The following decisions are attached:

Bien v. LifeLock, Inc. **("*Bien I*"), 2014 WL 7641546 (D. Ariz. Dec. 17, 2014)**

Bien v. LifeLock, Inc. **("*Bien II*"), 2015 WL 12819154 (D. Ariz. July 21, 2015)**

Avila v. LifeLock, Inc. **("*Avila I*"), 2016 WL 4157358 (D. Ariz. Aug. 3, 2016)**

Avila v. LifeLock, Inc. **("*Avila II*"), 2017 WL 3669615 (D. Ariz. Aug. 21, 2017)**

2014 WL 7641546
Only the Westlaw citation is currently available.
NOT FOR PUBLICATION
United States District Court, D. Arizona.

Dawn E. BIEN, et al., Plaintiffs,
v.
LIFELOCK INCORPORATED, et al., Defendants.

No. CV–14–00416–PHX–SRB.
|
Signed Dec. 17, 2014.

ORDER

SUSAN R. BOLTON, District Judge.

***1** The Court now considers Defendants' Motion to Dismiss Consolidated Amended Class Action Complaint for Violations of Federal Securities Laws ("MTD") (Doc. 50). The Court heard oral argument on this Motion on December 1, 2014. (Doc. 66, Minute Entry .)

I. BACKGROUND

This is a securities fraud class action brought on behalf of purchasers of Defendant LifeLock Incorporated ("LifeLock") common stock who purchased their stock between February 26, 2013 and May 16, 2014 ("the class period"). (Doc. 42, Consolidated Am. Class Action Compl. ("CAC") ¶ 1.) LifeLock, a publicly traded company, "is a self-proclaimed provider of proactive identity theft protection, and provides services to consumers and enterprises." (*Id.* ¶ 5.) Defendants Todd Davis, Chris Power, and Hilary Schneider (collectively, "Individual Defendants") were executives of LifeLock during the class period. (*Id.* ¶¶ 32–34.)

The CAC alleges that Defendants violated the Securities Exchange Act of 1934 ("the Exchange Act") during the class period by making false and materially misleading statements concerning LifeLock's compliance with a 2010 FTC Settlement Order ("FTC Order"), which expressly prohibits LifeLock from misrepresenting the methods and effectiveness of its identity theft protection services. (*Id.* ¶¶ 1–3.) The CAC also alleges that Defendants made statements misrepresenting its compliance with applicable payment card industry ("PCI") security standards. (*Id.* ¶ 210–12.)[1] Plaintiffs allege that these misleading statements allowed LifeLock to artificially maintain the price of its common stock throughout the class period and once investors learned of LifeLock's failure to comply with the FTC Order and applicable PCI security standards, the price of common stock significantly declined. (*Id.* ¶¶ 20–24 .) The CAC contains two counts: (1) violation of Section 10(b) of the Exchange Act and Rule 10b–5 promulgated thereunder, against all Defendants, and (2) violation of Section 20(a) of the Exchange Act, against the Individual Defendants. (*Id.* ¶¶ 237–51.) Defendants now move to dismiss the CAC, arguing that Plaintiffs have failed to adequately state a claim arising under Section 10(b) and Rule 10b–5. Defendants specifically argue that the CAC fails to adequately plead that Defendants made a false or misleading statement or that any of Defendants' allegedly false or misleading statements were made with scienter. (MTD at 11–25.)[2]

II. LEGAL STANDARDS AND ANALYSIS

A. Judicial Notice

The Court will first resolve Defendants' pending Request for Judicial Notice. (Doc. 52, Req. for Judicial Notice.) Ten of the exhibits to the Request for Judicial Notice are Securities and Exchange Commission ("SEC") filings made by LifeLock or are referenced in the CAC. (*Id.,* Exs. 1–9, 11.) Exhibit 10 is a table of LifeLock's stock price for the time period from February 26, 2013, through May 30, 2014. (*Id.,* Ex. 10.)

***2** Generally on a motion to dismiss a court limits its review to the contents of the complaint and may only consider material that is properly presented to the court as part of the complaint. *See Lee v. City of L.A.,* 250 F.3d 668, 688–89 (9th Cir.2001). However, a court may take judicial notice of "matters of public record" without converting a motion to dismiss into a motion for summary judgment. *Id.* (citing Fed.R.Evid. 201). Courts in the Ninth Circuit have routinely taken judicial notice of SEC filings. *See, e.g., Metzler Inv. GMBH v. Corinthian Colleges, Inc.,* 540 F.3d 1049, 1064 n. 7 (9th Cir.2008); *Karpov v. Insight Enters., Inc.,* No. CV 09–856–SRB, 2010 WL 2105448, at *2 (D.Ariz. Apr.30, 2010). Courts may also consider documents that are referenced in the complaint, if the authenticity of those documents is not at issue and the complaint relies on those documents. *Lee,* 250 F.3d at 688–89 (citations omitted). However, "a court

may not take judicial notice of a fact that is 'subject to reasonable dispute.' " *Id.* (quoting Fed.R.Evid. 201(b)).

The exhibits to the Defendants' Request for Judicial Notice are all properly noticeable. The SEC filings are matters of public record and are capable of accurate and ready determination. Similarly, the compilation of LifeLock's stock price data is a matter of public record and is not subject to reasonable dispute. Plaintiffs do not dispute the Court's taking judicial notice of these documents, but note that judicial notice is not appropriate for the purpose of determining the truth of any of the statements within the SEC filings. (Doc. 55, Pls.' Resp. to Req. for Judicial Notice at 2.) Accordingly, the Court takes judicial notice of the documents appended to Defendants' Request.

B. Motion to Dismiss

Rule 12(b) (6) dismissal for failure to state a claim can be based on either (1) the lack of a cognizable legal theory or (2) insufficient facts to support a cognizable legal claim. *Conservation Force v. Salazar,* 646 F.3d 1240, 1242 (9th Cir.2011), *cert. denied, Blasquez v. Salazar,* —— U.S. ——, 132 S.Ct. 1762, 182 L.Ed.2d 532 (2012). In determining whether an asserted claim can be sustained, "[a]ll of the facts alleged in the complaint are presumed true, and the pleadings are construed in the light most favorable to the nonmoving party." *Bates v. Mortg. Elec. Registration Sys., Inc.,* 694 F.3d 1076, 1080 (9th Cir.2012). "[A] well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof of those facts is improbable, and 'that a recovery is very remote and unlikely.' " *Bell Atl. Corp. v. Twombly,* 550 U.S. 544, 556, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007) (quoting *Scheuer v. Rhodes,* 416 U.S. 232, 236, 94 S.Ct. 1683, 40 L.Ed.2d 90 (1974)). However, "for a complaint to survive a motion to dismiss, the nonconclusory 'factual content,' and reasonable inferences from that content, must be plausibly suggestive of a claim entitling the plaintiff to relief." *Moss v. U.S. Secret Serv.,* 572 F.3d 962, 969 (9th Cir.2009) (quoting *Ashcroft v. Iqbal,* 556 U.S. 662, 678, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009)). In other words, the complaint must contain enough factual content "to raise a reasonable expectation that discovery will reveal evidence" of the claim. *Twombly,* 550 U.S. at 556.

***3** Claims brought under Section 10(b) of the Exchange Act and Rule 10b–5 must also meet the particularity requirements of Federal Rule of Civil Procedure 9(b), which requires that "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." Fed.R.Civ.P. 9(b); *see also In re Daou Sys., Inc. Sec. Litig.,* 411 F.3d 1006, 1014 (9th Cir.2005). Moreover, these claims must meet the heightened pleading standards of the Private Securities Litigation Reform Act ("PSLRA"). *See* 15 U.S.C. § 78u–4. The PSLRA requires a securities fraud complaint to "plead with particularity both falsity and scienter." *Gompper v. VISX, Inc.,* 298 F.3d 893, 895 (9th Cir.2002). To properly allege falsity, a complaint must "specify each 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, ... state with particularity all facts on which that belief is formed." *Id.* (quoting 15 U.S.C. § 78u–4(b)(1)) (quotation marks omitted). To adequately plead scienter, the complaint must "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). To adequately demonstrate that the "defendant acted with the required state of mind," a complaint must "allege that the defendants made false or misleading statements either intentionally or with deliberate recklessness." *In re Daou Sys. Inc.,* 411 F.3d at 1014–15. "[A]n actor is [deliberately] reckless if he had reasonable grounds to believe material facts existed that were misstated or omitted, but nonetheless failed to obtain and disclose such facts although he could have done so without extraordinary effort." *In re Oracle Corp. Sec. Litig.,* 627 F.3d 376, 390 (9th Cir.2010) (quoting *Howard v. Everex Sys., Inc.,* 228 F.3d 1057, 1064 (9th Cir.2000)). The Supreme Court has emphasized that courts "must review all the allegations holistically" when determining whether scienter has been sufficiently pled. *Matrixx Initiatives, Inc. v. Siracusano,* ——U.S. ——, ——, 131 S.Ct. 1309, 1324, 179 L.Ed.2d 398 (2011) (quoting *Tellabs, Inc. v. Makor Issues & Rights, Ltd.,* 551 U.S. 308, 326, 127 S.Ct. 2499, 168 L.Ed.2d 179 (2007)). The relevant inquiry is "whether all of the facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegation, scrutinized in isolation, meets that standard." *Tellabs,* 551 U.S. at 323. In securities cases, falsity and scienter "are generally strongly inferred from the same set of facts" and the two requirements may be combined into a unitary inquiry under the PSLRA." *Ronconi v. Larkin,* 253 F.3d 423, 429 (9th Cir.2011).

1. Statement Concerning the FTC Order

The CAC alleges that Defendants made misleading statements concerning Defendants' compliance with the FTC Order. The FTC Order specifically prohibits LifeLock from misrepresenting the effectiveness of any

> ***4** product, service or, program designed for the purpose of preventing, mitigating, or recovering from any form of identity theft .... includ[ing] but ... not limited to, the placement of fraud alerts on behalf of consumers, searching the internet for consumers' personal data, monitoring commercial transactions for consumers' personal data, identity theft protection for minors, and guarantees of any such products, services, or programs.

(CAC ¶ 62.) The CAC alleges that LifeLock was in violation of the FTC Order during the class period because although LifeLock publicly claimed to protect its customers by providing alerts informing them of any potential identity threats "as soon as [LifeLock] detect[ed] a threat," in reality, LifeLock would frequently turn off or reduce customer fraud alerts to lower the call volume received by its customer support center. (*Id.* ¶¶ 17–18.)

The CAC lists extensive excerpts from LifeLock's various SEC filings and public statements made by Individual Defendants. (*See id.* ¶¶ 170–85, 188–206, 209–19.)[3] Some of the excerpts contain highlighted text, which is presumably meant to indicate a false or misleading statement. At oral argument Plaintiffs' counsel clarified that only those statements that mention the FTC Order are at issue. However, of the highlighted statements listed in the CAC that reference the FTC Order, Plaintiffs' counsel could only point to one statement that allegedly misrepresents Defendants' compliance with the FTC Order, which appears in LifeLock's 2012 Form 10–K. This form states:

> [O]ur business is subject to the FTC [Order] ..., as well as the companion orders with 35 states' attorneys general that we entered into in March 2010. We incur significant costs to operate our business and monitor our compliance with these laws, regulations, and consent decrees.

