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IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF CALIFORNIA

SAN JOSE DIVISION

JAMES M. KELLEY, MIKI LARSSON, and DOUGLAS B. KELLEY, Plaintiffs, v. RAMBUS, INC., PRICEWATERHOUSE COOPERS, LLP, GEOFFREY TATE, DAVID MOORING, PAUL MICHAEL FARMWALD, BRUCE S. DUNLEVIE, WILLIAM DAVIDOW, and ROBERT EULAU, Defendants.	Case Number C 07-1238 JF (HRL) **ORDER[1] GRANTING MOTIONS TO DISMISS** Re: Docket Nos. 209, 210, 214, 215 & 219

I. BACKGROUND

In this consolidated action for violations of sections 14(a) and 18(a) of the Securities and Exchange Act of 1934 ("Exchange Act"), Plaintiffs James Kelley, Douglas Kelley, and Miki Larsson ("Plaintiffs") allege that Rambus, Inc., through a number of its current and former

[1] This disposition is not designated for publication in the official reports.

directors and officers ("Defendants"), engaged in and concealed an extensive pattern of options backdating. The original complaint, filed by James Kelley and Larsson on March 1, 2007, contained additional claims under federal securities laws and under California and Delaware law. James Kelley and Larsson subsequently filed three amended complaints, and Plaintiff Douglas Kelley filed a separate complaint on May 8, 2007, which he later amended. After the Court consolidated the cases on June 25, 2007, Plaintiffs filed a 295-page complaint that the Court dismissed for non-compliance with Federal Rule of Civil Procedure 8(a). With leave of Court, Plaintiffs filed an amended complaint on November 13, 2007, alleging violations of sections 10(b), 14(a), 18(a), and 20(a) of the Securities and Exchange Act of 1934 ("Exchange Act"), as well as common law fraud. Defendants subsequently filed motions to dismiss the amended complaint. On April 17, 2008, the Court granted the motions and granted Plaintiffs further leave to amend, but only as to their claims under sections 14 and 18 of the Exchange Act ("April 17, 2008 Order"). On May 15, 2008, Plaintiffs filed a pleading that restated allegations previously dismissed with prejudice in the April 17, 2008 Order. The Court accordingly struck the entire pleading by minute order on May 16, 2008. Plaintiffs then filed their Second (Revised) Consolidated Amended Complaint ("SRCAC"), which is now before the Court.

The remaining § 14 and § 18 claims stem from Defendants' alleged failure to disclose options backdating, allegedly occurring from 1997 through at least 2003, in the company's 2005 and 2006 proxy statements and in its 2005 10-K.[2] Plaintiffs allege that Rambus, current directors P. Michael Farmwald ("Farmwald"), William Davidow ("Davidow"), and Bruce Dunlevie ("Dunlevie"), and outside auditor PricewaterhouseCoopers ("PwC"), are responsible for the issuance of materially false proxy statements, in violation of § 14(a). Plaintiffs also allege that these same defendants, as well as former CFO Robert Eulau, former CEO Geoff Tate, and former president and director David Mooring made material misstatements or omissions in

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[2] Plaintiffs refer intermittently to Rambus's 2004 10-K, but the Court already has determined that claims arising from this statement, filed on February 13, 2004, are barred by the applicable three-year statute of repose. *See* April 17, 2008 Order at 8. Plaintiffs also refer to the 2004 proxy statement, but they make no attempt to plead reliance on any but the 2005 and 2006 proxy statements. *See* SRCAC ¶¶ 117-124.

documents filed with the SEC, in violation of § 18.

Defendants move to dismiss the complaint for failure to state a claim upon which relief may be granted. After a thorough review of Plaintiffs' voluminous pleadings and supporting documents, the Court agrees with Defendants that Plaintiffs have not stated a claim under sections 14(a) or 18(a). The Court also is convinced that there is no realistic possibility that Plaintiffs could cure the deficiencies in their § 14 claim. Finally, while there may be at least a theoretical possibility that Plaintiffs could state a viable § 18 claim, the Court is satisfied that in light of Plaintiffs' repeated failure to address identified deficiencies in their pleadings, the numerous inconsistencies in the allegations they do offer, and the continuing prejudice to Defendants, leave to amend that claim should be denied as well.

II. APPLICABLE LEGAL STANDARDS

A. Dismissal under Federal Rule of Civil Procedure 12(b)(6)

A complaint may be dismissed for failure to state a claim upon which relief may be granted for one of two reasons: (1) lack of a cognizable legal theory; or (2) insufficient facts under a cognizable legal theory. *Robertson v. Dean Witter Reynolds, Inc.*, 749 F.2d 530, 533-34 (9th Cir. 1984). For purposes of a motion to dismiss, all allegations of material fact in the complaint are taken as true and construed in the light most favorable to the nonmoving party. *Clegg v. Cult Awareness Network*, 18 F.3d 752, 754 (9th Cir. 1994). A complaint should not be dismissed "unless it appears beyond doubt the plaintiff can prove no set of facts in support of his claim that would entitle him to relief." *Clegg*, 18 F.3d at 754. However, a plaintiff is required to provide "more than labels and conclusions," *Bell Atl. Corp. v. Twombly*, __ U.S. __, 127 S.Ct. 1955, 1964 (2007), and the "[f]actual allegations must be enough to raise a right to relief above the speculative level." *Id*. at 1965.

B. Allegations of Fraud under Federal Rule of Civil Procedure 9(b)

Defendants argue that the entirety of Plaintiffs' complaint is subject to Federal Rule of Civil Procedure 9(b), which requires that claims sounding in fraud be pled with particularity. Plaintiffs contend that, except as to their concededly fraud-based § 18(a) claim against PwC, the applicable pleading standard is set forth in Rule 8(a)–requiring only a "short and plain statement" of the claim–as neither § 14 nor § 18 requires a showing of fraud. The Ninth Circuit has held that "in a case where fraud is not an essential element of a claim, only allegations ('averments') of fraudulent conduct must satisfy the heightened pleading requirements of Rule 9(b). Allegations of non-fraudulent conduct need satisfy only the ordinary notice pleading standards of Rule 8(a)." *Vess v. Ciba-Geigy Corp. USA*, 317 F.3d 1097, 1104-05 (9th Cir. 2003). Accordingly, unless the plaintiff alleges a "unified course of fraudulent conduct," such that the entire claim is "grounded in fraud," only the allegations of fraud must be pled with particularity. *Id*. at 1103-04. Where a plaintiff does allege a unified course of fraudulent conduct, the Court "is not required to sift through allegations of fraud in search of some 'lesser included' claim"–for example, one sounding in negligence. *In re Daou Systems, Inc.*, 411 F.3d 1006, 1028 (9th Cir. 2005). However, "[w]here averments of fraud are made in a claim in which fraud is not an element, an inadequate averment of fraud does not mean that no claim has been stated. The proper route is to disregard averments of fraud not meeting Rule 9(b)'s standard and then ask whether a claim has been stated." *Id*. at 1105 (quoting *Lone Star Ladies Inv. Club v. Schlotzsky's Inc.*, 238 F.3d 363, 368 (5th Cir.2001)).

In light of the above standards, the Court must determine the applicability of Rule 9(b) by examining the actual substance of the pleadings, *see Vess*, 317 F.3d at 1103-05; *Desaigoudar v. Meyercord,* 223 F.3d 1020, 1022-23 (9th Cir. 2000), notwithstanding Plaintiffs' purported "disavow[al of] any allegations of fraud," SRCAC ¶¶ 148, 165. In this instance, Plaintiffs' allegations as to all defendants, and as to both of their remaining claims, are replete with language associated with fraud. *See, e.g.*, SRCAC ¶¶ 29, 34, 39, 40, 67.[3] Plaintiffs have

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[3] The relevant allegations are as follows: SRCAC ¶ 29 ("[T]he board of directors disguised the return of backdated options to Mr. Tate."), ¶ 34 ("The Company, with the knowledge, approval, and participation of each of the Rambus Defendants, disseminated its false financial statements in, *inter alia*, the *audited* Form 10-K filings . . . "), ¶ 39 ("The Human Resources Department . . . , at the behest of the Stock Options Committee, forged the Stock Option Committee Memoranda to conceal the backdating as admitted by Rambus. At other times, Tate (the sole member of that Committee) falsified the Stock Option Committee Memoranda to conceal the backdating."), ¶ 40 ("For the remaining instances of falsification, the Compensation Committee prepared the falsified grant documents. . . . The Compensation

"incorporated, indiscriminately, all their allegations of fraud into the claims." *In re Enron Corp. Sec., Deriv. & ERISA Litig.*, 540 F. Supp. 2d 800, 827 (S.D. Tex. 2007); SRCAC ¶¶ 148 & 165 (incorporating all allegations, including allegations of fraud, into the claims). Plaintiffs thus have alleged the "continuous course of fraudulent conduct" contemplated in *Vess*, and their entire complaint must comport with Rule 9(b). *Vess*, 317 F.3d at 1103-05. Consistent with *Vess*, even if certain allegations fail the Rule 9(b) standard, the Court also must assess whether the remaining allegations state a claim under § 14 or § 18, neither of which requires a showing of fraud. *Id*.

