no  
21 more effective way to emasculate the policies of the federal  
22 securities laws than to deny relief solely because a fraud was  
23 committed by a director rather than by an outsider. Denial of relief  
24 on this basis would surely undercut the congressional  
25 determination to prevent the public distribution of worthless  
26 securities.

23 567 F.2d 209, 215 (2d Cir. 1977). Here, Plaintiffs allege that, “[h]ad Wells Fargo known of the  
24 material adverse information not disclosed by Defendants, or been aware of the truth behind  
25 Defendants’ material misstatements, the Company would not have repurchased Wells Fargo stock  
26 at artificially inflated prices.” ECF No. 83 ¶ 401. They have sufficiently alleged reliance for  
27 purposes of their 10(b) claims.  
28

1           Therefore, the Director Defendants face a substantial likelihood of liability as to Plaintiffs’  
2 Section 10(b) claims.

3                           **4.       Remaining Claims**

4           Defendants argue that Plaintiffs’ remaining causes of action for unjust enrichment,  
5 corporate waste, and mismanagement do not independently give rise to a substantial likelihood of  
6 Director liability because they are merely duplicative of the breach of fiduciary duty claims. ECF  
7 No. 98 at 16, n. 8. Defendants further argue that “Plaintiffs come nowhere near pleading waste”  
8 and that the Directors do not face a substantial likelihood of liability under California  
9 Corporations Code § 24503 because there is no private right of action under that statute. ECF No.  
10 99 at 27.

11                           **a.       Unjust Enrichment**

12           Because Plaintiffs’ claim for unjust enrichment rests on the same theory as the claim for  
13 breach of fiduciary duty, the Court concludes that Defendants also face a substantial likelihood of  
14 liability as to that claim for the same reasons. See MCG Capital Corp. v. Maginn, No. CIV.A.  
15 4521-CC, 2010 WL 1782271, at \*25, n. 147 (Del. Ch. May 5, 2010) (“If [plaintiff] is able prove  
16 [defendant] breached his duty of loyalty in Count Five then it will also be successful in proving  
17 unjust enrichment in Count Six.”); Jackson Nat. Life Ins. Co. v. Kennedy, 741 A.2d 377, 394 (Del.  
18 Ch. 1999) (same). Where, as here, the plaintiff’s theory of liability for unjust enrichment is the  
19 same as the theory for breach of fiduciary duty, such that “the unjust enrichment claim depends  
20 per force on the breach of fiduciary duty claim,” courts often “treat [those claims] in the same  
21 manner when resolving a motion to dismiss.” Frank v. Elgamal, No. CIV.A 6120-VCN, 2014 WL  
22 957550, at \*31 (Del. Ch. Mar. 10, 2014), order enforced, (Del. Ch. Mar. 14, 2014).

23           To the extent Defendants argue that the unjust enrichment claim should be dismissed as  
24 duplicative at this stage in the litigation, they are wrong. Although courts have dismissed  
25 redundant claims at the summary judgment stage because the plaintiff is only entitled to one  
26 recovery, they have noted “that, assuming there is a reasonably conceivable basis for both claims,  
27 the plaintiff is entitled to discovery on them.” Id. at \*32. In sum, “there is no bar to bringing both  
28 claims against a director,” and “it is not at all clear that the Court, on a motion to dismiss, should

1 reject an equitable claim on the basis that it is duplicative of another equitable claim.” Dubroff v.  
2 Wren Holdings, LLC, No. CIV.A. 3940-VCN, 2011 WL 5137175, at \*15, n. 58 (Del. Ch. Oct. 28,  
3 2011) (quoting MCG Capital Corp., 2010 WL 1782271 at \*25, n. 147).

4 **b. Corporate Waste**

5 Plaintiffs allege that, “[b]y approving the stock repurchase program, the Director  
6 Defendants . . . caused Wells Fargo to waste its corporate assets on the repurchase of stock at  
7 artificially inflated prices.” ECF No. 83 ¶ 591.

8 Faced with allegations similar to those raised in this Complaint, the Countrywide court  
9 held that plaintiffs had adequately pleaded a corporate waste claim based on a stock repurchase  
10 program, and that demand was accordingly excused as futile with respect to that claim.  
11 Countrywide, 554 F. Supp. 2d at 1078, 1082–83. The plaintiffs in Countrywide similarly alleged  
12 that the director defendants caused the company to repurchase common stock during the relevant  
13 time period, thus signaling to the market that the Board thought the shares were underpriced, while  
14 simultaneously selling their own personal shares. Id. at 1066–67. The court concluded that “the  
15 repurchase program could properly be viewed as an attempt to keep the ball rolling – i.e. to propel  
16 the Company forward (steady the stock price, or sending it upward) for a period of time before  
17 the weight of the loan origination practices began taking its toll on the Company’s operations and  
18 the value of its stock.” Id. at 1068. Since the allegations in the complaint created “a strong  
19 inference of scienter” on behalf of several of the director defendants, “it follow[ed] that Plaintiffs  
20 have stated a claim that the repurchase is not subject to protection by the business judgment rule  
21 because . . . it may have served to delay the eventual impairment caused by unsound business  
22 practices.” Id. at 1078. In other words, the court’s prior finding of scienter provided “reason to  
23 doubt that the stock repurchase program . . . was the product of the Board’s ‘valid exercise of  
24 business judgment,’” and therefore demand was futile. Id. at 1082–83.