(*Id.* ¶ 171.) Plaintiffs argue that once Defendants chose to discuss their obligations under the FTC Order, "they were obliged to disclose conduct and *policies* ... that comprised outright violations of the FTC [Order]." (Doc. 54, Pls.' Resp. in Opp'n to MTD ("Resp. to MTD") at 10–11.) Plaintiffs argue that the above statement was misleading because Defendants failed to provide investors with information concerning LifeLock's alleged policy of turning off or reducing customer alerts, in violation of the FTC Order. (*Id.*) Plaintiffs argue that this omission was material because its disclosure "would have significantly altered the 'total mix' of available information" for investors. (*Id.* at 11 (quoting *Matrixx,* 131 S.Ct. at 1318).) Defendants argue that even if the Court concludes that the statement at issue is incomplete, the statement is not misleading because nothing in Defendants' Form 10–K "states that Defendants are *in fact* complying with the FTC Order." (Reply at 14.) Defendants also argue they were not obligated to disclose every incident of mismanagement within LifeLock. (*Id.*)

***5** Section 10(b) of the Exchange Act and Rule 10b–5 prohibit "only misleading and untrue statements, not statements that are incomplete ." *Police Retirement Sys. of St. Louis v. Intuitive Surgical, Inc.,* 759 F.3d 1051, 1061 (9th Cir.2014) (quoting *Brody v. Transitional Hosps. Corp.,* 280 F.3d 997, 1006 (9th Cir.2002)). The Ninth Circuit has "expressly declined to require a rule of completeness for securities disclosures because '[n]o matter how detailed and accurate disclosure statements are, there are likely to be additional details that could have been disclosed but were not.' " *Id.* Therefore, "[t]o be actionable under the securities laws, an omission must be misleading," meaning "it must affirmatively create an impression of a state of affairs that differs in a material way from the one that actually exists." *Id* . The Court concludes that the Form 10–K's reference to the FTC Order is not misleading because it does not "affirmatively create an impression" that LifeLock was actually in compliance with the FTC Order. The statement at issue appears in a paragraph entitled "Government Regulation," which outlines the laws and regulations relevant to LifeLock's operations. While the Form states that LifeLock "incur[s] significant costs to operate [its] business and monitor [its] compliance with [the FTC Order]," the Form goes on shortly thereafter to state that "any determination that we have violated any of these laws, regulations, or consent decrees may result in liability for fines, damages or other penalties, which could

have a material adverse effect on our business, operating results, financial condition, and prospects." (Doc. 51–3, Ex. 3, 2012 Form 10–K at 5.) A reasonable investor would not read this paragraph and conclude that LifeLock is representing that it is in fact in compliance with the FTC Order. The overall picture presented in this section of the Form 10–K is that LifeLock incurs costs in an effort to comply with the FTC Order, however, LifeLock clearly acknowledges that it may be determined that it is not in compliance with the FTC Order. Because the statement at issue does not misrepresent LifeLock's compliance with the FTC Order, LifeLock was not obligated to disclose every company action that may have violated the FTC Order. *See Matrixx,* 131 S.Ct. at 1321–22 (stating that disclosure is required under Rule 10b–5 only when necessary "to make ... statements made, in the light of the circumstances under which they were made, not misleading"). Because the Court concludes that Plaintiffs have failed to show that LifeLock's statement concerning the FTC Order was misleading, it need not address the issue of scienter concerning this statement. [4]

2. Statements Concerning PCI Security Standards

The CAC also alleges that Defendants made false and misleading statements concerning Lifelock's compliance with applicable PCI security standards. The CAC first alleges that "LifeLock's operations were not PCI-compliant in general." (CAC ¶ 212.) After a review of the CAC's reproduction of extensive excerpts from LifeLock's various SEC filings and public statements made by Individual Defendants, the Court could find only one statement that concerns LifeLock's general operations' compliance with PCI security standards: "We have received a PCI Level 1 certification in our consumer and enterprise businesses ...." (*Id.* ¶¶ 172, 200 (citing LifeLock's 2012 and 2013 Forms 10–K).) Plaintiffs do not allege that Defendants have not received a PCI Level 1 certification; instead they argue that this statement was misleading because they allege that Defendants engaged in practices that did not conform to PCI security standards. (*Id.* ¶¶ 177(h), 206(h); Resp. to MTD at 11.) The Court could only find one allegation in the CAC that refers to a LifeLock practice that allegedly violates PCI security standards, and this allegation is solely supported by the observations of one confidential witness, Confidential Witness 3 ("CW3"). (CAC ¶¶ 130–42; Resp. at 20.) [5] CW3 alleges that "PCI compliance prohibits merchants from keeping the recordings of consumer credit card numbers on recorded phone calls. LifeLock, however, was not erasing the credit card numbers off of the phone calls it recorded ...." (CAC ¶ 137.)

***6** Even assuming that Plaintiffs have adequately pled that Defendants' statement concerning its PCI Level 1 certification is misleading because one of their practices violated applicable PCI security standards, the CAC fails to adequately plead that this statement was made with scienter. *See* 15 U.S.C. § 78u–4(b)(2) (requiring scienter to be plead "with respect to *each act or omission* alleged to violate this chapter" (emphasis added)). The CAC appears to rely on the following allegations to support an inference of scienter with respect to the statement at issue: (1) statements of CW3, (2) statements of former LifeLock employee Michael Peters, and (3) statements made in filing the corporation's Sarbanes–Oxley certifications. (*See* CAC ¶¶ 85–89, 137, 176; Resp. to MTD at 16–21.) [6] Considering these allegations both individually and collectively, they fail to sufficiently allege that the statement at issue was made with scienter. First, the CAC does not allege that CW3 interacted with any Individual Defendant; therefore, it does not establish that CW3 had firsthand knowledge concerning whether the Individual Defendants were actually aware of the alleged PCI standards violation. *See Zucco Partners, LLC v. Digimarc Corp.,* 552 F.3d 981, 998 (9th Cir.2009) (stating that even a confidential witness's "generalized claims about corporate knowledge are not sufficient to create a strong inference of scienter, since they fail to establish that the witness reporting them has reliable personal knowledge of the defendants' mental state"); *Karpov,* 2010 WL 2105448, at *8–9 (concluding that because the CAC "does not set forth the basis for the CWs' firsthand knowledge of the state of mind of the [defendants]," the CWs' statements do not establish an inference of scienter on the part of the defendants). Second, although the CAC claims that former LifeLock employee Michael Peters reported potential security risks to Defendant Power, the CAC does not allege that these reported risks violated PCI security standards. (*See* CAC ¶ 85–89.) Therefore, the Court cannot conclude that these reports support a strong inference of scienter for the specific statement at issue. Finally, to the extent Plaintiffs rely Defendants' quarterly Sarbanes–Oxley certifications to create an inference of scienter, the Ninth Circuit has expressly stated that "[b]oilerplate language in a corporation's 10–K form, or required certifications under Sarbanes–Oxley ... add nothing substantial to the scienter calculus" and therefore

"are not enough to create a strong inference of scienter." *Zucco Partners,* 552 F.3d at 1003–04. The Court has considered these allegations separately and as a whole. Even in combination, they fail to sufficiently allege that Defendants intentionally or with deliberate recklessness made a misleading statement concerning LifeLock's PCI certification or its general compliance with applicable PCI standards.

Plaintiffs also allege that Defendants made misleading statements specifically concerning LifeLock's newly acquired mobile Wallet application's compliance with PCI security standards. The CAC claims that during an Investor and Analyst Day, "as speakers hyped the new mobile Wallet app," Defendant Davis stated:

> ***7** We have continually invested knowing that the credibility hit to our brand if we have a data compromise is meaningful and material. So we, **our standard is in just the PCI level 1 certification that we're proud to have, which courses [sic] the data handling, data security certification that all your major financial institution, the highest level of certification you can have.**
>
> Certainly we're proud to have the monitor PCI level 1 but know that's not the bar that we said is [sic] just to achieve PCI level 1. **It is to make sure that we are constantly looking at were there points of vulnerability, points of attack, new and innovative threats. And we're constantly investing on that front to make sure that we are protecting that enterprise and consumer data.** So that we can maintain our trusted relationship with the brand.

(CAC ¶¶ 210–11.) Plaintiffs argue that this statement was misleading because the Wallet application was not compliant with applicable PCI security standards. (*Id.* ¶ 212.) Defendants argue that the above statement does not assert that the Wallet application was in fact PCI-compliant, therefore it is not false or misleading. (MTD at 27 n. 60.) Defendants also argue that the CAC fails to adequately plead that the above statement was made with scienter, and that LifeLock's voluntary disclosure concerning the Wallet application's PCI security standards compliance further negates any alleged inference of scienter. (*Id.* at 11–12, 16–18 .)[7]

Even assuming the CAC adequately pleads that Defendants made a misleading statement concerning LifeLock's compliance with applicable PCI security standards in the context of promoting its mobile Wallet application, the CAC fails to adequately plead that this statement was made with scienter. The CAC contains no specific allegations that the Individual Defendants had actual knowledge that the mobile Wallet application was not PCI-compliant, or that Defendants were in a position to discover the alleged violation "without extraordinary effort," at the time of the statement was made. *See In re Oracle Corp. Sec. Litig.,* 627 F.3d at 390. None of the CAC's allegations based on observations of former employees or confidential witnesses supports an inference of scienter because each of these individuals either stopped working for LifeLock before LifeLock acquired the Wallet application or has not claimed to have personal knowledge of any aspect of the mobile Wallet application. (*See* CAC ¶¶ 72–165 (alleging that all individuals left LifeLock prior to December 2013 except for Confidential Witness 5, who has not claimed to have personal knowledge of the Wallet application).) Considering the CAC's allegations as a whole, they fail to sufficiently allege that Defendants intentionally or with deliberate recklessness made a misleading statement concerning the mobile Wallet application's compliance with applicable PCI security standards.

III. CONCLUSION

***8** The Court grants Defendants' Motion to Dismiss because the CAC does not adequately allege that the statements at issue were either misleading or made with scienter. Count One of the CAC is dismissed as against all Defendants. Count Two is also dismissed, as a violation of Section 20(a) of the Exchange Act, which provides for liability for "controlling" persons, requires a predicate violation of Section 10(b). *See* 15 U.S.C. § 78t(a); *Zucco Partners,* 552 F.3d at 990. As the Complaint in this case has only been amended once and because of the liberal policy in favor of amendment embodied in Federal Rule of Civil Procedure 15(a), the Court will grant the Motion to Dismiss but allow Plaintiffs to seek leave to amend no later than 21 days from the date of this Order. *See, e.g., Mark H. v. Lemahieu,* 513 F.3d 922, 939–40 (9th Cir.2008) (citing *Verizon Del., Inc. v. Covad Commc'ns Co.,* 377 F.3d 1081, 1091 (9th Cir.2004)). Plaintiffs are instructed to follow the applicable local and procedural rules governing amended pleadings in seeking leave to amend. *See* Fed.R.Civ.P. 15; LRCiv. 15.1.

IT IS ORDERED granting Defendants' Motion to Dismiss Consolidated Amended Class Action Complaint for Violations of Federal Securities Laws (Doc 50).

IT IS FURTHER ORDERED denying as moot Lead Plaintiff's Motion for Leave to File Sur–Reply to Correct Scrivener's Error (Doc 58).

IT IS FURTHER ORDERED denying as moot Defendants' Motion to Strike Lead Plaintiff's Notice of Errata Re: Consolidated Amended Complaint Paragraph 215 (Doc. 61).

IT IS FURTHER ORDERED that Plaintiffs must seek leave to amend within 21 days of this Order. If they fail to do so, the Clerk of Court is instructed to enter a judgment of dismissal.

All Citations

Not Reported in F.Supp.3d, 2014 WL 7641546

Footnotes

1 PCI security standards are "technical and operational requirements set by the Payment Card Industry Security Standards Council to protect cardholder data" and they "govern all merchants and organizations that store, process or transmit this data." PCI Security Standards Council, *Payment Card Industry Security Standards* (2008), https://www.pcisecuritystandards.org/pdfs/pcissc_overview.pdf.

2 Defendants also argue that the CAC fails to adequately plead that any economic loss was caused by Defendants' allegedly false or misleading statements. (MTD at 2529.); *see also Halliburton Co. v. Erica P. John Fund, Inc.,* —— U.S. ——, ——, 134 S.Ct. 2398, 2407, 189 L.Ed.2d 339 (2014) (outlining the elements necessary to state a claim under Section 10(b) of the Exchange Act and Rule 10b–5). Because the Court concludes that the CAC fails to adequately plead falsity and scienter, the Court does not reach the issue of whether the CAC adequately pled loss causation.