C. The Private Securities Litigation Reform Act ("PSLRA")

Plaintiffs also must comply with the requirement of the PSLRA that the complaint "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2); *Desaigoudar*, 223 F.3d at 1023 (applying PSLRA pleading standards to section 14(a) claims); *In re Verisign, Inc., Derivative Litig.*, 531 F. Supp. 2d 1173, 1202-1203 (N.D. Cal. 2007) (same); *In re Zoran Corp. Derivative Litigation*, 511 F. Supp. 2d 986, 1015 (N.D. Cal. 2007) (same); *see also Deephaven Private Placement Trading Ltd, v. Grant Thornton & Co.*, 454 F.3d 1168, 1172 (10th Cir. 2006) (applying PSLRA to § 18(a) claims); *In re Stone & Webster, Inc., Securities Litigation*, 414 F.3d 187, 194 (1st Cir. 2005) (same). Under the PSLRA, "[i]t is not sufficient for a plaintiff's pleadings to set forth a belief that certain unspecified sources will reveal, after appropriate discovery, facts that will validate her claim." *South Ferry LP, No. 2 v. Killinger*, __ F.3d __, 2008 WL 4138237, at *4 (9th Cir. 2008) (quoting *Silicon Graphics*, 183 F.3d 970, 985 (9th Cir. 1999)).[4]

Committee at that time was comprised of Davidow, Dunlevie, Geschke, and later Farmwald. . . "), ¶ 67 ("Davidow, Dunlevie, and Geschke also controlled the Audit Committee and had to meet with PwC and prepare the 10-K annual report. The October 16 backdated option grants . . . were intentionally and falsely put into the annual report for the fiscal year ending September 30, 2001.")

[4] In light of the Supreme Court's decision in *Tellabs, Inc. v. Makor Issues and Rights, Ltd.*, __ U.S. __, 127 S.Ct. 2499, 2510 (2007), the Ninth Circuit in *Killinger* revisited several prior holdings interpreting the PSLRA, but it did not purport to alter this aspect of the pleading standard articulated in *Silicon Graphics*.

The required state of mind for § 14 claims is negligence. *Verisign,* 531 F. Supp. 2d at 1211. Section 18, while requiring "something more than negligence," *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 211 n.31 (1976); *In re Fed. Nat'l Mortg. Ass'n Sec., Deriv., and ERISA Litig.*, 503 F. Supp. 2d 25, 44 (D.D.C. 2007), gives Defendants the burden of showing that they acted "in good faith and had no knowledge that [a] statement was false or misleading," and Plaintiffs initially are required to plead no more than facts giving rise to a strong inference of negligence. *See, e.g.*, *Magna Inv. Corp. v. John Does One Through Two Hundred*, 931 F.2d 38, 39-40 (11th Cir. 1991) (holding that § 18 Plaintiff need only plead negligence, and that Defendants must raise "good faith" as an affirmative defense); *In re Alstom* SA, 406 F. Supp. 2d 402, 420 (S.D.N.Y. 2005) ("[I]t is not the plaintiff's burden to anticipate and plead in his complaint a rebuttal to the defendant's potential defense [of good faith]."); *see also Howard v. Everex Sys., Inc.*, 228 F.3d 1057, 1065 (9th Cir. 2000) (noting, under similar § 20 provision, that "[p]laintiff need not show that the defendant was a culpable participant in the violation, but defendant may assert a 'good faith' defense").

III. DISCUSSION

A. Section 14(a) Claims

To state a claim under §14(a) of the Exchange Act, a plaintiff must show that (1) the defendant made a material misrepresentation or omission in a proxy statement, (2) the misrepresentation or omission was made with the requisite level of culpability, and (3) the misrepresentation or omission was an essential link in the accomplishment of a transaction proposed in the proxy solicitation. *Desaigoudar*, 223 F.3d at 1022. Each of these requirements–and the "essential link" requirement in particular–reflects the purpose of section 14(a), which is to prevent corporate management "from obtaining authorization for corporate action by means of deceptive or inadequate disclosure of proxy solicitation." *J.I. Case Co. V. Borak*, 277 U.S. 426, 431 (1964).[5]

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[5] As an initial matter, there remain substantial questions as to whether Plaintiffs can maintain their § 14 claim as a direct action. In dismissing Plaintiffs' § 14 claim, the Court previously noted that the claim as pled appeared derivative rather than direct. April 17, 2008

1. Material misstatements or omissions

Although Plaintiffs' allegations are at times difficult to follow, the SRCAC appears to allege four material misstatements or omissions with respect to Rambus and the director and officer defendants. First, Rambus is alleged to have represented falsely in its 2005 and 2006 proxy statements that "[u]nless otherwise indicated, options were granted at an exercise price equal to the fair market value of the Company's Common Stock at the date of grant." SRCAC ¶¶ 30, 53. The 2006 proxy statement, however, simply does not contain such a representation, and therefore cannot support Plaintiffs' claims. While the representation does appear in the 2005 proxy statement, it refers exclusively to grants made in 2004. Defendants contend that the SRCAC cannot be read to challenge any backdating after 2003, and that a representation concerning options grant procedures in 2004 thus is irrelevant. The SRCAC, however, does contain scattered allegations of backdating in 2004. *See* SRCAC ¶ 38 ("This new hire backdating continued into December 2004."), ¶ 53 (noting unspecified backdated grants in December 2004); *id.* at 181, Ex. C-3 (containing a chart purportedly summarizing options backdated through October 12, 2004). Plaintiffs noted at oral argument that Rambus admitted to such backdating in the September 14, 2007 restatement of its 2006 10-K, albeit without identifying the grantees or any other details. Plaintiffs contend that without discovery they cannot yet determine whether the backdated options were granted to any of the named defendants. Transcript at 3:9-5:15. However, as noted above, a plaintiff may not merely "set forth a belief that certain unspecified sources will reveal, after appropriate discovery, facts that will validate her claim," *South Ferry LP, No. 2 v. Killinger*, __ F.3d __, 2008 WL 4138237, at

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Order at 7:13-26. To maintain a direct claim, a stockholder must allege that he suffered an injury separate and distinct from any harm suffered by the corporation, and that he, not the corporation, would receive the benefit of a remedy. *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1035 (Del. 2004). Plaintiffs' Opposition (Doc. No. 242, at 5:13-19) appears to place exclusive reliance on the theory–not contained in any pleading–that the section 14(a) claim is direct because the 2006 proxy statement sought and won ratification of the 2006 Equity Incentive Plan and Employee Stock Plan, which proposed to authorize an additional 10% dilution of Rambus capital stock. But it is well established that equity dilution "does not generally constitute a direct harm, but a derivative one." *Oliver v. Boston Univ.*, 2006 WL 1064169, at *16 (Del. Ch. Apr. 14, 2006).

*4 (9th Cir. 2008).[6]

Second, Plaintiffs allege that Rambus falsely represented in its 2005 and 2006 proxy statements that its "1997 Stock Plan ha[d] been . . . administered to meet [the] requirement[s]" of § 162(m). SRCAC ¶ 53. Although Plaintiffs' pleadings once again are not entirely clear, it appears that Defendants' alleged non-compliance with § 162(m) flowed from both (1) an alleged conflict of interest arising from Farmwald's simultaneous service on the Compensation Committee and as a director; and (2) the backdating itself, since 162(m) prescribes rules for the deductibility of compensation. Neither of these statements comports with the particularity requirements of the PSLRA. Farmwald was not a member of the Compensation Committee in 2004 or 2005, SRCAC ¶ 52, and Plaintiffs do not explain how Farmwald's previous service on the Committee supports the alleged falsity of the 2005 proxy statement. Moreover, the representation at issue refers to the Compensation Committee's work in 2004 and 2005 (the periods covered by the 2005 and 2006 proxy statements). Because Plaintiffs do not allege backdating in 2005, the representation in the 2006 proxy statement is irrelevant. To the extent the challenged backdating ceased in 2003, the representation in the 2005 proxy statement also is irrelevant. Because Plaintiffs' allegations of backdating in 2004 are conclusory and unsupported by particular facts, neither representation, as currently pled, can support liability, and the only question is whether further details concerning the alleged 2004 backdating could render the representation actionable.