25 The same is true here. Because Plaintiffs have alleged particularized facts that create a  
26 reasonable doubt as to whether the stock repurchase program was the product of a valid exercise  
27 of business judgment, demand is excused as futile with respect to Plaintiffs’ corporate waste claim  
28 challenging that transaction. Silicon Graphics, 183 F.3d at 990.

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**c. Mismanagement**

Contrary to Defendants’ assertion, the complaint does not state a separate cause of action for “mismanagement.” ECF No. 99 at 16, n. 8. Rather, the complaint acknowledges that “Delaware law does not recognize an independent cause of action against corporate directors or officers for gross mismanagement or abuse of control,” and states that “Plaintiffs’ claims for breach of fiduciary duty include abuse of control and gross mismanagement.” ECF No. 83 ¶ 244.

**d. California Corporations Code Section 25403**

There is no private right of action under California Corporations Code Section 25403. Apollo Capital Fund, LLC v. Roth Capital Partners, LLC, 158 Cal. App. 4th 226, 233, 255 (2007) (“[T]he civil liability provisions of [Section 25403] do not expressly provide a private right of action for a violation of section 25403, as they do for other specified provisions of the Act.”). As a result, Defendants do not face a substantial likelihood of liability for that claim.

Plaintiffs’ only response is that “the California Supreme Court has yet to resolve whether Section 25403 of the California Corporations Code affords a private right of action . . .” ECF No. 115 at 30, n. 15. While that may be true, “[a] state appellate court’s announcement of a rule of law is a datum for ascertaining state law which is not to be disregarded by a federal court unless it is convinced by other persuasive data that the highest court of the state would decide otherwise.” Miller v. Cty. of Santa Cruz, 39 F.3d 1030, 1036, n. 5 (9th Cir. 1994), as amended (Dec. 27, 1994) (internal quotation marks omitted). Plaintiffs have failed to point to any such data here.

The Court therefore dismisses Count IX of the Consolidated Amended Complaint.

**e. Exchange Act Section 29(b)**

Defendants argue that “Count VII, which seeks injunctive relief or rescission of Defendants’ contracts under Section 29(b) as a means to ensure that any clawback of compensation is unencumbered, is entirely derivative of the breach of duty and Securities Exchange Act claims – Directors face no independent liability pursuant to this cause of action.” ECF No. 99 at 28, n. 16.

Defendants are correct that “Section 29(b) itself does not define a substantive violation of the securities laws; rather, it is the vehicle through which private parties may rescind contracts that

1 were made or performed in violation of other substantive provisions.” In re Asyst Techs., Inc.  
2 Derivative Litig., No. C-06-04669 EDL, 2008 WL 4891220, at \*9 (N.D. Cal. Nov. 12, 2008)  
3 (quoting Berkeley Inv. Group Ltd v. Colkitt, 455 F.3d 195, 205 (3d Cir. 2006)). However, for  
4 the reasons stated above, Plaintiffs have already demonstrated that the Director Defendants face a  
5 substantial likelihood of liability for both the breach of fiduciary duty and Securities Exchange  
6 Act claims. And Defendants do not otherwise argue that Plaintiffs have failed to state a claim  
7 under Section 29(b).

8 Therefore, the Court denies the motion to dismiss Count VII.

9 **CONCLUSION**

10 The particularized factual allegations in the Consolidated Amended Complaint create a  
11 reasonable doubt as to whether a majority of the Director Defendants face a substantial likelihood  
12 of personal liability for Plaintiffs’ breach of fiduciary duty, securities, and derivative claims. The  
13 allegations also create a reasonable doubt as to whether the stock repurchase program was the  
14 product of a valid exercise of business judgment. Therefore, the Court concludes that demand is  
15 excused as futile, and accordingly denies Defendants motion to dismiss on that ground. However,  
16 the Court grants Defendants’ motion to dismiss Count IX of the Consolidated Amended  
17 Complaint because there is no private right of action under California Corporations Code Section  
18 25403.

19 IT IS SO ORDERED.

20 Dated: May 4, 2017

21   
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23 JON S. TIGAR  
24 United States District Judge  
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