3 Defendants argue that the CAC should be dismissed because it adopts a "puzzle" style of pleading that fails to identify specific false statements, in violation of 15 U.S.C. § 78u–4(b)(1). (MTD at 27 n. 57; Doc. 56, Defs.' Reply in Supp. of MTD ("Reply") at 13 n. 26); *see also In re Autodesk, Inc. Sec. Litig.,* 132 F.Supp.2d 833, 842 (N.D.Cal. Nov.14, 2000) (describing "puzzle pleadings" as those that require the defendants and the court to "match the statements up with the reasons they are false or misleading"). Although the Court agrees that the complaint is repetitive and poorly organized, the Court has concluded it is at least clear enough to put Defendants on notice of the allegations and to enable Defendants to respond. *See Twombly,* 550 U.S. at 555.

4 Should Plaintiffs elect to amend the CAC, they should be mindful of the requirement to plead with particularity both falsity and scienter *for each alleged misrepresentation* in order to bring a securities fraud action under the PSLRA. *See* 15 U.S.C. § 78u–4(b). Moreover, the Court notes Defendants' compelling arguments concerning the CAC's reliance on the five confidential witnesses to support a strong inference of scienter. (MTD at 19–23.)

5 The Court notes that the CAC also contains allegations of Michael Peters, a former LifeLock employee, who believes that "LifeLock's security posture was at high risk." (¶¶ 85–88.) However, none of the allegations based on Peters's observations identify how LifeLock's practices comported with applicable PCI security standards, therefore these allegations provide little weight to support Plaintiffs' contention that LifeLock was not PCI-compliant.

6 Plaintiffs' responsive memorandum also argues that the CAC's allegations concerning Defendants' motives to make misleading statements, failure to provide a non-fraudulent explanation for their conduct, actual access to information, and the "core operations" inference support an inference of scienter. (Resp. to MTD at 22–26.) However, Plaintiffs only argue that these allegations support an inference of scienter for statements made concerning the FTC Order, and have not shown that they support an inference of scienter for the statement concerning the compliance of LifeLock's general practices to the applicable PCI standards.

7 On May 16, 2014, LifeLock filed a Form 8–K stating:

> **We have determined that certain aspects of the Lemon Wallet (now called the LifeLock Wallet mobile application), which we acquired as part of our acquisition of Lemon, Inc., are not fully compliant with applicable payment card industry (PCI) security standards.** As a result, we have temporarily suspended the Wallet mobile application, and are deleting the data (encrypted or otherwise) from our servers, until we can operate the Wallet mobile application in accordance with those standards.

(CAC ¶ 221.)

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Only the Westlaw citation is currently available.
NOT FOR PUBLICATION
United States District Court, D. Arizona.

Dawn E. BIEN, et al., Plaintiffs,
v.
LIFELOCK INCORPORATED, et al., Defendants.

No. CV-14-00416-PHX-SRB
|
Signed 07/21/2015

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ORDER

Susan R. Bolton, United States District Judge

***1** The Court now considers Defendants' Motion to Dismiss Second Consolidated Amended Class Action Complaint for Violations of Federal Securities Laws ("MTD") (Doc. 77). The Court heard oral argument on March 16, 2015. (Doc. 85, Minute Entry.)

I. BACKGROUND

The Court has summarized the facts of this case in a previous Order, which is fully incorporated herein. (*See* Doc. 70, Dec. 17, 2014 Order at 1-2.) The Court dismissed Plaintiffs' Consolidated Amended Class Action Complaint ("CAC"), finding that the CAC failed to sufficiently allege a violation of Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5, 17 C.F.R. § 240.10b-5. (*Id.* at 12-13.) The Court specifically concluded that the CAC had failed to adequately allege that Defendants made a false or misleading statement concerning LifeLock Incorporated's ("LifeLock") compliance with a 2010 FTC Settlement Order ("FTC Order"). The FTC Order prohibits LifeLock from misrepresenting the methods and effectiveness of its identity theft protection services. (*Id.* at 5-7.) The Court also concluded that the CAC failed to allege that Defendants had made a misleading statement concerning its compliance with applicable payment card industry ("PCI") security standards or that any allegedly misleading statement was made with scienter. (*Id.* at 8-12.) Plaintiffs have filed a Second Consolidated Amended Class Action Complaint ("SCAC"). (Doc. 75.) Defendants move to dismiss the SCAC, arguing that the SCAC fails to adequately plead that Defendants made a false or misleading statement or that any of Defendants' allegedly false or misleading statements were made with scienter. (MTD at 2-27.) [1]

II. LEGAL STANDARDS AND ANALYSIS

A. Legal Standards

***2** Rule 12(b)(6) dismissal for failure to state a claim can be based on either (1) the lack of a cognizable legal theory or (2) insufficient facts to support a cognizable legal claim. *Conservation Force v. Salazar*, 646 F.3d 1240, 1242 (9th Cir. 2011), *cert. denied*, *Blasquez v. Salazar*, 132 S. Ct. 1762 (2012). In determining whether an asserted claim can be sustained, "[a]ll of the facts alleged in the complaint are presumed true, and the pleadings are construed in the light most favorable to the nonmoving party." *Bates v. Mortg. Elec. Registration Sys., Inc.*, 694 F.3d 1076, 1080 (9th Cir. 2012). "[A] well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof of those facts is improbable, and 'that a recovery is very remote and unlikely.' " *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 556 (2007) (quoting *Scheuer v. Rhodes*, 416 U.S. 232, 236 (1974)). However, "for a complaint to survive a motion to dismiss, the nonconclusory 'factual content,' and reasonable inferences from that content, must be plausibly suggestive of a claim entitling the plaintiff to relief." *Moss v. U.S. Secret Serv.*, 572 F.3d 962, 969 (9th Cir. 2009) (quoting *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009)). In other words, the complaint must contain enough factual content "to raise a reasonable expectation that discovery will reveal evidence" of the claim. *Twombly*, 550 U.S. at 556.

Section 10(b) or Rule 10b-5 claims also must meet the particularity requirements of Federal Rule of Civil Procedure 9(b), which requires that "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." Fed. R. Civ. P. 9(b); *see also In re Daou Sys., Inc. Sec. Litig.*, 411 F.3d 1006, 1014 (9th Cir. 2005). Moreover, these claims must meet the heightened pleading standards of the Private Securities Litigation Reform Act ("PSLRA"). *See* 15 U.S.C. § 78u-4. The PSLRA requires a securities fraud complaint to "plead with particularity both falsity and scienter." *Gompper v. VISX, Inc.*, 298 F.3d 893, 895 (9th Cir. 2002). To properly allege falsity, a complaint must "specify each 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, ... state with particularity all facts on which that belief is formed." *Id.* (quoting 15 U.S.C. § 78u-4(b)(1)) (quotation marks omitted). To adequately plead scienter, the complaint must "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). To adequately demonstrate that the "defendant acted with the required state of mind," a complaint must "allege that the defendants made false or misleading statements either intentionally or with deliberate recklessness." *In re Daou Sys.*, 411 F.3d at 1014-15. "[A]n actor is [deliberately] reckless if he had reasonable grounds to believe material facts existed that were misstated or omitted, but nonetheless failed to obtain and disclose such facts although he could have done so without extraordinary effort." *In re Oracle Corp. Sec. Litig.*, 627 F.3d 376, 390 (9th Cir. 2010) (quoting *Howard v. Everex Sys., Inc.*, 228 F.3d 1057, 1064 (9th Cir. 2000)). The Supreme Court has emphasized that courts "must review all the allegations holistically" when determining whether scienter has been sufficiently pled. *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1324 (2011) (quoting *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 326 (2007)). The relevant inquiry is "whether all of the facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegation, scrutinized in isolation, meets that standard." *Tellabs*, 551 U.S. at 323. In securities cases, falsity and scienter "are generally strongly inferred from the same set of facts" and the two requirements may be combined into a unitary inquiry under the PSLRA." *Ronconi v. Larkin*, 253 F.3d 423, 429 (9th Cir. 2011).

B. Analysis

1. Compliance with the FTC Order

***3** In the initial dismissal Order, the Court concluded that Plaintiffs had failed to sufficiently allege that Defendants made a false or misleading statement related to LifeLock's compliance with the FTC Order. (*See* Dec. 17, 2014 Order at 5-8 (stating that the FTC-related statement at issue was not misleading because, when read in context, it did not " 'affirmatively create an impression' that LifeLock was actually in compliance with the FTC Order").) Similar to the CAC, the SCAC lists extensive excerpts from LifeLock's various SEC filings and public statements made by Defendants Davis and Power that reference the FTC Order. (*See, e.g.*, SCAC ¶¶ 211-16, 220-22, 228-30, 234-36.) The SCAC emphasizes some of the excerpts in bold typeface, which is presumably meant to indicate a false or misleading statement. Almost all of the statements referencing the FTC Order were previously alleged in the dismissed CAC. (*Compare id.*, *with* CAC ¶¶ 170-76, 178-80, 182-84, 188-90.) Plaintiffs have included one additional statement from LifeLock's 2013 Form 10-K related to Defendants' FTC compliance that was not alleged as a false or misleading statement in the CAC:

> On January 17, 2014, we met with FTC Staff, at our request, to discuss issues regarding allegations that have been asserted in a whistleblower claim against us relating to **our compliance with the FTC Order.** Following this meeting, we expect to receive either a formal or informal investigatory request from the FTC for documents and information regarding our policies, procedures, and practices for our services and business activities. Given the heightened public awareness of data breaches and well as attention to identity theft protection services like ours, it is also possible that the FTC, at any time, may commence an unrelated inquiry or investigation of our business practices and our compliance with the FTC Order. **We endeavor to comply with all**

> **applicable laws and believe we are in compliance with the requirements of the FTC Order.** We believe the increased regulatory scrutiny will continue in our industry for the foreseeable future and could lead to additional meetings or inquiries or investigations by the agencies that regulate our business, including the FTC.

(SCAC ¶ 239.)

a. Opinion Statement

Defendants argue that the above statement "we ... believe we are in compliance with the requirements of the FTC Order" is an opinion statement and Plaintiffs' allegations "fail to satisfy the legal requirement for alleging statements of belief and opinion to be false." (MTD at 10-13.) The Supreme Court has recently addressed the standard for determining whether a statement of opinion or belief is actionable as securities fraud. *See Omnicare, Inc. v. Laborers Dist. Council Constr. Indus. Pension Fund*, 135 S. Ct. 1318, 1325-32 (2015). In *Omnicare*, the Supreme Court confirmed that "a sincere statement of pure opinion is not an 'untrue statement of ... fact' " simply because the stated opinion ultimately proves incorrect. *Id.* at 1327. The Court also concluded that opinion statements are not wholly immune from liability and may be considered material misstatements or omissions in certain circumstances. *Id.* at 1326-28. In the omission context, the Court stated that "depending on the circumstances, [a reasonable investor may] understand an opinion statement to convey facts about how the speaker has formed the opinion." *Id.* at 1328. If a party's opinion statement "omits material facts about the [party's] inquiry into or knowledge concerning a statement of opinion, and if those facts conflict with what a reasonable investor would take from the statement itself," liability may accrue. *Id.* at 1329.[2] The Court also stated that an opinion statement is not necessarily misleading "when an issuer knows, but fails to disclose, some fact cutting the other way," as a reasonable investor "does not expect that every fact known to an issuer supports its opinion statement." *Id.* The Court further explained that "whether an omission makes an expression of opinion misleading always depends on context," noting that an investor reads each statement, "whether of fact or opinion, in light of all its surrounding text, including hedges, disclaimers, and apparently conflicting information." *Id.* at 1330. In order to sufficiently allege that a statement of opinion is actionable a plaintiff

> ***4** must identify particular (and material) facts going to the basis for the issuer's opinion—facts about the inquiry the issuer did or did not conduct or the knowledge it did or did not have—whose omission makes the opinion statement at issue misleading to a reasonable person reading the statement fairly and in context.

Id. at 1332.