Third, Plaintiffs allege that Rambus "materially overstate[d]" fiscal year end values of unexercised in-the-money options. SRCAC ¶¶ 123-24. This allegation, however, is unsupported by any reference to particular options, the amount by which the exercise prices were understated, or the extent of overvaluation. As such, it falls far short of the PSLRA's

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[6] Plaintiffs recently filed what they claim is evidence of backdating accomplished by the Compensation Committee–and in particular by defendants Larson and Dunlevie–in October 2004. The Court expresses no opinion as to whether this evidence would allow Plaintiffs to allege backdating in 2004 with the requisite particularity. *See* Declaration of James Kelley, filed Nov. 16, 2008 (attaching "a Rambus internal document" purportedly showing that specific acts of backdating occurred in 2004).

demanding standard with respect to the context of alleged misrepresentations or omissions. In addition, as Defendants point out, an overstatement of the value of "in-the-money" options would mean that Rambus's compensation expenses for 2004 and 2005 would have been overstated. Logically, such overstatement would mean that the price of Rambus stock purchased by Plaintiffs was deflated rather than inflated.

Fourth, Plaintiffs allege that both proxy statements were false because they were accompanied by allegedly false financial statements, such as Rambus's10-K filings. This theory is wholly unpersuasive. Although provided as a courtesy with the proxy statements, the financial statements cannot be considered part of the proxy statements for § 14(a) purposes unless they are specifically incorporated therein. *See, e.g.*, *Hulliung v. Bolen*, 548 F. Supp. 2d 336, 340-41 (N.D. Tex. 2008) ("Inaccuracies in an annual report cannot form the basis for proxy fraud liability unless the annual report is specifically incorporated into proxy materials."); *Markewich v. Adikes*, 422 F. Supp. 1144, 1147 (E.D.N.Y. 1976) ("Absent a specific declaration of incorporation, a mere mention of the annual report does not incorporate it by reference . . .; otherwise, an annual report would automatically be incorporated by reference in any proxy statement which ever recognized the existence of, or merely accompanies, an annual report."); *Stricklin v. Ferland*, No. Civ. A-98-3279, 1999 WL 89694, at *2 (E.D. Pa. Jan.19, 1999) ("Flaws in annual reports are not actionable under Rule 14a-9 unless the issuer specifically requests that they be treated as part of the proxy material or incorporated them into the materials by reference."). The 2005 and 2006 proxy statements merely noted–as is customary–that copies of the financial statements could be obtained from Rambus free of charge. They did not "incorporate" the accompanying annual reports.

With respect to PwC, Plaintiffs attempt to state three theories of § 14(a) liability: (1) that the inclusion of PwC audit opinions with Rambus's 10-K forms constituted a misstatement or omission by PwC in the proxy statements, since the 10-K forms were included with the proxy statements; (2) that PwC permitted the use of its name in the proxy statements; and (3) that PwC had a duty to "affirmatively permit" the use of its name in the proxy statements, and that its silence therefore amounts to "permission" to use its name. Each of these theories is fundamentally unsound. First, because the 10-Ks themselves were *not* "incorporated" into the proxy statements, Plaintiffs' doubly attenuated theory with respect to PwC fails *a fortiori*. Second, "the reach of section 14(a) could not possibly extend so far" as to make the mere appearance of a party's name in a proxy statement the basis for that party's liability, *Yamamoto v. Omiya*, 564 F.2d 1319, 1322-23 (9th Cir. 1977) (rejecting plaintiff's § 14 claim because "[t]he mere presence of [defendant's] name in the [proxy] materials . . . [does] not reveal any significant control by [the defendant] over the statement, or his adoption of it"), and neither the SRCAC nor its voluminous supporting materials contains any indication that PwC affirmatively "permitted the use of its name" in a manner sufficient to associate it with the proxy statements.

Finally, as to Plaintiffs' argument that PwC had a duty affirmatively to permit the use of its name,[7] there is no authority holding that § 14 creates liability for those not involved in the drafting or review of proxy statements merely by virtue of their silence. *See N.J. v. Sprint Corp.*, 314 F. Supp. 2d 1119, 1148-49 (D. Kan. 2004) (refusing to hold outside auditor liable for omissions in a proxy statement since, without making any representations, an auditor has no general duty to disclose any information in the proxy statement, even where the proxy statement sought shareholder ratification of the auditor). In short, Plaintiffs have failed to allege a material misstatement or omission in the proxy statements by PwC or the Rambus Defendants, and their allegations with respect to the latter can be saved only by further particularized evidence of 2004 backdating.

2. Strong inference of Defendants' negligence

The PSLRA's requires that Plaintiffs plead facts creating a "strong inference" of Defendants' negligence. The inference must be "cogent and compelling, thus strong in light of other explanations." *Tellabs*, 127 S.Ct. at 2510. In that regard, Plaintiffs "must plead particular facts as to *each defendant's* negligence." *In re Zoran*, 511 F. Supp. 2d at 1015 (emphasis added). This standard raises two issues in this case: first, whether a defendant "made" a

[7] This theory appears for the first and only time in Plaintiffs' oppositions to the instant motions to dismiss.

particular statement in a corporate document, and second, whether that defendant did so with the required mental state. Previously, the so-called "group pleading" doctrine permitted an inference that certain documents and statements were the collective work of individuals with "direct involvement" in high-level operations. *In re Pfizer Inc. Sec. Litig.*, __ F.R.D. __, 2008 WL 2627131 (S.D.N.Y. July 1, 2008). The group pleading doctrine was eliminated by the PSLRA. *See, e.g.*, *In re Hansen Natural Corp. Sec. Litig.*, 527 F. Supp. 2d 1142 (C.D. Cal. 2007). However, an officer or director who *signs* a document is deemed to have "made" all of the statements therein. *Howard v. Everex Sys., Inc.*, 228 F.3d 1057, 1061-63 (9th Cir. 2000). While signing a document typically does not establish that the officer or director acted with the requisite mental state, *Howard* involved claims requiring scienter, and it has been suggested that the *Howard* rule alone could support liability in claims requiring only negligence. *See, e.g.*, *Enron*, 540 F. Supp. 2d 800, 825 n.29, 813-14 (S.D. Tex. 2007) (explaining that the holding in *Howard* was premised on the signing defendants' scienter, but that the *Howard* rule alone supports liability in the context of negligence claims).

Even if a defendant did not sign a particular document, a court may, in limited circumstances, infer the "making" of a statement with the requisite mental state from that defendant's position in the corporation. The Ninth Circuit recently addressed the availability of this so-called "core operations inference" in *South Ferry LP, No. 2 v. Killinger*, 2008 WL 4138237 (9th Cir. 2008). In light of the Supreme Court's holding in *Tellabs*, the court concluded that "the core-operations inference can be one relevant part of a complaint that raises a strong inference" of the required mental state." *Id.* at *5. Accordingly, "a series of less precise allegations [may] be read together to meet the PSLRA requirement[s]," such that "[v]ague or ambiguous allegations are now properly considered as a part of a holistic review when considering whether the complaint raises a strong inference" of the requisite mental state. *Id*. The Ninth Circuit also held that without "additional detailed allegations about the defendants' actual exposure to information, it will usually fall short of the PSLRA standard" with respect to *scienter* under § 10(b). *Id.*; *see also Metzler Inv. GmbH v. Corinthian Colleges, Inc.*, 534 F.3d 1068, 1087 (9th Cir. 2008) (holding that bare core-operations inference failed to meet *Tellabs* standard). However, the court has not so held with respect to negligence under § 14, and presumably far less is required when Plaintiffs invoke the core-operations inference merely to establish negligence.