Plaintiffs argue that LifeLock's 2013 Form 10-K omitted the fact that Defendants Davis and Power were aware that LifeLock failed to send out a number of alerts to customers as advertised (a practice known as "throttling"). (Doc. 81, Resp. in Opp'n to MTD ("Resp. to MTD") at 12-13 (citing SCAC ¶¶ 73-81, 85, 90 (alleging that LifeLock's practice of throttling was described in both a wrongful termination and a whistleblower complaint), 145-47 (alleging that Defendants Davis and Power were present at meetings addressing LifeLock's failure to send out timely alerts), 179-80 (alleging that the Chief Marketing Officer informed Defendant Davis that the LifeLock's advertising would have to change in light of throttling)).) Plaintiffs argue that because this practice was not disclosed in the 2013 Form 10-K, this omission renders LifeLock's opinion that it was in compliance with the FTC Order misleading. (*Id.*) Defendants counter that even if the SCAC sufficiently alleges that Defendants were aware that a number of alerts were not being timely sent to LifeLock customers, the SCAC fails to allege that these service lapses were "indicative of anything beyond an ordinary quality-control problem" or that Defendants "knew that such lapses put LifeLock in violation of the FTC Order." (MTD at 12; *see also id.* at 12 n.24 (noting that LifeLock has 3.2 million members, so even if thousands of alerts were unsent, this lapse "may have been minuscule in comparison to the number of alerts sent").) Defendants argue that without such allegations, Plaintiffs have failed to allege that the opinion statement that LifeLock was in compliance with the FTC Order was

a misleading statement under the Exchange Act. (*Id.* at 12-13.)

Plaintiffs have failed to sufficiently allege that Defendants were aware of undisclosed, material facts whose omission rendered the opinion statement at issue misleading in the context of the 2013 Form 10-K. Even if Plaintiffs have sufficiently alleged that Defendants knew LifeLock was sending out delayed alerts to certain customers, conclusory allegations that "Defendants flagrantly violated the terms of the [FTC] Order" are insufficient to demonstrate that Defendants knew or reasonably should have known that this practice violated the FTC Order. (*See* SCAC ¶ 69.) The SCAC does not contain sufficient factual allegations demonstrating that Defendants knew the extent of LifeLock's throttling practice or whether this practice was actually pervasive enough to put LifeLock in violation of the FTC Order. (*See, e.g.*, *id.* ¶¶ 76-77 (alleging only that a former employee expressed concern to "LifeLock personnel" that throttling "might violate" the FTC Order).) The SCAC also contains allegations that after Defendants became aware of the service lapses, they acted to resolve the issues and altered their advertisements to reflect the delayed alerts. (*See id.* ¶ 145 (alleging that a confidential witness claimed Defendant Davis was "very well aware of the system issues" and Davis stated that LifeLock was "bringing on new people and reorganizing the technology department" to address them), 179-80 (alleging that after a confidential witness told Defendant Davis that LifeLock's advertising would have to change to reflect LifeLock's throttling of alerts, this confidential witness received approval to change the advertising and the advertising was in fact temporarily changed).) Even if Plaintiffs have sufficiently alleged that Defendants were aware of LifeLock's throttling practice, the Court cannot conclude that Plaintiffs have sufficiently alleged that Defendants were aware of undisclosed material facts tending to significantly undermine the accuracy of their belief that LifeLock was still in compliance with the FTC Order.

***5** The context in which LifeLock expressed its opinion concerning its compliance with the FTC Order further supports the conclusion that LifeLock's alleged omission does not render the opinion statement misleading. *See Omnicare*, 135 S. Ct. at 1330 (stating that "an omission that renders misleading a statement of opinion when viewed in a vacuum may not do so once that statement is considered, as is appropriate, in a broader frame"). In addition to the opinion statement at issue, LifeLock's 2013 Form 10-K contained negative disclosures concerning the effect of its rapid growth on its services. (*See* Doc. 51-1, 2013 Form 10-K.)[3] LifeLock specifically disclosed that it had experienced substantial growth, which "place[d] a strain on [its] operational, financial, and management infrastructure," and warned that its "failure to effectively manage growth could have a material adverse effect on [its] business ... [and] operating results." (*Id.* at 18; *see also id.* at 17 (warning that its business could be adversely affected by "challenges encountered by companies that are rapidly developing and are experiencing rapid growth in evolving industries").) LifeLock also acknowledged that its business could be harmed if LifeLock experienced problems related to "customer service and responsiveness to any customer complaints" or it is not able to update its technology to match its growth, which would cause "outages" or "disruption[s] in [LifeLock's] business operations." (*Id.* at 15-17.) LifeLock also disclosed the FTC Order's injunctive terms (including LifeLock's submission of an annual compliance report) and the consequences of and penalties for noncompliance with those terms. (*Id.* at 9-10.) LifeLock stated that although it had submitted its annual compliance report, it had not been accepted or approved by the FTC. (*Id.* at 10.) LifeLock also disclosed that it had recently met with FTC staff to discuss allegations of noncompliance with the FTC Order, that it expected to receive an investigatory request from the FTC for documents and information regarding its business practices, and that the FTC may begin an investigation of LifeLock's business practices or compliance with the FTC Order. (*Id.*) In light of these negative disclosures concerning potential service disruptions due to LifeLock's rapid growth, allegations of noncompliance with the FTC Order, and LifeLock's anticipation of an FTC investigation, the Court cannot conclude that Defendants' failure to specifically disclose their knowledge of unsent or delayed alerts rendered the opinion statement "misleading to a reasonable person reading the statement fairly and in context." *See Omnicare*, 135 S. Ct. at 1332.

b. Statements Previously Alleged in CAC

Defendants argue that the remaining statements concerning LifeLock's compliance with the FTC Order were previously alleged in the dismissed CAC and, therefore, the Court has already determined that these

statements are not false or misleading. (MTD at 1-3.) The Court previously stated that the "overall picture presented in ... the Form 10-K is that LifeLock incurs costs in an effort to comply with the FTC Order, however, LifeLock clearly acknowledges that it may be determined that it is not in compliance with the FTC Order." (Dec. 17, 2014 at 7-8.) The Court concluded that a reasonable investor would not understand that LifeLock was representing it was in fact in compliance with the FTC Order. (*Id.*) Plaintiffs argue that they have cured the CAC's deficiencies because the SCAC includes an allegation that a Deutsche Bank Market Research ("DBMR") analyst who covered LifeLock understood that Defendants represented LifeLock was in compliance with the FTC Order and, therefore, the SCAC sufficiently alleges that the FTC-related statements in the 2013 Form 10-K are misleading. (Resp. to MTD at 16; *see also* SCAC ¶ 255.) Plaintiffs also argue that all of the FTC-related statements are actionable as incomplete statements because the SCAC includes allegations that LifeLock's Code of Business Conduct and Ethics required "only complete, factual and truthful statements about [the] Company." (Resp. to MTD at 16-17; *see also* SCAC ¶ 72.) Plaintiffs contend that Defendants were obligated to discuss those practices, such as throttling, "that comprised outright violations of the FTC [Order]." (Resp. to MTD at 15.)

Plaintiffs' additions fail to cure the deficiencies identified in the Court's previous Order. The SCAC alleges that the DBMR analyst stated, in relevant part:

> [W]e view LifeLock's meeting with the FTC, and subsequent 10-[K] disclosure as an effort to be more transparent with investors.... LifeLock has already settled [a whistleblower lawsuit filed with the FTC], and is engaging proactively with the FTC, as they have been since 2010 **to stay compliant with FTC regulations.**

(SCAC ¶ 255.) As an initial matter, the Court notes that the statements made by the DBMR analyst are not alleged in the SCAC as evidence of the market's understanding of LifeLock's statements in the 2013 Form 10-K, but instead are alleged to be actionable statements made by a third party. (*See* SCAC ¶ 256 (stating that "[t]he [analyst's] statements in Paragraph 255 above were materially false when made, and/or omitted material information necessary to make the statements not misleading ..."); *see also* Resp. to MTD at 16 n.8 (disputing Defendants' assertion that the analyst's statements cannot support a securities fraud claim).) To the extent Plaintiffs argue that the statement concerning FTC compliance in the DBMR report can support a securities fraud claim, the Court disagrees. The DBMR report does not identify which (if any) LifeLock employee affirmatively stated that the company was compliant with the FTC Order and therefore this is not an actionable third party statement. *See Nursing Home Pension Fund, Local 144 v. Oracle Corp.*, 380 F.3d 1226, 1235 (9th Cir. 2004) (stating that a statement made by a third party is only actionable when it "clearly originated" from the defendants). Plaintiffs also fail to identify the specific statements upon which the analyst's belief is based. Without such allegations, the Court cannot determine which statement the market allegedly understood to represent that LifeLock was actually in compliance with the FTC Order. Because the analyst's statements do not sufficiently demonstrate that Defendants made a false or misleading statement within the context of LifeLock's 2013 Form 10-K concerning its FTC compliance, this allegation fails to cure the deficiencies identified in the CAC.

***6** Plaintiffs' allegations that LifeLock's Code of Business Ethics "required only complete, factual and truthful statements about [the] Company" also fails to cure the deficiencies identified in the Order dismissing the CAC. As discussed in the initial dismissal Order, Section 10(b) of the Exchange Act prohibits "only misleading and untrue statements, not statements that are incomplete." *Brody v. Transitional Hosps. Corp.*, 280 F.3d 997, 1006 (9th Cir. 2002) ("No matter how detailed and accurate disclosure statements are, there are likely to be additional details that could have been disclosed but were not."); (*see* Dec. 17, 2014 Order at 7.) Even assuming that an incomplete statement concerning LifeLock's compliance with the FTC Order could be actionable as securities fraud, in light of the negative disclosures in LifeLock's 2013 Form 10-K discussed above, the Court cannot conclude the allegedly misleading statements Plaintiffs identify were incomplete when read in context. Because Plaintiffs have not sufficiently alleged that Defendants made a false or misleading statement concerning LifeLock's compliance with the FTC Order, the amendments in the SCAC fail to cure the deficiencies identified in the Court's prior Order.

2. Compliance with PCI Standards

In the initial dismissal Order, the Court concluded that even if Plaintiffs had made a misleading statement concerning LifeLock's compliance with the applicable PCI security standards, Plaintiffs had failed to allege that any such statement was made with scienter. (*See* Dec. 17, 2014 Order at 8-12 (stating that Plaintiffs "fail[ed] to sufficiently allege that Defendants intentionally or with deliberate recklessness made a misleading statement concerning" LifeLock's PCI certification, general compliance with PCI standards, or LifeLock's mobile Wallet application's PCI compliance).) In the SCAC Plaintiffs re-allege two statements addressed in the Court's previous Order:

> "We have received a PCI Level 1 certification in our consumer and enterprise businesses...." [(SCAC ¶ 247 (quoting LifeLock's 2013 Form 10-K).)]
>
> ....
>
> We have continually invested knowing that the credibility hit to our brand if we have a data compromise is meaningful and material. So we, **our standard is in just the PCI level 1 certification that we're proud to have, which courses [sic] the data handling, data security certification that all your major financial institution, the highest level of certification you can have.**
>
> Certainly we're proud to have the monitor PCI level 1 but know that's not the bar that we said is [sic] just to achieve PCI level 1. **It is to make sure that we are constantly looking at were there points of vulnerability, points of attack, new and innovative threats. And we're constantly investing on that front to make sure that we are protecting that enterprise and consumer data. So that we can maintain our trusted relationship with the brand.** [(*Id.* ¶ 258 (quoting Defendant Davis at an Investor and Analyst Day).)]

(*See also* Dec. 17, 2015 Order at 8-10.) The SCAC also alleges that the following statements are either false or misleading because LifeLock's operations and the mobile Wallet application were not PCI-compliant:

> LifeLock identify theft protection helps proactively safeguard your credit, your finances and your good name.... [(*Id.* ¶ 224 (quoting a June 28, 2013 advertisement).)]
>
> ....
>
> The LifeLock Wallet mobile application allows ... mobile use of items such as credit, identification, ATM, insurance, and loyalty cards. [(*Id.* ¶ 250 (quoting LifeLock's 2013 Form 10-K).)]
>
> ....
>
> As you know, we acquired Lemon, Inc. late in the fourth-quarter.... We can now help organize what's in your wallet and protect it as well. [(*Id.* ¶ 253 (quoting a statement made by Defendant Davis at LifeLock's Q4 2013 Earnings Call).)]