In the instant case, this Court already has narrowed the scope of potential misrepresentations or omissions to the possible falsity of representations concerning Rambus's options grant practices contained in the 2005 proxy statement. Because the 2005 proxy statement was signed "on behalf of the board of directors," *Howard* permits the Court to assume that each of the then-directors "made" the alleged representations. Davidow, Dunlevie, Farmwald, Tate, and Mooring were directors at the time the 2005 proxy statement was released, *see SRCAC* ¶¶ 14-18, and the representations therein can be attributed to these defendants. Moreover, *Howard* may permit the Court to assume that Defendants made the representations negligently, as explained above. Even without the *Howard* rule, Plaintiffs may be able to invoke the core-operations inference because of the presumably lower standard for applying it in the context of negligence claims. In that respect, the Court will give Plaintiffs the benefit of the doubt. It follows that, if Plaintiffs could provide more detailed facts regarding the alleged 2004 backdating, they might be able to establish a strong inference of Defendants' negligence as to the 2005 proxy statement with the aid of *Howard* and the core-operations inference.

3. Essential link

Section 14(a) plaintiffs must demonstrate that the misstatement or omission was an "essential link in the accomplishment of the proposed transaction." *Desaigoudar*, 223 F.3d at 1022 (emphasis added). The essential link requirement can "only be established when the proxy statement at issue *directly authorizes* the loss-generating corporate action." *Hulliung v. Bolen*, 548 F. Supp. 2d 336, 341 (N.D. Tex. 2008) (emphasis added). As noted earlier, this requirement flows from the purpose of § 14(a), which is to prevent shareholder voting on the basis of deceptive proxy solicitations. *Borak*, 277 U.S. at 431.

The only actions put to shareholders by the 2005 and 2006 proxy statements were the following: in 2005, the election of four Class II directors and ratification of PwC as independent auditor; and in 2006, the election of 5 Class I directors, approval of the 2006 Equity Incentive

Plan, approval of the 2006 Employee Stock Purchase Plan, and ratification of PwC as independent auditor. *See* Rambus Notices of Annual Meetings of Stockholders, Decl. of Betty Chang Rowe, Exs. A & B. Plaintiffs attempt to state three theories of an "essential link" between the allegedly false proxy statements and a loss-generating corporate action authorized at the shareholder meetings.

Plaintiffs' first theory turns on Rambus's failure to disclose options grant practices that ceased in 2003 (or, as discussed previously, at the latest in 2004). This theory illogically postulates an "essential link" between the allegedly false proxy statements and corporate actions that occurred years earlier–i.e., the backdating. Several district courts recently have rejected § 14(a) claims based on such a theory. In *Hulliung v. Bollen*, 548 F. Supp. 2d 336 (N.D. Tex. 2008), plaintiffs asserted that the defendant company's proxy statements "were false or misleading because they failed to disclose the company's past backdating [of options]." *Id.* at 340. The court dismissed the claim, holding that, "[a]s a matter of common sense, the Proxies cannot be an essential link to harm caused by stock option backdating that occurred years prior to [the] Proxies' issuance." *Id.* Similarly, the court found it "simply illogical to suggest that Proxies could be an 'essential link' to–i.e., directly authorize–corporate actions that were taken three years or more *before* any of the proxies were distributed." *Id.* (emphasis in original). Similarly, in *In re iBasis, Inc. Deriv. Litig.*, 532 F. Supp. 2d 214 (D. Mass. 2007), plaintiffs brought a § 14(a) claim on the basis of alleged nondisclosure of backdating practices. There, too, the court dismissed the claim because any fallout associated with the backdating would have occurred regardless of disclosure, and because plaintiffs had failed to allege that any backdated options were issued *in connection with the challenged proxy statement*. *Id.* at 222-23. Finally, in *In re Asyst Techs., Inc. Deriv. Litig.*, No. C-06-04669 EDL, 2008 WL 2169021 (N.D. Cal. May 23, 2008), the court rejected a § 14 claim premised on a failure to disclose certain options backdating in a 2004 proxy statement because "[p]laintiffs ha[d] failed to allege that any *additional* backdated stock options were granted after the 2004 statement issued in July, and the last challenged grant occurred in April 2004." *Id.* at *9.

Indeed, future backdating, or the involvement of directors authorized by the proxy vote in some future wrongdoing, has been critical in every case that has found an essential link. *See, e.g.*, *In re Zoran Corp. Deriv. Litig.*, 511 F. Supp. 2d 986, 1016 (N.D. Cal. 2007) ("If defendants had not falsely stated in Zoran's proxy statements that stock options were being granted properly under the plans, and that directors were complying with the terms of the plans that the shareholders approved, shareholders would have voted those board members out, and the board members would no longer have had the means *to grant more backdated stock options*.") (emphasis added); *In re Maxim Integrated Prods., Inc., Deriv. Litig.*, No. C 06-03344 JW, 2008 WL 4061075, at *13 (N.D. Cal. Aug. 27, 2008) (refusing to dismiss § 14(a) claim because "[d]efendants were at least negligent in preparing the proxy statements and that . . . negligence was an essential link in accomplishing *further backdating* transactions which harmed the Company) (emphasis added). By contrast, Plaintiffs in the instant case have "failed to allege . . . that any related–*but not essentially preexisting*–injury occurred after the shareholders approved the recommended action in the proxy statement." *In re iBasis*, 532 F. Supp. 2d at 223 (emphasis added).

Plaintiffs' second theory is that shareholder ratification of PwC as an outside auditor was an essential link in the perpetuation of Rambus's illicit options backdating, as a result of PwC's alleged audit failures and false audit opinions. This theory fails for the reasons already discussed, since Plaintiffs only have alleged backdating that occurred well before Rambus solicited PwC's ratification in the 2005 and 2006 proxy statements. Ratification of PwC as Rambus's auditor cannot have been an essential link to past backdating.

Plaintiffs' third theory is that Rambus's omission with respect to prior backdating in the 2006 proxy statement facilitated the passage of two stock plans at the 2006 shareholder meeting, which plans purportedly caused a decline in Rambus's stock price. *See* Pls.' Opp. to Rambus Mot. to Dismiss, at 23:18-22 ("Rambus' failure to disclose their backdating practices resulted in adoption of the two new stock plans at Rambus in 2006 alone and these plans called for an additional 10% dilution of Rambus capital stock with the consequent negative effect on Rambus stock price. Plaintiffs were damaged by the prospect of a further 10% capital stock dilution."). This theory–which appears for the first time in Plaintiffs' opposition to the instant motions to dismiss–is the only one that *prospectively* implicates a loss-generating corporate action. Yet Plaintiffs offer no support for the proposition that the plans likely would not have been ratified had the previous backdating been disclosed, *cf. id*. at 5 & n.13, nor do they allege any harm that flowed from the "prospect" of a further dilution of Rambus stock. This unsupported theory is a transparent attempt shift attention from Rambus's historical backdating, which is the ultimate wrong of which Plaintiffs complain. That "essentially preexisting . . . injury," *In re iBasis*, 532 F. Supp. 2d at 223, cannot form the basis for § 14 liability.[8] Because none of Plaintiffs' three theories is adequate, Plaintiffs have failed to show that alleged misrepresentations or omissions in the proxy statements were an essential link to a subsequent loss-generating action.

B. Section 18(a) Claims

Section 18(a) creates a right of action in favor of any person who, "in reliance upon [a false or misleading statement contained in a document filed with the SEC], shall have purchased or sold a security at a price which was affected by such statement." 15 U.S.C. § 78r. Thus, to state a claim under § 18, "the plaintiff must plead that (1) a document filed pursuant to the Exchange Act, or any rule or regulation promulgated under it, contained a false or misleading statement; (2) the defendant made or caused to be made the false or misleading statement; (3) the plaintiff actually relied on the false statement; and (4) that reliance caused loss to the plaintiff." *Enron*, 540 F. Supp. 2d at 813.

1. Statute of Limitations

Section 18 contains a limitations period that expires one year from discovery of the alleged violation. 15 U.S.C. § 78i-(e). A large majority of courts have held that the Sarbanes-Oxley statute of limitations found in 28 U.S.C. § 1658(b) did not extend the limitations period

[8] While the Court does not read Plaintiffs' papers to make such arguments, it is clear that Plaintiffs may not claim that the re-election of the directors was an essential link to loss-generating corporate action because of the directors' subsequent mismanagement. *See, e.g.*, *In re Affiliated Computer Servs. Deriv. Litig.*, 540 F. Supp. 2d 695, 704 (N.D. Tex. 2007) ("The mere fact that omissions in proxy materials, by permitting directors to win re-election, indirectly led to financial loss through mismanagement will not create a sufficient nexus with the alleged monetary loss.").

under § 18. *See, e.g.*, *In re Fed. Nat'l Mortg. Ass'n Sec., Deriv., and ERISA Litig.*, 503 F. Supp. 2d 25, 34-35 (D.D.C. 2007); *In re Alstom SA Secs. Litig.*, 406 F. Supp. 2d 402, 419-20 (S.D.N.Y. 2005). In determining when the statute of limitations began to run in this case, the Court first must ask when Plaintiffs had "inquiry notice" of the alleged fraud, and second, when Plaintiffs in the exercise of reasonable diligence should have discovered the facts constituting their claim. *See Betz v. Trainor Wortham & Co.*, 504 F.3d 1017, 1024-25 (9th Cir. 2007). Whether a plaintiff had inquiry notice and conducted a reasonable investigation frequently is a factual question not suitable for resolution as a matter of law. *See Betz*, 504 F.3d at 1026. This is particularly so "where the plaintiff alleges that the defendants' reassurances convinced the plaintiff to postpone his or her legal action." *Id*. However, the question well may be suitable for resolution as a matter of law where (1) the investor is "experienced" or "sophisticated"; (2) the defendants made no reassurances; or (3) the "total[ity] [of] circumstances" otherwise indicates that there are no disputed material facts. *Betz*, 504 F.3d at 1025 n.4, 1027.

In addition, when the effect of the limitations period turns on whether plaintiff exercised reasonable diligence in investigating the facts supporting the claim, the standard under § 18 presumably is far lower than under the Sarbanes-Oxley statute at issue in *Betz*, which applies only to claims sounding in fraud. *See* 28 U.S.C. § 1658(b). Indeed, the Ninth Circuit in *Betz* framed the second step of the inquiry as "whether the plaintiff exercised reasonable diligence in investigating the facts underlying the alleged *fraud*." *Betz*, 504 F.3d at 1025 (emphasis added). In other words, the question was when the plaintiff "actually discovered that she had a claim against the defendants," including evidence of each element of such a claim. *Betz*, 504 F.3d at 1022. *Betz*'s relatively high standard for deciding the limitations question as a matter of law was driven primarily by its concern with the plaintiff's heavy burden of discovering facts indicating scienter. *Betz*, 504 F.3d at 1021-22. A § 18 claim, by contrast, requires only negligence, meaning that far less is required to alert a potential § 18 claimant of his claim.

In the instant case, Plaintiffs base their § 18 claims entirely on alleged misstatements or omissions in Rambus's 2005 10-K form and 2006 proxy statement, filed with the SEC on February 21, 2006, and March 29, 2006, respectively. As an initial matter, there is no doubt that

Plaintiffs were on inquiry notice of their § 18 claim long before they filed the instant action. Plaintiffs previously have acknowledged that they became highly suspicious of Rambus's option grants well before the statutory cutoff date, in effect conceding that they had inquiry notice. *See* Consolidated Amended Complaint ("CAC"), ¶ 125 (stating that 2000 and 2001 losses "caused the Plaintiffs to examine closely the option grants and compensation expenses reported in the 2004 and 2005 10-K and the 2004 and 2005 Proxy Statements in making and retaining Rambus securities in 2005 and 2006"). With respect to whether Plaintiffs in the exercise of reasonable diligence should have discovered their claims, Plaintiffs repeatedly have based their allegations of backdating on a simple analysis of the exercise price for options (which was publicly disclosed shortly after each grant), and the price of Rambus stock before and after the grant (which would show that options were being granted at market lows). *See, e.g.*, Third Amended Complaint, filed May 23, 2007, ¶ 484 (b)-(c); SRCAC ¶ 120 (noting that examination based on the public records indicated that "Rambus was probably backdating"). Based on Plaintiffs' own allegations and judicial admissions, there is nothing to indicate that this analysis could not have been performed–and indeed that it *was not* performed–prior to April 1, 2006, one year before Plaintiffs filed their initial complaint.

The Court's Order of April 17, 2008 recognized that Plaintiffs' claims based on SEC filings prior to the one-year cutoff date appeared to be barred by the statute of limitations "because the facts constituting the cause of action were in the public domain." April 17, 2008 Order at 8:18-22. Only because the Court could not "say with certainty that Plaintiffs could not plead additional facts that would support a claim of delayed discovery" was leave to amend granted. *Id*. In their amended pleading and papers opposing the instant motions, Plaintiffs claim only that they were not on inquiry notice, or could not have discovered the facts underlying their claim, until Rambus "*confirmed*" the "material falsity of the financial statements . . . [on] June 27 and July 18, 2006." SRCAC ¶ 114 (emphasis added); *see also id.* ¶ 115 (stating that "[t]he specific misrepresentations and omissions that comprise the Section 18(a) cause of action were not revealed until Rambus restated it [sic] 2006 Financials on September 14, 2007."). There is, however, no requirement that backdating be "confirmed" before the limitations period runs. The question is whether reasonable diligence would have revealed the existence of a claim.

As the Court already has recognized, and as Plaintiffs' papers make abundantly clear, Plaintiffs are experienced and sophisticated investors. *See* April 17, 2008 Order at 6:22-28. In light of that fact, and considering (1) Plaintiffs' prior admissions as to their awareness of the alleged wrongdoing, (2) the Court's prior direction to Plaintiffs to allege facts to support delayed discovery of Defendants' alleged wrongdoing (i.e., that Plaintiffs were *not* on inquiry notice in the first place or, if on notice, conducted a reasonable investigation into the suspected fraud), and (3) Plaintiffs' failure to plead any such relevant facts, there is a strong argument for dismissal of all of Plaintiffs' § 18 claims on limitations grounds alone. Nonetheless, assuming that the 2005 10-K–the earlier of the two allegedly false documents, filed on February 21, 2006–was the first document containing *all* of the information required to put Plaintiffs on notice of their claims, Plaintiffs would have had thirty-eight days within which to identify the facts underlying the claims and file a lawsuit. Much as in *In re Metropolitan Securities Litigation*, 532 F. Supp. 2d 1260 (E.D. Wash. 2007), in which plaintiffs would have had forty-one days between the issuance of reports allegedly triggering their duty to investigate and the cutoff date under the § 18 statute of limitations, it would seem unfair to assume that Plaintiffs could "investigate the compan[y's] . . . problems, hire an attorney, and file a complaint" in such a brief time. *Id*. at 1288. For that reason, the Court turns to the merits of Plaintiffs' § 18 claim.

2. Material misstatements or omissions

Plaintiffs argue that the 2005 10-K and 2006 proxy statements were false in that they omitted disclosure of prior backdating.[9] The PSLRA requires that Plaintiffs "specify each

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[9]Although Plaintiffs appear to rest solely on their allegations that the 2005 10-K and 2006 proxy statements were false or misleading, the SRCAC is replete with references to "false" Form 4 filings by the named defendants. *See, e.g.*, ¶¶ 57-58, 83. However, nowhere do Plaintiffs (1) explain how these filings are "false" or (2) even assert that they relied on these statements in selling or purchasing securities. It is possible that Plaintiffs rely on the forms to create a strong inference of negligence on the part of defendants Tate, Mooring, and Eulau in issuing the 2005 10-K and 2006 proxy statements. However, because Plaintiffs have not pled the most basic facts in connection with the Form 4 allegations–such as their relevance or how they were false–the

statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint [must] . . . state with particularity all facts on which that belief is formed." 15 U.S.C. § 78u-4(b)(1). The Court already has pointed out the absence of an actionable misstatement or omission in the 2006 proxy statement. *See supra* Section III.B.1. Plaintiffs attack the 10-K filings by stating the following: (1) "The backdating practices materially affected the income statements, the tax deferred assets, the amount of shareholder equity, the assertions and representations as of adequate internal controls, 162(m) tax deductions for incentive stock option (ISO) grants and executive compensation disclosures by grants in each of the Rambus' [sic] 10-K statements which were all materially false because in violation of Generally Accepted Accounting Principles (GAAP), the defendants, inter alia, understated expenses for the reporting period by failing to expense the in-the-money amount of the backdated grants," SRCAC ¶ 33; (2) "Each 10-Q and 10-K filed during 2004, 2005 and 2006 incorporate [sic] the financial statements from the preceding two years and each was materially misstated and omitted material disclosures because of the Defendants' prior backdating practices," SRCAC ¶ 36; and (3) "[The 2005 10-K] . . . showed a further improvement in the SFAS 123 pro forma net income to $3,056,000. . . . In fact, the restatement shows that Rambus suffered another net loss of $9,003,000 for the year and that this statement that Plaintiffs relied on was materially false. . . . In 2004 and 2005, Rambus actually lost over $20 million while reporting that it had earned $2.6 million." SRCAC ¶¶ 112-13.