Plaintiffs allege that the above statements were false or misleading because LifeLock was not capable of "safeguard[ing]" or "protect[ing]" its customers' personal information as claimed because its general services were not PCI-compliant, and the Wallet application did not actually permit the customers' mobile use of their credit or identity cards because the application also was not PCI-compliant. (*See id.* ¶¶ 225(f), 252(*l*), 254(a).) Defendants argue that Plaintiffs have failed to sufficiently establish that the above statements are false or misleading because the statements do not reference the PCI standards, let alone assert that LifeLock or its Wallet application were in compliance with these standards. (MTD at 20-22.) Defendants also argue that even if LifeLock was not PCI-compliant, the SCAC does not sufficiently allege that the Wallet application did not permit the mobile uses indicated, or that LifeLock was actually incapable of protecting its customers' information. (*Id.*)

***7** Even if the Court were to conclude that the above statements concerning PCI compliance are misleading, Plaintiffs have again failed to adequately plead that the statements were made with scienter. *See* 15 U.S.C. § 78u-4(b)(2) (requiring scienter to be plead "with respect to each act or omission alleged to violate this chapter"). For each of the above statements, Plaintiffs allege that "Defendants had actual knowledge of this PCI noncompliance and/or were reckless in rushing the Wallet App onto the market." (*See* SCAC ¶¶ 252(m), 259(j), 254(b).)[4] The SCAC appears to rely on the following allegations to support Plaintiffs' position that Defendants "had actual knowledge" of LifeLock's and its Wallet application's PCI noncompliance: (1) statements of three confidential witnesses ("CW-2," "CW-4," and

"CW-5"), (2) statements of former LifeLock employee Michael Peters, and (3) statements made in filing the corporation's Sarbanes–Oxley certifications. (*See* SCAC ¶¶ 82-91, 108-29, 149-73, 216.) In the initial dismissal Order, the Court concluded that the allegations related to CW-2 (previously identified as "CW-3"), Michael Peters, and the Sarbanes–Oxley certifications failed to sufficiently establish that Defendants intentionally or with deliberate recklessness made a misleading statement concerning LifeLock's or its Wallet application's PCI compliance. (*See* Dec. 17, 2014 Order at 9-12.) Plaintiffs have re-alleged these allegations without amendments and the Court concludes that they fail to raise a strong inference of scienter for the same reasons identified in its previous Order. (*See id.*)

The Court also concludes that the allegations of CW-4 and CW-5 fail to establish that Defendants had actual knowledge or recklessly disregarded LifeLock's or its Wallet application's PCI noncompliance.

> [A] complaint relying on statements from confidential witnesses must pass two hurdles to satisfy the PSLRA pleading requirements. First, the confidential witnesses whose statements are introduced to establish scienter must be described with sufficient particularity to establish their reliability and personal knowledge. Second, those statements which are reported by confidential witnesses with sufficient reliability and personal knowledge must themselves be indicative of scienter.

Zucco Partners, LLC v. Digimarc Corp., 552 F.3d 981, 995 (9th Cir. 2009) (citations omitted). In analyzing the first prong, whether the confidential witnesses have personal knowledge of the events they allege, a court must "look to 'the level of detail provided by the confidential sources, the corroborative nature of the other facts alleged (including from other sources), the coherence and plausibility of the allegations, the number of sources, the reliability of the sources, and similar indicia.' " *Id.* (quoting *In re Daou Sys.*, 411 F.3d at 1015). Here, Plaintiffs describe CW-4 and CW-5 with some "degree of specificity." *See In re Daou Sys.*, 411 F.3d at 1016. The SCAC provides job titles, dates of employment, and the employee to whom the witness reported. (*See* SCAC ¶¶ 149-53, 169-70.) Many of their statements, however, fail to demonstrate the level of detail required to establish personal knowledge of Defendants' alleged state of mind. *See In re Daou Sys.*, 411 F.3d at 1016. Even if some of the SCAC's allegations do reach the "requisite level of particularity to withstand the first prong of the ... confidential witness test," the allegations "fail to demonstrate the deliberate recklessness required to survive the second prong." *See Zucco Partners*, 552 F.3d at 998.

The SCAC alleges that CW-4 worked as Director of Marketing Intelligence at LifeLock from 2007 to 2012 and as Director of Corporate Development from 2012 to May 2014. (SCAC ¶ 149.) CW-4 states that he "was involved in the due diligence conducted for LifeLock's acquisition of Lemon and its Wallet App." (*Id.* ¶ 153.) CW-4 also states that the "due diligence teams gathered their research and data, [then] they presented their findings to the Executive Leadership Board," which included Defendants Davis and Power. (*Id.* ¶ 161.) CW-4 claims that "the fact that the Wallet App was not PCI-compliant came up in discussions with the Executive Leadership Board" and that Defendant Davis was "aware of all the risks of acquiring Lemon." (*Id.* ¶¶ 164-65.) These allegations fail to provide sufficient detail to establish reliability or to be indicative of scienter. CW-4 never alleges that he attended discussions with the Executive Leadership Board and therefore the Court cannot determine whether his knowledge of what occurred at these meetings was based on his personal knowledge or secondhand information. *See Zucco Partners*, 552 F.3d at 996-97. Further, CW-4's allegations that Defendant Davis was "aware of all the risk of acquiring Lemon" and that the Executive Leadership Board "discussed ten to twenty risks involved with the purchase of Lemon" are too vague to create an inference of scienter because they do not specifically allege that PCI noncompliance was ever presented by the due diligence teams to either Defendant Davis or Power. These allegations fail to satisfy the PSLRA pleading requirements because they lack sufficient particularity to establish CW-4's reliability and personal knowledge of Defendants' alleged state of mind.

***8** The SCAC alleges that CW-5 worked as Senior Executive Assistant to LifeLock's Executive Vice President of Corporate Development and Strategy Villi Iltchev and Chief Product Officer Steve Seoane from April 2013 to March 2014. (SCAC ¶ 169.) CW-5 only

alleges that Iltchev and Seoane "were proud that they were able to release [the Wallet App] so fast" and that "Iltchev and the product department were still making sure the app was functioning properly and synching with LifeLock's technology." (*Id.* ¶¶ 171-73.) CW-5's statements fail to reference either Defendant Davis or Power and the Wallet application's compliance with PCI standards. These allegations do not meet the PSLRA pleading requirements because they lack sufficient particularity to establish CW-5's reliability and personal knowledge of Defendants' alleged state of mind. Considering the SCAC's scienter allegations individually and as a whole, they fail to sufficiently allege that Defendants intentionally or with deliberate recklessness made a misleading statement concerning LifeLock's or its Wallet application's compliance with applicable PCI security standards.

3. LifeLock's Technology and Services

In the initial dismissal Order, the Court did not address Defendants' statements concerning LifeLock's technology or services because Plaintiffs argued that only those statements that referenced the FTC Order were false or misleading. (Dec. 17, 2014 Order at 6.) Plaintiffs now argue that Defendants' statements concerning LifeLock's technology and services are themselves "actionable misrepresentations." (Resp. to MTD at 11-12.)

a. SEC Filings

Plaintiffs have re-alleged the following statements from LifeLock's SEC filings as false or misleading statements:

> [A]s part of our consumer services, we offer 24x7x365 member service support. If a member's identity has been compromised, our member service team and remediation specialists will assist the member until the issue has been resolved." [(SCAC ¶¶ 213, 221, 229, 235, 248, 265 (same).)]
>
> ....
>
> **We regularly assess the effectiveness of our information security practices and technical controls.** In addition to regular external audits, we conduct internal security testing to ensure current practices are effective against emerging threats. Additionally, outside penetration tests are conducted on a regular basis. We ensure that our systems are free from critical vulnerabilities by conducting regular vulnerability scans and penetration tests. We also remain aware of publicly disclosed vulnerabilities in commercial and open source products, and remediate issues in a timely manner. [(*Id.* ¶¶ 214, 249 (same).)]
>
> ....
>
> We protect our members by constantly monitoring identity-related events, such as new account openings and credit-related applications. **If we detect that a member's personally identifiable information is being used, we offer notifications and alerts, including proactive near real-time, actionable alerts** that provide our members peace of mind that we are monitoring use of their identity and allow our members to confirm valid or unauthorized identity use. [(*Id.* ¶¶ 215, 220, 228, 234, 264 (same).)]

Plaintiffs argue that these statements are misleading because LifeLock failed to assess the effectiveness of its security practices, was unable to handle the number of alerts it received, and sent out a number of delayed alerts to its customers. (Resp. to MTD at 11-12, 18.) Defendants counter that these statements cannot survive the current Motion because they were alleged in the dismissed CAC and Plaintiffs' previous clarification that only statements referencing the FTC Order still applies to the SCAC. (Doc. 83, Reply in Supp. of MTD ("Reply") at 3-5.) Defendants also argue that even if Plaintiffs were not barred from arguing that these statements are false or misleading, the SCAC fails to allege that LifeLock's service lapses were anything more than quality control issues; therefore, these statements are not actionable as securities fraud. (*Id.* at 4.)

Plaintiffs have failed to sufficiently allege that the statements concerning LifeLock's technology and services are actionable as false or misleading statements under the Exchange Act. The Court cannot conclude that product descriptions in LifeLock's quarterly and annual SEC filings are rendered false or misleading because the Company was unable to consistently deliver "24x7x365" customer service or "near real-time actionable alerts." *See Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 479 (1977) (stating that federal securities laws may not be used to redress mere nondisclosure of corporate mismanagement). As discussed above, the SCAC fails to sufficiently allege the actual extent of LifeLock's

practice of throttling and Plaintiffs have not responded to Defendants' argument that even if thousands of alerts were unsent, this lapse "may have been minuscule in comparison to the number of alerts sent." (*See* MTD at 12 n.24.) Although Plaintiffs argue that mismanagement or improper business practices are sufficient to support a claim for securities fraud where "deception, misrepresentation, or nondisclosure" are alleged, the SCAC fails to sufficiently meet this burden. (Resp. to MTD at 18 (quoting *Santa Fe*, 430 U.S. at 2476).) As discussed above, Defendants made a number of negative disclosures in both LifeLock's 2012 and 2013 Form 10-K. While these SEC filings stated that LifeLock offered "24x7x365" customer service or "near real-time actionable alerts" when describing its product, LifeLock specifically disclosed that it had experienced substantial growth, which has "place[d] a strain on [its] operational, financial, and management infrastructure" and warned that its "failure to effectively manage growth could have a material adverse effect on [its] business ... [and] operating results." (2013 Form 10-K at 18; *see also* Doc. 53-3 2012 Form 10-K at 24 (same).) Based on these disclosures in LifeLock's SEC filings, the Court cannot conclude that Defendants' statements describing their product and services were deceptive or misleading.

b. Advertisements

***9** Plaintiffs have also alleged for the first time that statements made in LifeLock's advertisements are actionable as securities fraud. (*See* Resp. to MTD at 11-12 (citing SCAC ¶¶ 218, 224, 226).) Similar to the statements above from LifeLock's SEC filings, Plaintiffs allege that these advertisements contained false or misleading statements because they misrepresent the capabilities of LifeLock's customer alert and credit monitoring services. (*See* SCAC ¶¶ 219, 225, 227.) Defendants argue that the advertisements alleged in the SCAC cannot support Plaintiffs' Section 10(b) claim because there is no allegation that investors relied on these advertisements, as opposed to the "SEC periodic reports" and "established market communication mechanisms, including regular disseminations of press releases on the national circuits of major newswire services," "communications with the financial press," and "analyst[ ] ... reports," as alleged in the SCAC. (MTD at 7-8 n.13 (quoting SCAC ¶ 284).) Plaintiffs counter that reliance on the advertisements can be presumed because the SCAC alleges a fraud-on-the-market theory of reliance. (Resp. at 11 n.5 (arguing that Plaintiffs relied on "wide-ranging public disclosures," which includes the advertisements at issue); *see also* SCAC ¶ 284.) Plaintiffs also argue that the advertisements alleged in the SCAC are actionable statements because "advertisements can constitute statements made 'in connection with' a securities transaction for purposes of a Section 10(b) claim." (Resp. to MTD at 11-12 (citing *In re Carter-Wallace, Inc., Sec. Lit.*, 150 F.3d 153 (2nd Cir. 1998)).)