Neither of the first two statements offers any specific facts supporting Plaintiffs' claim of alleged deviations from accounting standards. The third statement, however, does point to a specific alleged discrepancy between Rambus's stated and actual financial condition. Plaintiffs allege that this discrepancy resulted from the extensive pattern of backdating at Rambus. Indeed, Rambus does not even attempt to argue that the 2006 10-K did not contain false statements. *See* Rambus Mot. to Dismiss, at 17:5-25:6 (arguing failure of Plaintiffs' § 18 claim,

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Court will not consider the allegations.

but declining to dispute the existence of material misstatements or omissions in the 2006 10-K).

As to PwC, Plaintiffs allege (1) that PwC's audit opinions with respect to Rambus's financial statements and internal controls were false and misleading, and (2) that PwC is responsible for errors in Rambus's financial statements. Regarding Plaintiffs' second contention, outside auditors may not be held liable under § 18(a) for misstatements in the company's financial statements that were certified by the auditor. This is because "auditors do not 'certify' a company's financial statements in the sense that they 'guarantee' or 'insure' them. Nor do they, by virtue of auditing a company's financial statements, somehow make, own or adopt the assertions contained therein." *Deephaven Private Placement Trading Ltd, v. Grant Thornton & Co.*, 454 F.3d 1168, 1174 (10th Cir. 2006). With respect to their first contention, Plaintiffs generally must argue either (1) that PwC did not believe its audit opinions were true, or (2) that it did not have a reasonable basis for its audit opinions. *See Deephaven*, 454 F.3d at 1176.

Plaintiffs rely exclusively on a theory that PwC lacked a reasonable basis for its opinions. *See* Pls.' Opp. to PwC Mot. to Dismiss, ¶ 49 ("Plaintiffs have not alleged that PWC disbelieved their own audit and internal control opinions. Plaintiffs here have alleged that PWC had no reasonable basis for its opinion."). They argue in essence that PwC did not recognize "any material weakness in Rambus [sic] internal controls at any time from 1998 into 2006 despite grievous control problems in the stock compensation accounting." Plaintiffs' Opp. to PwC Mot. to Dismiss, at 6:18-22. Plaintiffs point to a series of alleged GAAS and GAAP violations, including PwC's failure to detect overlapping Audit Committee and Compensation Committee conflicts of interest, SRCAC ¶ 95, and failure to discover that Rambus did not amortize compensation costs ratably over the vesting period, as required by the then-applicable APB 25 stock options accounting standard–all amounting essentially to a "failure to audit the single largest expense of the company, i.e., the stock and option grants," SRCAC ¶¶ 101-02.

As already noted, Plaintiffs have alleged a "uniform course of fraudulent conduct" such that Rule 9(b) applies to all of the allegations. *Vess v. Ciba-Geigy Corp. USA*, 317 F.3d 1097, 1103-04 (9th Cir. 2003). PwC is correct that none of the allegations is sufficiently particularized to meet that standard. Plaintiffs do not "link the subsequent restatement of [Rambus's] financial statements with any facts available during the audit that could have alerted [PwC] to the inaccuracies in the information furnished by [Rambus], and thus fail[] to provide particular facts to suggest that PwC actually committed a GAAS violation." *Reiger v. Altris Software, Inc.*, No. 98-528-TW, 1999 WL 540893, at *7 (S.D. Cal. Apr. 30, 1999), *aff'd sub nom. DSAM Global Value Fund v. Altris Software, Inc.*, 288 F.3d 385 (9th Cir. 2002). However, as discussed earlier, Plaintiffs' failure to comply with Rule 9(b) does not end the inquiry. "Where averments of fraud are made in a claim in which fraud is not an element, an inadequate averment of fraud does not mean that no claim has been stated. The proper route is to disregard averments of fraud not meeting Rule 9(b)'s standard and then ask whether a claim has been stated." *Vess*, 317 F.3d at 1105 (quotation marks and citation omitted). Viewing the claims under a negligence standard and drawing all inferences in Plaintiffs' favor, the combination of red flags and the sheer magnitude of the ultimate restatement of Rambus's 2006 10-K could be read to suggest that PwC lacked a reasonable basis for its audits.

3. Strong inference of negligence

As explained above in Section III.A, § 18 requires "something more than negligence." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 211 n.31 (1976). It does so, however, by giving Defendants the opportunity to plead that they acted "in good faith and had no knowledge that [a] statement was false or misleading." 15 U.S.C. § 78r(a). Plaintiffs initially are required to plead no more than facts giving rise to a strong inference of negligence. *See, e.g.*, *Magna Inv. Corp. v. John Does One Through Two Hundred*, 931 F.2d 38, 39-40 (11th Cir. 1991); *In re Alstom* SA, 406 F. Supp. 2d 402, 420 (S.D.N.Y. 2005). The Court therefore rejects without further discussion Defendants' argument that Plaintiffs' claim fails because it pleads only negligence. *See, e.g.*, Tate Mot. to Dismiss, at 6:20-7:8; Rambus Mot. to Dismiss, at 13:17-14:8. Because this action is at the pleading stage, Plaintiffs have no duty to anticipate and rebut such a defense.

In other respects, the PSLRA's "strong inference" requirement for a § 18 claim is similar to that for a § 14 claim. As noted in the § 14 context, several courts have shown a willingness to treat corporate signatures or positions as sufficient to support liability under § 18. *See, e.g.*, *Enron*, 540 F. Supp. 2d 800, 813-14 (S.D. Tex. 2007) (noting that "liability may be imposed on the issuer's officers and directors, in particular those who sign the filed documents") (citing *Kramer v. Scientific Control Corp.*, 452 F. Supp. 812, 817 (E.D. Pa. 1978) (holding that the "fact [of defendants' service as directors on the effective date of the registration statement] alone, if proved, would subject each to liability based upon § 18")). Moreover, consistent with the rule that "a series of less precise allegations [may] be read together to meet the PSLRA requirement[s]," *South Ferry LP, No. 2 v. Killinger*, 2008 WL 4138237, at *5 (9th Cir. 2008), courts have inferred mental states as high as scienter based on a combination of defendants' positions, the magnitude of the alleged wrongdoing, and the common wisdom that "books do not cook themselves," *In re McKesson HBOC, Inc. Sec. Litig.*, 126 F. Supp. 2d 1248, 1273 (N.D. Cal. 2000). *See, e.g.*, *Communications Workers of America Plan for Employees' Pensions and Death Benefits v. CSK Auto Corp.*, 525 F. Supp. 2d 1116, 1124-25 (D. Ariz. 2007) ("The widespread problems at [the company] may have resulted from poor management, but it appears equally plausible that [defendants] possessed the deliberate recklessness or fraudulent intent necessary for scienter in this circuit."); *Batwin v. Occam Networks, Inc.*, No. CV 07-2750 CAS, 2008 WL 2676364, at *13 (C.D. Cal. July 1, 2008) (holding that "significant violations of GAAP, [if] taking place over an extended period of time, give rise to a strong inference of scienter); *In re LDK Solar Securities Litigation*, No. C 07-05182 WHA, 2008 WL 2242185, at *12 (N.D. Cal. May 29, 2008) (following logic of *CSK Auto Corp.*, *supra*, in light of *Tellabs*).