The Court cannot conclude that the advertisements identified in the SCAC constitute violations of the Exchange Act. Liability extends to only those false or misleading statements that were made "in connection with" the purchase or sale of securities, and this requirement is satisfied when the statements were made "in a manner reasonably calculated to influence the investing public." *See McGann v. Ernst & Young*, 102 F.3d 390, 393 (9th Cir. 1996) (quoting *Wessel v. Buhler*, 237 F.3d 279, 282 (9th Cir. 1971)). Documents such as press releases, annual reports, and investment prospectuses are typical sources of information used to guide investors. *See United States v. Arthur Young & Co.*, 465 U.S. 805, 810 (1984); *SEC v. Rana Research*, 8 F.3d 1358, 1362 (9th Cir. 1993). Plaintiffs rely solely on the Second Circuit case *In re Carter-Wallace, Inc. Securities Litigation* for the proposition that certain advertisements may also satisfy the connection requirement. In *Carter-Wallace* the Second Circuit concluded that a drug manufacturer's detailed advertisements that "us[ed] technical jargon and [were] published in sophisticated medical journals" may satisfy the "in connection with" requirement. *Carter-Wallace*, 150 F. 13d at 156-57 (noting that "[i]n an economy that produces highly sophisticated products, technical information is of enormous importance to financial analysts"). The court specifically stated that "[t]echnical advertisements in sophisticated medical journals detailing the attributes of a new drug could be highly relevant to analysts evaluating the stock of the company marketing the drug" and therefore the plaintiffs had met their burden of alleging the "in connection with" element in that case. *Id.* at 156. The SCAC fails to provide sufficient factual allegations demonstrating that reasonable investors would base their investment decisions on the advertisements in this case. As presented in the SCAC, the advertisements have little in common with both the types of communications typically relied upon by investors and the advertisements alleged

in *Carter-Wallace.* The SCAC contains no allegations describing in which publications the advertisements appeared and, specifically, whether they appeared in publications reasonably used by market professionals to evaluate LifeLock stock. Plaintiffs have failed to sufficiently allege that the advertisements meet the "in connection with" element in alleging a violation of the Exchange Act.

4. Whistleblower Complaints

Plaintiffs also argue that the SCAC sufficiently alleges that Defendants made false or misleading statements concerning "whistleblower" claims filed against LifeLock. (Resp. to MTD at 2, 15.) [5] Plaintiffs specifically argue that the following statements were false or misleading:

> On January 17, 2014, we met with FTC Staff, at our request, to discuss issues regarding allegations that have been asserted in a whistleblower claim against us relating to **our compliance with the FTC Order.** Following this meeting, we expect to receive either a formal or informal investigatory request from the FTC for documents and information regarding our policies, procedures, and practices for our services and business activities. Given the heightened public awareness of data breaches and well as attention to identity theft protection services like ours, it is also possible that the FTC, at any time, may commence an unrelated inquiry or investigation of our business practices and our compliance with the FTC Order. **We endeavor to comply with all applicable laws and believe we are in compliance with the requirements of the FTC Order.** We believe the increased regulatory scrutiny will continue in our industry for the foreseeable future and could lead to additional meetings or inquiries or investigations by the agencies that regulate our business, including the FTC. [(SCAC ¶ 239 (quoting LifeLock's 2013 Form 10-K).)]
>
> ***10** ....
>
> **[W]e pro-actively requested and met with the FTC in January of this year to discuss some acquisitions [sic] that had been made by terminated employee. It's important to understand that we have then settled that matter favorably for LifeLock with the former employee and that former employee has now come back and agreed that we were not violating any laws for the term of the agreement with the FTC.** [(*Id.* ¶ 257 (quoting a statement made by Defendant Davis during an Investor and Analyst Day).)]

Plaintiffs also argue that the DBMR analyst reported that LifeLock "ha[d] settled a whistleblower lawsuit filed with the FTC by an ex-employee of the company for a modest amount, in the last month." (*Id.* ¶ 255.) Plaintiffs argue that these statements are false or misleading because they misrepresent the "number and status of 'whistleblower' claims against the Company." (*Id.* ¶ 240(c).) Plaintiffs specifically argue that although a former employee had settled his wrongful termination lawsuit in February 2014, a second former employee had filed complaints with the FTC and SEC and a whistleblower complaint under the Sarbanes–Oxley Act with the Department of Labor in August 2013, which had not been settled at the time the statements were made. (*Id.* ¶¶ 81-82, 256(a)-(b), 259.)

The SCAC fails to sufficiently allege that the above statements are false because there are no allegations that LifeLock asserted that the whistleblower complaint referenced in each statement was the only complaint that had been filed against LifeLock. The Court also concludes that while the above statements fail to disclose the exact number of whistleblower complaints filed against LifeLock, they were not plausibly misleading because LifeLock disclosed in its 2013 Form 10-K that "there ha[d] been a recent increase in whistleblower claims made to regulatory agencies, including whistleblower claims made by former employees, which [LifeLock] believe[d] w[ould] likely continue." (2013 Form 10-K at 10.) Omitting specific details such as the number of whistleblower complaints made against LifeLock was not an omission that "affirmatively created an impression of a state of affairs that differs in a material way from the one that actually exists." *Brody*, 280 F.3d at 1006. Because the omission of the specific number of whistleblower complaints faced did not plausibly render the above statements misleading, these statements are not sufficient to state a claim for securities fraud.

III. CONCLUSION

The SCAC does not adequately allege that the statements at issue were either misleading or made with scienter to violate Section 10(b) or Rule 10b-5. Because the Complaint in this case has been amended twice and Plaintiffs' Response does not indicate that further amendment would cure the deficiencies identified, further leave to amend is not warranted.

***11 IT IS ORDERED** granting Defendants' Motion to Dismiss Second Consolidated Amended Class Action Complaint for Violations of Federal Securities Laws (Doc. 77).

IT IS FURTHER ORDERED denying the Request for Judicial Notice in Support of Defendants' Motion to Dismiss Second Consolidated Amended Class Action Complaint for Violations of Federal Securities Laws (Doc. 79).

IT IS FURTHER ORDERED directing the Clerk to enter judgment dismissing Plaintiffs' Second Consolidated Amended Class Action Complaint for Violations of Federal Securities Laws.

All Citations

Not Reported in Fed. Supp., 2015 WL 12819154

Footnotes

1 Defendants also argue that the SCAC fails to adequately plead that any economic loss was caused by Defendants' allegedly false or misleading statements. (MTD at 27); *see also Halliburton Co. v. Erica P. John Fund, Inc.*, 134 S. Ct. 2398, 2407 (2014) (outlining the elements necessary to state a claim under Section 10(b) of the Exchange Act). Because the Court concludes that the SCAC fails to adequately plead falsity and scienter, the Court does not reach the issue of whether the SCAC adequately pleads loss causation.

> The parties dispute whether the Court can take judicial notice of an online news article written by Jon C. Ogg for the website *24/7 Wall St.* that is referenced in the SCAC. (*See* Doc. 79, Req. for Judicial Notice at 2 (citing SCAC ¶ 271); Doc. 82, Resp. to Req. for Judicial Notice at 1.) Defendants request that the Court consider the entire online article, arguing that the article is properly noticeable under the incorporation by reference doctrine because it is quoted and necessarily relied upon in the SCAC. (Req. for Judicial Notice at 2-3.) Even if the Court were to consider the entire online article for the truth of its factual content, the portions of the article not cited in the SCAC are not relevant to the Court's determination of whether Plaintiffs have stated a legal claim. The Court therefore denies Defendants' judicial notice request.

2 The *Omnicare* opinion provides a straightforward example: if a speaker states that he believes his conduct is lawful but has failed to consult a lawyer before making this statement, it could be actionable as a misleading opinion statement. *Omnicare*, 135 S. Ct. at 1328.

3 LifeLock's SEC filings are properly noticeable because they "are matters of public record and are capable of accurate and ready determination." (Dec. 17, 2014 Order at 2-3.)

4 Plaintiffs also allege throughout the SCAC that certain statements were made with scienter because they related to matters that were part of LifeLock's "core operations." (*See, e.g.*, SCAC ¶¶ 225(g), 252(j), 259(h).) It is unclear from the SCAC whether Plaintiffs allege that PCI compliance is part of LifeLock's core operations. Because Plaintiffs only argue that LifeLock's compliance with the FTC Order is part of its core operations, the Court will not address the "core operations" theory of scienter for those statements related to PCI compliance. (*See* Resp. to MTD at 27-28.)

5 The SCAC alleges that LifeLock misrepresented the number of "whistleblower" claims against the company; however, former employee Stephen Burke filed a complaint against LifeLock alleging wrongful termination and invoked no whistleblower provisions. (*See* SCAC ¶¶ 71-83.)

2016 WL 4157358
NOT FOR PUBLICATION
United States District Court, D. Arizona.

Miguel AVILA, et al., Plaintiffs,
v.
LIFELOCK INCORPORATED, et al., Defendants.

No. CV-15-01398-PHX-SRB
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Signed 08/03/2016

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ORDER

Susan R. Bolton, United States District Judge

***1** The Court now considers Defendants' Motion to Dismiss Amended Class Action Complaint ("MTD") (Doc. 56).[1] The Court heard oral argument on this Motion on May 2, 2016. (Doc. 71, Minute Entry.)

I. BACKGROUND

This is a securities fraud class action brought on behalf of purchasers of Defendant LifeLock Incorporated ("LifeLock") common stock or call options and sellers of LifeLock's publicly traded put options, who purchased or sold their stock or options between July 30, 2014 and July 21, 2015 ("the class period"). (Doc. 48, Am. Class Action Compl. ("CAC") ¶ 1.) LifeLock "provides identity theft protection services for consumers and risk management services for enterprise clients." (*Id.* ¶ 2.) Defendants Todd Davis and Chris Power ("Individual Defendants") were executives of LifeLock during the class period. (*Id.* ¶¶ 34-35.)

The CAC alleges that Defendants violated the Securities Exchange Act of 1934 ("the Exchange Act") during the class period by making false or materially misleading statements concerning the effectiveness of LifeLock's identity theft protection services and its compliance with applicable payment card industry security standards. (*Id.* ¶¶ 79-111, 119-22.) The CAC also alleges that Defendants made statements misrepresenting the scope and severity of an FTC investigation into LifeLock's compliance with a 2010 FTC Settlement Order ("2010 FTC Order"), which expressly prohibited LifeLock from misrepresenting the methods and effectiveness of its services. (*Id.* ¶¶ 135-47.) Plaintiffs allege that these misleading statements allowed LifeLock to artificially maintain the price of its common stock and call options throughout the class period. (*Id.* ¶ 166.) Plaintiffs further allege that once investors learned of the severity of the FTC investigation and that LifeLock had failed to provide its services as advertised and failed to comply with the applicable security standards, the price of common stock and call options significantly declined, and the price of put options significantly rose. (*Id.* ¶¶ 166-71.) The CAC contains two counts: (1) violation of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, against all Defendants, and (2) violation of Section 20(a) of the Exchange Act, against Individual Defendants. (*Id.* ¶¶ 185-99.) Defendants now move to dismiss the CAC, arguing that Plaintiffs have failed to adequately state a claim arising under Section 10(b) and Rule 10b-5. Defendants specifically argue that the CAC fails to adequately plead that Defendants made a false or misleading statement or that any of Defendants' allegedly false or misleading statements were made with scienter. (MTD at 16-35.)