The Court already has concluded that the allegations of a misstatement or omission in the 2006 proxy statement are insufficient to state a claim. However, the circumstances surrounding the alleged misstatements and omissions in the 2005 10-K do establish a strong inference of defendants' negligence. First, the 2005 10-K was signed by defendants Eulau, Tate, Dunlevie, Farmwald, and Mooring. *See* Motion for Judicial Notice, Doc. No. 91, Ex. 5, at 84. As the *Enron* Court held, "the rational of *Howard*[, holding corporate officials accountable for statements they sign], supports imposition of liability under § 18 on directors who sign the corporation's Forms 10-K." *Enron*, 540 F. Supp. 2d at 814 (citing *Howard*, 228 F.3d at 1061). Plaintiffs also have alleged the receipt of multiple and large backdated options grants by Tate, SRCAC ¶¶ 28, 63, 123, 124, Eulau, SRCAC ¶¶ 48, 63, 123, 124, and Mooring, SRCAC ¶ 63, 123, 124, during their tenure as directors and officers, and direct involvement in the authorization of the grants by Tate, SRCAC ¶¶ 39, 58, 65, 69, 76, Eulau, SRCAC ¶ 61, Davidow, SRCAC ¶¶ 40, 59, 62, 64, 67, 71, 74, Dunlevie, SRCAC ¶¶ 40, 59, 62, 64, 67, 71, 74, and Farmwald, SRCAC ¶¶ 40, 56, 59. *See also* SRCAC, Ex. B-14 (showing membership over time of committees responsible for alleged backdating). "The inquiry . . . is whether all of the facts alleged, taken collectively, give rise to a strong inference of [the requisite mental state], not whether any individual allegation, scrutinized in isolation, meets that standard." *Tellabs*, 127 S.Ct. at 2509. Given the magnitude and extent of the problems at Rambus, Defendants' key positions in the company, and their alleged involvement in the granting and receipt of backdated options, even several years before the alleged misstatements or omissions, it would strain credulity to say that Defendants would not have been at least negligent in failing to detect and disclose the vast diversion of cash allegedly accomplished by the backdating. *See Berson v. Applied Signal Tech., Inc.*, 527 F.3d 982, 988 (9th Cir. 2008) (finding strong inference of *scienter* based on defendants' corporate positions because it was "hard to believe that they would not have known about [actions] that allegedly halted tens of millions of dollars of the company's work").

4. Actual Reliance

A § 18 claimant must allege actual reliance on the relevant misstatements or omissions in purchasing or selling a security, and may not allege constructive or presumed reliance. *Howard*, 228 F.3d at 1063; *In re Redback Networks, Inc. Sec. Litig.*, No. CO3-5642JF (HRL), 2007 WL 963958, at *7 (N.D. Cal. Mar. 30, 2007). Conclusory assertions of reliance are insufficient, and plaintiffs must "plead facts probative of their actual reliance on any specific false statement" in the filings at issue. *In re. Supreme Specialties, Inc., Sec. Litig.*, 438 F.3d 256, 284 (3d Cir. 2006). Statements to the effect that plaintiffs "received, reviewed, actually read, and relied upon" certain financial documents, or "actually read and relied upon [them] in making their decisions to invest in [company] common stock," are inadequate. *Suprema Specialties*, 438 F.3d at 284. Finally, a § 18(a) plaintiff must affirmatively allege that such reliance occurred "when he *bought or sold* the security at issue." *Ravenswood Inv. Co. v. Bishop Capital Corp.*, 374 F. Supp. 2d 1055, 1064 (D. Wy. 2005) (emphasis added).

With respect to the 2005 10-K, Plaintiffs state only that "Douglas Kelley and James Kelley read the 2005 10-K filed on February 21, 2006 and it showed a further improvement in the SFAS pro forma net income to $3,056,000. Plaintiff relied on this 10-K data, inter alia, in maintaining investment in Rambus securities." SRCAC ¶ 112. Because Plaintiffs make no attempt anywhere in the complaint to explain the relevance of the figures in these statements, or how they were false, the statements are of the kind rejected by the Third Circuit in *Suprema Specialties*. In addition, because Plaintiffs must show reliance during the sale or purchase of a security, their *maintenance* of Rambus securities is irrelevant for § 18(a) purposes. Plaintiffs' opposition papers confirm the absence of any actual reliance. There, under the heading "Evidence of Actual and Presumed Reliance," Plaintiffs offer nothing but a theory of presumed reliance. Plaintiffs' Opp. to Rambus Mot. to Dismiss, at 20-21. This theory is directly at odds with Ninth Circuit authority. *See Howard*, 228 F.3d at 1063 (holding that actual reliance is required under § 18).

Plaintiffs also have submitted "selected pages from Rambus's 2005 Annual Report, sent to me [James Kelley] prior to the 2005 Annual Shareholders Meeting," which pages "show annotations in my hand, which I made contemporaneously as I read and evaluated Rambus' 10K [sic] and Proxy Statements incorporated in the same 2005 Annual Report." Decl. of James Kelley, at 2:9-15.[10] These pages contain circles and underlining, including with respect to the issuance of options. However, Plaintiffs do not allege when they read any of these documents, or whether and how they relied on them in any way in the sale or purchase of a security. Each of these details is a prerequisite to the Court's attribution of any meaning to the annotated documents.

Plaintiffs' deficient allegations and evidence of reliance are consistent with other patterns affirmatively indicating a lack of reliance on Rambus's financial or proxy statements.

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[10] These documents accompany Plaintiffs' replies the instant motions to dismiss.

As the Court previously found, the assertion that Plaintiffs relied on the 2005 10-K statement is "belied by [their] averment that 'earlier losses [in 2000 and 2001] caused the Plaintiffs to examine closely the options grants and compensation expenses reported in the 2004 and 2005 10-K and the 2004 and 2005 Proxy Statements in making and retaining Rambus securities in 2005 and 2006.'" April 17, 2008 Order at 6:22-28. Indeed, Plaintiffs appear to be "day traders who sought to profit from the short term volatility in Rambus's stock price." *Id.* In addition, Plaintiffs appear to have held short positions on Rambus stock between 2004 and 2006, SRCAC ¶ 144, casting serious doubt on their purported reliance on the market price of that stock or the company's financial or proxy statements.[11] The foregoing facts, combined with Plaintiffs' inadequate affirmative assertions of reliance, require dismissal of Plaintiffs' § 18 claims for lack of actual reliance.

5. Loss Causation

Loss causation requires that the plaintiff "demonstrate a causal connection between the deceptive acts that form the basis for the claim of securities fraud and the injury suffered by the plaintiff." *In re Gilead Sciences Sec. Litig.*, 536 F.3d 1049, 1055-56 (9th Cir. 2008). Plaintiffs must allege that the price of the stock in question was affected by the alleged misrepresentation or omission at the time plaintiffs bought or sold that stock. *See* 15 U.S.C. § 78(r)(a); *Erath v. Xidex Corp.*, No. CIV-89-198TUCACM, 1991 WL 338322, at *11 (D. Ariz. Feb. 7, 1991) (noting that "under § 18(a) the price plaintiff paid must have been affected by the misleading statement"). The misrepresentation "need not be the sole reason for the decline in value of the securities, but it must be a 'substantial cause.'" *In re Gilead*, 536 F.3d at 1055-56 (internal quotation marks omitted). In general, "[s]o long as the complaint alleges facts that, if taken as true, plausibly establish loss causation, a Rule 12(b)(6) dismissal is inappropriate." *Id*.

In the April 17, 2008 Order, the Court noted that "Plaintiffs ha[d] yet to allege loss causation adequately in any of their multiple and voluminous pleadings, [and that] their claims

[11] Plaintiffs respond by asserting that the "Rambus Defendants falsely characterize Plaintiffs [sic] investments as short position [sic] from 2004-2006," Plaintiffs' Opp. to Rambus Mot. to Dismiss, at 17:5-6, but their own pleadings establish this fact.

[were] subject to dismissal for this reason alone." Order at 4:17-23. In their current pleadings, Plaintiffs have alleged several loss-causative events that, viewed in isolation, might present a plausible causal chain. With respect to their alleged 2006 losses, Plaintiffs appear to claim that Rambus's stock price was inflated due to backdating concealed in the 2005 10-K, that the issuance of the Center for Financial Research report concerning companies suspected of backdating precipitated a decline in Rambus's stock price (albeit not an immediate decline) that continued with further revelations of backdating, and that Plaintiffs' suffered losses as a result. Plaintiffs also have alleged–although in completely cursory fashion–that the price of certain stocks they purchased in 2005 was materially affected by the failure to disclose the backdating. *See* SRCAC ¶ 175 & Ex. L-4. While Defendants argue that this causal chain is undermined by Plaintiffs' acknowledgment that Rambus's stock price was "greatly inflated in 2006 because Rambus won a spoliation trial, announced new contracts and entered a patent infringement trial that they were expected to win," SRCAC ¶ 139, the alleged misrepresentation and subsequent correction need only be a "substantial cause" of the alleged loss. *In re Gilead*, 536 F.3d at 1055-56. Moreover, the apparent lack of downward price movement immediately after Rambus filed its 2005 10-K does not necessarily destroy the causal chain. *See id.* at 1057-58.