II. LEGAL STANDARDS AND ANALYSIS

***2** Rule 12(b)(6) dismissal for failure to state a claim can be based on either (1) the lack of a cognizable legal theory or (2) insufficient facts to support a cognizable legal claim. *Conservation Force v. Salazar*, 646 F.3d 1240, 1242 (9th Cir. 2011), *cert. denied*, *Blasquez v. Salazar*, 132 S. Ct. 1762 (2012). In determining whether an asserted claim can

be sustained, "[a]ll of the facts alleged in the complaint are presumed true, and the pleadings are construed in the light most favorable to the nonmoving party." *Bates v. Mortg. Elec. Registration Sys., Inc.*, 694 F.3d 1076, 1080 (9th Cir. 2012). "[A] well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof of those facts is improbable, and 'that a recovery is very remote and unlikely.' " *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 556 (2007) (quoting *Scheuer v. Rhodes*, 416 U.S. 232, 236 (1974)). However, "for a complaint to survive a motion to dismiss, the nonconclusory 'factual content,' and reasonable inferences from that content, must be plausibly suggestive of a claim entitling the plaintiff to relief." *Moss v. U.S. Secret Serv.*, 572 F.3d 962, 969 (9th Cir. 2009) (quoting *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009)). In other words, the complaint must contain enough factual content "to raise a reasonable expectation that discovery will reveal evidence" of the claim. *Twombly*, 550 U.S. at 556.

Section 10(b) or Rule 10b-5 claims also must meet the particularity requirements of Federal Rule of Civil Procedure 9(b), which requires that "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." Fed. R. Civ. P. 9(b); *see also In re Daou Sys., Inc. Sec. Litig.*, 411 F.3d 1006, 1014 (9th Cir. 2005). Moreover, these claims must meet the heightened pleading standards of the Private Securities Litigation Reform Act ("PSLRA"). *See* 15 U.S.C. § 78u-4. The PSLRA requires a securities fraud complaint to "plead with particularity both falsity and scienter." *Gompper v. VISX, Inc.*, 298 F.3d 893, 895 (9th Cir. 2002). To properly allege falsity, a complaint must "specify each 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, ... state with particularity all facts on which that belief is formed." *Id.* (quoting 15 U.S.C. § 78u-4(b)(1)) (quotation marks omitted). To adequately plead scienter, the complaint must "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). To adequately demonstrate that the "defendant acted with the required state of mind," a complaint must "allege that the defendants made false or misleading statements either intentionally or with deliberate recklessness." *In re Daou Sys.*, 411 F.3d at 1014-15. "[A]n actor is [deliberately] reckless if he had reasonable grounds to believe material facts existed that were misstated or omitted, but nonetheless failed to obtain and disclose such facts although he could have done so without extraordinary effort." *In re Oracle Corp. Sec. Litig.*, 627 F.3d 376, 390 (9th Cir. 2010) (quoting *Howard v. Everex Sys., Inc.*, 228 F.3d 1057, 1064 (9th Cir. 2000)). The Supreme Court has emphasized that courts "must review 'all the allegations holistically' " when determining whether scienter has been sufficiently pled. *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 49 (2011) (quoting *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 326 (2007)). The relevant inquiry is "whether all of the facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegation, scrutinized in isolation, meets that standard." *Tellabs*, 551 U.S. at 323. In securities cases, falsity and scienter "are generally strongly inferred from the same set of facts" and the two requirements may be combined into a unitary inquiry under the PSLRA." *Ronconi v. Larkin*, 253 F.3d 423, 429 (9th Cir. 2011).

A. "Proactive" and "Near Real-Time" Alert Services

***3** Plaintiffs allege that Defendants have made a number of misleading or false statements during the class period concerning LifeLock's ability to provide its customers with "proactive" and "near real-time" alert services to prevent identity theft transactions. (CAC ¶¶ 79-111.) Plaintiffs claim that Defendants made such statements in LifeLock's SEC filings, at investor conferences, and on LifeLock's website. (*Id.*)[2] Even if the Court were to conclude that the statements identified in the CAC concerning LifeLock's alert services are false or misleading, Plaintiffs have failed to adequately plead that the statements were made with scienter. *See* 15 U.S.C. § 78u-4(b)(2) (requiring scienter to be pled "with respect to each act or omission alleged to violate this chapter"). For each of the relevant statements, Plaintiffs allege that Individual Defendants "knew, or with deliberate recklessness disregarded," that LifeLock failed to send out "proactive" or "near real-time" alerts to customers. (CAC ¶ 177.) The CAC relies on the following to support this proposition: (1)a PowerPoint entitled "Project Granite" that was presented to "LifeLock executives" in March 2015; (2) statements of four confidential witnesses ("CW 1," "CW 2," "CW 3," and "CW 4"); (3) statements of former LifeLock employees Michael Peters and Stephen Burke; and (4) an allegation that the false or misleading statements were related to matters that were part of LifeLock's "core operations." (*Id.* ¶¶ 51-61, 73-77, 112-18,

172-73; Doc. 67, Resp. in Opp'n to MTD ("Resp.") at 21-28.)[3] Considering these allegations both individually and collectively, they fail to sufficiently allege that the statements at issue were made with scienter.

The allegation concerning Project Granite fails to indicate that Individual Defendants had contemporaneous knowledge of or recklessly disregarded a failure on LifeLock's part to provide "proactive" or "near real-time alerts" when such statements were made. Plaintiffs allege that Project Granite was presented to "LifeLock's executives" in March 2015, eight months into the class period. (CAC ¶ 113.) Plaintiffs claim that during this presentation the Director of Design and User Experience told LifeLock executives that LifeLock's alerts were "stale" because banks and credit card companies were capable of sending out alerts that reached their customers before LifeLock's alerts. (*Id.*) This single allegation fails to specifically state that Individual Defendants were present for the Project Granite presentation and therefore does not indicate that they had firsthand knowledge of its content. *See In re Cadence Design Sys., Inc. Sec. Litig.*, 654 F. Supp. 2d 1037, 1048-49 (N.D. Cal. 2009) (stating a plaintiff must allege facts establishing a strong inference that defendants were likely to know firsthand the facts that put them on notice of the falsity of the relevant statements). Even so, the CAC contains no allegations concerning the length of the delay between the time a customer received an alert from her bank or credit card company and an alert from LifeLock. Specifically, there are no allegations that this delay was so significant that it necessarily rendered LifeLock's alerts insufficient to allow customers to "proactively" protect their identities or that the alerts were not sent in "near real time." Because Plaintiffs have not sufficiently alleged that the information presented in Project Granite demonstrates that LifeLock's alerts did not allow its customers to "proactively" protect their identities or were not sent in "near real time," these allegations fail to indicate the statements at issue were made with scienter.

***4** The allegations of the confidential witnesses also fail to establish that Individual Defendants had contemporaneous knowledge of or recklessly disregarded LifeLock's failure to provide "proactive" or "near real-time alerts" when such statements were made. *See Berson v. Applied Signal Technology, Inc.*, 527 F.3d 982, 989 (9th Cir. 2008) (stating that the PSLRA demands "particular allegations which strongly imply Defendants' *contemporaneous* knowledge that the statement was false when made" (internal quotation marks and alteration omitted)).

> [A] complaint relying on statements from confidential witnesses must pass two hurdles to satisfy the PSLRA pleading requirements. First, the confidential witnesses whose statements are introduced to establish scienter must be described with sufficient particularity to establish their reliability and personal knowledge. Second, those statements which are reported by confidential witnesses with sufficient reliability and personal knowledge must themselves be indicative of scienter.

Zucco Partners, LLC v. Digimarc Corp., 552 F.3d 981, 995 (9th Cir. 2009) (citations omitted). In analyzing the first prong, whether the confidential witnesses have personal knowledge of the events they allege, a court must "look to 'the level of detail provided by the confidential sources, the corroborative nature of the other facts alleged (including from other sources), the coherence and plausibility of the allegations, the number of sources, the reliability of the sources, and similar indicia.' " *Id.* (quoting *In re Daou Sys.*, 411 F.3d at 1015). Here, Plaintiffs describe the confidential witnesses with some "degree of specificity." *See In re Daou Sys.*, 411 F.3d at 1016. The CAC provides job titles, dates of employment, and the employee to whom the witness reported. (*See* CAC ¶¶ 74-77.) Many of their statements, however, fail to demonstrate the level of detail required to establish personal knowledge of Defendants' alleged state of mind. *See In re Daou Sys.*, 411 F.3d at 1016. Even if some of the CAC's allegations do reach the "requisite level of particularity to withstand the first prong of the ... confidential witness test," the allegations "fail to demonstrate the deliberate recklessness required to survive the second prong." *See Zucco Partners*, 552 F.3d at 998.

The CAC alleges that CW 1 was Director of Mobile Product Management at LifeLock from August 2014 to April 2015 and reported to the Vice President of Products. (CAC ¶ 74.) It also alleges that CW 1 "took ownership of the Company's mobile products and applications," "has personal knowledge about customer alerts sent through

the mobile platform," and was told that Project Granite was presented to LifeLock's senior management. (*Id.*) There are no allegations that CW 1 interacted with any Individual Defendant; therefore, the CAC does not establish that CW 1 had firsthand knowledge of whether Individual Defendants were aware that LifeLock's alerts were not "proactive" or were not being sent in "near real time." *See Zucco Partners*, 552 F.3d at 998 (stating that even a confidential witness's "generalized claims about corporate knowledge are not sufficient to create a strong inference of scienter, since they fail to establish that the witness reporting them has reliable personal knowledge of the defendants' mental state"); *Karpov v. Insight Enters., Inc.*, No. CV 09-856-PHX-SRB, 2010 WL 2105448, at *8-9 (D. Ariz. Apr. 20, 2010) (concluding that because the CAC "does not set forth the basis for the CWs' firsthand knowledge of the state of mind of the [defendants]," their statements do not establish an inference of scienter on the part of the defendants). These allegations fail to satisfy the PSLRA pleading requirements because they lack sufficient particularity to establish CW 1's personal knowledge of Defendants' alleged state of mind.

***5** The CAC alleges that CW 4 was a Partner Operations Implementation Analyst at LifeLock from 2007 to October 2014. (CAC ¶ 77.) It also alleges that during CW 4's employment he "had personal knowledge about LifeLock's customer alert practices, including throttling" and "had direct conversations with Defendant Davis to discuss LifeLock's internal systems issues." (*Id.*) The allegation that CW 4 at some point discussed LifeLock's "internal systems issues" with Defendant Davis fails to provide sufficient detail to establish reliability or to be indicative of scienter. There is no indication of when CW 4 spoke with Defendant Davis about LifeLock's "internal systems issues" and, specifically, there is no particular allegation that CW 4 had any discussion with Defendant Davis about such issues during the class period. *See Zucco Partners*, 552 F.3d at 997. Further, the phrase "internal systems issues" is too vague to create an inference of scienter because it does not establish that CW 4 specifically discussed with Defendant Davis whether LifeLock alerts were "proactive" or issued in "near real time." These allegations fail to satisfy the PSLRA pleading requirements because they lack sufficient particularity to establish CW 4's reliability and personal knowledge of Defendants' alleged state of mind.