Nonetheless, the Court previously has noted numerous internal inconsistencies in Plaintiffs' loss causation arguments, particularly with respect to the purported corrective disclosures. A review of the SRCAC reveals that the inconsistencies remain, and Plaintiffs' theory of a corrective disclosure continues to shift. For example, with respect to their alleged losses in 2006, Plaintiffs previously contended that their first loss occurred on April 21, 2006, following a disappointing earnings report on April 19, 2006, CAC ¶ 121, but they now tie their losses to the release of the CFRA report on May 16, 2006, SRCAC ¶ 140. Plaintiffs' latest theory–again asserted only in their opposition papers–is that they "were damaged by the prospect of a further 10% capital stock dilution as evidenced by the $ 7 decline in Rambus stock price from May 10, 2006 (when the solicitations were passed)." SRCAC ¶ 82. There is "an element of the theory of the day" with respect to the alleged corrective disclosures, *see* Statement of Counsel for Rambus, Transcript of September 12, 2008 Hearing, Doc. 259, at 20:1, and these theories, when taken together, are anything but coherent or plausible. Critically, Plaintiffs have not alleged with any clarity that securities they bought or sold were affected by the alleged misstatements or omissions. Ultimately, Plaintiffs must identify securities (1) whose price was affected by specific misstatements or omissions in the 2005 10-K, (2) upon which Plaintiffs actually relied, (3) in purchasing or selling such securities, (4) which securities subsequently were affected by a corrective disclosure, (5) causing Plaintiffs to suffer losses. Plaintiffs have failed once again to allege any such causal chain.

IV. CONCLUSION

Having thoroughly reviewed Plaintiffs' Second (Revised) Consolidated Amended Complaint with respect to each element of the claims, the Court concludes that Plaintiffs cannot state a claim under § 14 of the Exchange Act, and that no additional amendment could save that claim. Even assuming that Plaintiffs could show that their § 14 claim is direct in nature and could cure their defective allegations with respect to misstatements in the 2005 proxy statement by providing particularized evidence of backdating in 2004, their theory would create an insoluble logical conflict with the essential link requirement. With respect to the § 18 claim, Plaintiffs' apparent lack of reliance is evidenced not merely by their repeated failure adequately to plead actual reliance–and their corresponding insistence upon an impermissible theory of presumed reliance–but by the seemingly intractable contradictions that plague those allegations they do offer. Similarly with respect to loss causation, Plaintiffs' inability to settle on a corrective disclosure–and the inconsistency among the disclosures they allege–indicates the lack of a causal relationship between the alleged misstatements and omissions and any actual loss. For these reasons, Defendants' motions to dismiss will be granted.

In assessing whether Plaintiffs once again should be given leave to amend, the Court must consider "the presence or absence of undue delay, bad faith, dilatory motive, repeated failure to cure deficiencies by previous amendments, undue prejudice to the opposing party[,] and futility of the proposed amendment." *Lee v. SmithKline Beecham, Inc.*, 245 F.3d 1048, 1052 (9th Cir. 2001) (quoting *Moore v. Kayport Package Exp., Inc.*, 885 F.2d 531, 538 (9th Cir. 1989)); *see also Foman v. Davis*, 371 U.S. 178, 182 (1962) (providing factors constraining district court's discretion to deny leave to amend). These factors, however, are "not given equal weight . . . , [and] futility of amendment can, by itself, justify the denial of a motion for leave to amend." *Bonin v. Calderon*, 59 F.3d 815, 845 (9th Cir. 1995).

While there is no evidence that Plaintiffs have been guilty of undue delay, bad faith, or dilatory motive, it should be clear from the Court's discussion that amendment of the § 14 claim necessarily would be futile. With respect to the § 18 claim, the Court is convinced that while there may have been wrongdoing at Rambus, Plaintiffs did not rely on that wrongdoing in purchasing or selling any securities and therefore are not within the class of persons protected by the statute. Corporate wrongdoing may well provide ample fodder for allegations of negligent misstatements and omissions, but § 18's reliance and loss causation requirements ensure that only those directly harmed by the alleged misstatements or omissions may recover. Plaintiffs long have been aware of the requirement that they plead actual reliance, *see*, *e.g.*, Transcript of Hearing, Sept. 12, 2008 (containing Plaintiffs' claim to have demonstrated actual reliance); Rambus Reply ISO Mot. to Dismiss, filed Jan. 4, 2008, at 10:15-17 (referring Plaintiffs to Ninth Circuit holding in *Howard*, 228 F.3d at 1063, that § 18 claimants must allege *actual*, as opposed to presumed, reliance); PwC Mot. to Dismiss, filed Dec. 30, 2007, at 14:9-15:9 (explaining actual reliance requirement in light of *Howard*),[12] and of the Court's concern that their contradictory allegations *precluded* a finding of such reliance, *see* Order at 6:22-28 (discussing contradictory nature of Plaintiffs' allegations of reliance), but still have not cured this deficiency in the *tenth* iteration of their complaint.[13] Plaintiffs also have received extensive guidance from the Court with respect to the requirements of loss causation,[14] but they still have not alleged that

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[12] Plaintiffs also were informed explicitly of the requirement that they allege actual reliance at a motion hearing held on March 14, 2008.

[13] Several of these pleadings, including Plaintiffs' second and third amended complaints, were not authorized by the Court.

[14] Not only have Defendants provided citation to all of the relevant authorities on loss causation, but the Court offered a thorough discussion on the subject during the March 14, 2008 motion hearing and in the April 17, 2008 Order.

they relied on the purported misstatements or omissions in *purchasing or selling* a security whose price was *affected* by the alleged misstatements or omissions. Indeed, Plaintiffs have stated only that they "maintained" such securities, which cannot be the basis of a plausible loss causation theory.

In addition to the apparent futility of permitting Plaintiffs to amend their claims, the Court must consider the very real prejudice that defendants have suffered and will continue to suffer if leave to amend is granted. Throughout this litigation, each of Plaintiffs' filings has required Defendants to sift through an enormous volume of highly disorganized material in an attempt to identify relevant facts and legal theories. In dismissing an early version of the complaint for failure to comply with Federal Rule of Civil Procedure 8(a), the Court agreed with Defendants that the complaint, with its 735 paragraphs and extensive requests for judicial notice, amounted to no more than a 1,137-page "morass of allegations . . . . [l]oaded with multiple theories of conspiracies." Order of October 15, 2007, at 3:3-7. In the Order dated April 17, 2008, the Court again noted that "many of Plaintiffs' allegations are confusing and/or internally inconsistent, [such that] both Defendants and the Court have been limited severely in attempting to address the substantive adequacy [of the claims] . . . . [As a result], each of the Defendants has suffered substantial prejudice by having to pay lawyers to read, attempt to understand[,] and respond to Plaintiffs' allegations." Order at 10:19-24. As the foregoing discussion indicates, numerous factual inconsistencies in Plaintiffs' § 18 allegations suggest that no amendment would permit them *truthfully* to plead actual reliance or loss causation. Even accepting that there is at least a theoretical possibility that Plaintiffs could do so given further leave to amend, the Court finds that such a possibility is outweighed by the continuing prejudice that Defendants undoubtedly would suffer as a result. For these reasons, leave to amend will be denied, and judgment will be entered for Defendants.[15]

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[15] At the September 12, 2008 hearing on the instant motions to dismiss, Plaintiffs alerted the Court to new information allegedly revealing that Rambus's internal auditor notified the company and PwC of severe internal control deficiencies with respect to options accounting. *See* Transcript of September 12, 2008 Hearing, Doc. No. 259, at 12:6-23. Given the Court's

IT IS SO ORDERED.

DATED: 12/9/08

JEREMY FOGEL
United States District Judge

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determination that Plaintiffs adequately have pled (1) PwC's negligent failure to provide a reasonable basis for its audit opinions, and (2) the negligence of the other named Defendants with respect to the management and disclosure of the options grant process, the Court does not believe that this information materially affects its disposition. Plaintiffs also have filed what they consider evidence of wrongdoing that would support certain claims previously dismissed with prejudice by this Court. *See* Declaration of James Kelley, filed Nov. 16, 2008 (noting existence of new evidence). With respect to this evidence, the Court offers no opinion as to whether Plaintiffs successfully might seek relief from the judgment pursuant to Federal Rules of Civil Procedure 59(e) or 60(b).

This Order has been served electronically upon the following persons:

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