The allegations concerning CW 2, CW 3, and former LifeLock employees Burke and Peters also fail to meet the PSLRA's scienter pleading requirements. The CAC alleges that CW 2 was a Senior Financial Analyst at LifeLock from June 2012 through January 2014, and that CW 3 was the Vice President of Marketing at LifeLock from 2007 to October 2011. (*Id.* ¶¶ 75-76.) It also alleges that Burke was employed as a Senior Financial Analyst and Cross Business Analytics Analyst from February 2010 to March 2013, and that Peters was employed as Chief Information Security Officer until July 2013. (*Id.* ¶¶ 14-15.) CW 2, CW 3, Peters, and Burke all left LifeLock before the class period began and, therefore, information they have about the effectiveness of LifeLock's alerts or Individual Defendant's knowledge of the alerts during the class period is necessarily secondhand and thus "does not provide the requisite particularity to establish that certain statements of these confidential witnesses are based on the witnesses' personal knowledge." *Zucco Partners*, 552 F.3d at 996 (concluding that two confidential witnesses who were not employed during the class period "have only second-hand information about accounting practices at the corporation during that year"); *see also Shurkin v. Golden State Warriors*, 471 F. Supp. 2d 998, 1015 (N.D. Cal. 2006) ("CW3's employment ended before the Class Period and thus, CW3 lacks any personal knowledge as to the [defendant's] production activity during the [time period] that is at issue here."). These allegations do not meet the PSLRA pleading requirements because they lack sufficient particularity to establish the confidential witnesses', Peters', and Burke's reliability and personal knowledge of Defendants' alleged state of mind. Considering the CAC's scienter allegations individually and as a whole, they fail to sufficiently allege that Defendants intentionally or with deliberate recklessness made a misleading statement concerning the effectiveness of LifeLock's alerts. [4]

B. Payment Card Industry Data Security Standard Compliance

Plaintiffs also allege that Defendants have made false or misleading statements concerning LifeLock's compliance with "the highest standards of data security applicable to major financial institutions, which is known as Level 1 of the Payment Card Industry Data Security Standard ('PCI DSS')." (CAC ¶ 120.) [5] Plaintiffs specifically claim that Defendant Davis made the following false or misleading statement at an investor conference in response to a

Deutsche Bank analyst's question concerning LifeLock's data security: "[O]f course we're going to look to operate under the highest data handling and data security standards, PCI Level 1, for our core business, right? That's how we're going to make sure that we operate ...." (*Id.* ¶ 121 (quoting Defendant Davis at the September 9, 2014 Deutsche Bank Technology Conference).) Plaintiffs also allege that throughout the class period LifeLock's website listed the following false or misleading statement under a heading entitled "Our Credentials": "Level 1 compliant under the Payment Card Industry Data Security Standard." (*Id.* ¶ 122.) Plaintiffs claim that these statements were false because LifeLock did not have adequate data security protection and, specifically, failed to "comply with PCI DSS Level 1 requirements at all relevant times." (*Id.* ¶ 123(d).)

***6** Even if the Court were to conclude that the statements identified in the CAC concerning LifeLock's PCI DSS Level 1 compliance were actionable statements under the PSLRA, Plaintiffs have failed to adequately plead that the statements were made with scienter. The CAC relies on the following to support Plaintiffs' proposition that Individual Defendants knew or recklessly disregarded LifeLock's failure to comply with the PCI DSS Level 1 standards: (1) statements of CW 2, CW 3, and CW 4; and (2) statements of former LifeLock employee Peters. (*Id.* ¶¶ 124-34.) As stated above, CW 2, CW 3, and Peters all left LifeLock before the class period began and, therefore, they have only secondhand information about LifeLock's compliance with the PCI DSS Level 1 requirements during the relevant time period. The CAC also contains no allegations that demonstrate CW 4 interacted with an Individual Defendant during the class period in such a way that would establish his personal knowledge of Individual Defendants' alleged state of mind concerning LifeLock's Level 1 compliance. (*See id.* ¶¶ 130-34.) Further, Defendants argue, and Plaintiffs do not dispute, that LifeLock received PCI DSS Level 1 certification for its enterprise business in June 2014 and its consumer business in July 2014. (*See* MTD at 27 n.33; *see also* Doc. 57-1, Ex. 1, 2014 Form 10-K at 13.) The Court concludes that LifeLock's receipt of Level 1 certification shortly before the class period began further negates any inference of scienter for the two statements identified in the CAC concerning LifeLock's PCI compliance. The CAC's scienter allegations fail to sufficiently allege that Defendants intentionally or with deliberate recklessness made a misleading statement concerning LifeLock's compliance with the PCI DSS Level 1 standard.

C. FTC Investigation

Plaintiffs also allege that Defendants have made material misrepresentations and omissions concerning the FTC's investigation into LifeLock's compliance with the 2010 FTC Order prohibiting LifeLock from misrepresenting the effectiveness of its services. (CAC ¶¶ 135-54.) Plaintiffs claim that Defendants made such misrepresentations in LifeLock's SEC filings, at investor conferences, in a press release, and during an earnings call. (*Id.* ¶¶ 138-44, 148-50.)[6] Plaintiffs allege that the statements detailed in the CAC were misleading because they downplayed the scope and severity of the FTC's investigation. Plaintiffs specifically allege that "Defendants knew that the FTC was not merely engaged in an innocent 'dialogue' or non-threatening 'inquiry,' or looking at LifeLock as part of an industry-wide, run-of-the-mill regulatory surveillance program." (*Id.* ¶ 145.) Rather, Plaintiffs argue, Defendants should have disclosed that "the FTC was formally investigating the Company in connection with the contemplated filing of a motion to hold LifeLock in contempt for violating the FTC Order." (*Id.*; *see also id.* ¶ 154.) Defendants counter that they did, in fact, disclose the FTC's investigation into LifeLock in its 2013 Form 10-K and throughout the class period continued to disclose the development of the investigation and warned investors of its possible effects on LifeLock's business operations. (MTD at 20-25.) Defendants argue that these disclosures adequately addressed the scope and severity of the FTC's investigation into LifeLock and, therefore, the statements identified in the CAC are not false or misleading when considered in context. (*Id.*)

The Court concludes that, in light of LifeLock's numerous disclosures made prior to and throughout the class period concerning the FTC's investigation into its operations, Plaintiffs have failed to sufficiently allege any misstatement or omission concerning the severity or scope of the investigation. On February 19, 2014, five months prior to the class period, LifeLock disclosed that there had been a whistleblower claim against the company related to its compliance with the 2010 FTC Order, that it was expecting to receive "a formal or informal investigatory request from the FTC for documents and information," and that at any time the FTC may commence an "inquiry or investigation of ... [LifeLock's]

compliance with the FTC Order." (CAC ¶ 137.) On March 17, 2014, LifeLock filed a Form 8-K and reported that on March 13, 2014 the company had received "a request from the FTC for documents and information related to LifeLock's compliance with the [2010 FTC Order]." (Doc. 57-4, Ex. 4, Mar. 17, 2014 Form 8-K Excerpt.) On July 31, 2014, LifeLock filed its second quarter 10-Q and reiterated that there had been allegations against the company concerning its compliance with the FTC Order and that in March 2014 the FTC had requested it submit documents related to LifeLock's compliance with the FTC Order. (Doc. 57-5, 2Q 2014 Form 10-Q Excerpt at 32.) LifeLock stated that it had submitted a portion of the requested information and was working on both completing its response to the FTC's request for information and preparing a response to a subsequent request for clarification on the information it had previously submitted. (*Id.*) LifeLock went on to describe the possible consequences of and penalties if the FTC were to determine that LifeLock was not in compliance with the terms of the 2010 FTC Order and the investigation's potential effects on LifeLock's business operations:

> ***7** A determination that we are in violation of the FTC Order, including as a result of the FTC's review of our information security programs and alert and notification processing or our PCI non-compliance in connection with the LifeLock Wallet mobile application, could result in liability for fines, damages, or other penalties or require us to make changes to our services and business practices, and cause us to lose customers, any of which could have a material adverse impact on our business, operating results, financial condition, and prospects.

(*Id.*) LifeLock referred to these disclosures in its third quarter 10-Q filed on November 10, 2014. (Doc. 57-6, Ex. 6, 3Q 2014 10-Q Excerpt.) On February 4, 2015, LifeLock filed its 2014 Form 10-K and disclosed that it had completed the FTC's request for information and on January 5, 2015 it had completed its response to the FTC's subsequent requests for clarification of certain information previously submitted. (2014 Form 10-K at 11.) LifeLock also disclosed that on February 4, 2015, it had made a $20 million settlement offer to the FTC, but advised that there was no guarantee that LifeLock could settle the inquiry for $20 million, if at all. (*Id.*) LifeLock again disclosed additional possible penalties that it may incur and the potential effects on LifeLock's business operations if the FTC were to conclude that LifeLock was not operating in compliance with the 2010 FTC Order. (*Id.*) In light of LifeLock's disclosures of the progress of the FTC's investigation and its possible adverse consequences, the Court concludes that Plaintiffs have failed sufficiently allege that Defendants misrepresented the scope or severity of the investigation and have failed to identify any undisclosed information that would have altered the "total mix" of information available to investors. *See Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988)). Because the Court concludes that Plaintiffs have failed to show that LifeLock's statements concerning the scope and severity of the FTC's investigation were misleading, it need not address the issue of scienter concerning these statements.

III. CONCLUSION

The Court grants Defendants' Motion to Dismiss because the CAC does not adequately allege that the statements concerning LifeLock's alert services and PCI DSS Level 1 compliance were made with scienter, and it fails to sufficiently allege that the statements concerning the scope and severity of the FTC's investigation were misleading. Count One of the CAC is dismissed against all Defendants. Count Two is also dismissed because a violation of Section 20(a) of the Exchange Act, which provides for liability for "controlling" persons, requires a predicate violation of Section 10(b). *See* 15 U.S.C. § 78t(a); *Zucco Partners*, 552 F.3d at 990. As the Complaint in this case has only been amended once and because of the liberal policy in favor of amendment embodied in Federal Rule of Civil Procedure 15(a), the Court will grant the Motion to Dismiss but allow Plaintiffs to seek leave to amend no later than 21 days from the date of this Order. *See, e.g.*, *Mark H. v. Lemahieu*, 513 F.3d 922, 939-40 (9th Cir. 2008) (citing *Verizon Del., Inc. v. Covad Commc'ns Co.*, 377 F.3d 1081, 1091 (9th Cir. 2004)). Plaintiffs are instructed to follow the applicable local and procedural rules governing amended pleadings in seeking leave to amend. *See* Fed. R. Civ. P. 15; LRCiv 15.1.

IT IS ORDERED granting Defendants' Request for Judicial Notice ISO Motion to Dismiss Amended Class Action Complaint (Doc. 58).

IT IS FURTHER ORDERED granting Defendants' Motion to Dismiss Amended Class Action Complaint (Doc. 56).

***8** Dated this 3rd day of August, 2016.

All Citations

Not Reported in Fed. Supp., 2016 WL 4157358, Fed. Sec. L. Rep. P 99,260

Footnotes

1 In deciding this Motion, the Court considered the contents of the Amended Class Action Complaint and Defendants' exhibits submitted with their Motion. The Court concludes, and Plaintiffs do not dispute, that these exhibits are properly noticeable on a motion to dismiss because they are either incorporated by reference in the Amended Class Action Complaint or are "matters of public record." (*See* Doc. 58, Defs.' Req. for Judicial Notice); *Lee v. City of L.A.*, 250 F.3d 668, 688-89 (9th Cir. 2001).

2 The CAC emphasizes some of the excerpts in bold typeface, which Plaintiffs state is meant to indicate the false or misleading statement. (CAC ¶ 79 n.2.)

3 Plaintiffs also attached a document entitled "Joint Declaration of Hank Bates and Michael W. Sobol in Support of Plaintiffs' Motion for Preliminary Approval of Class Action Settlement," which was filed by the plaintiffs' counsel in *Ebarle v. LifeLock, Inc.*, No. 3:15-cv-00258-HSG (N.D. Cal.). (*See* Doc. 68-1, Ex. A, Decl. of Bates and Sobol.) Plaintiffs argue the statements within this declaration also support an inference of scienter and that it is proper for the Court to consider these allegations that are not contained within the CAC because the declaration is a "matter[ ] of public record." (Resp. at 1 n.3.) By arguing that the Court can infer scienter from the statements within this declaration, however, Plaintiffs' appear to seek judicial notice of the truth of the document's contents. Doing so would be inappropriate in the context of a motion to dismiss under Rule 12(b)(6); therefore, the Court will not consider the substance of the joint declaration. *See Lee*, 250 F.3d at 690 (stating that a court may not take judicial notice of disputed facts stated within public records); *see also In re Am. Apparel, Inc. S'holder Litig.*, 855 F. Supp. 2d 1043, 1064 (C.D. Cal. 2012).

4 Plaintiffs also argue that scienter may be imputed in this case under the "core operations" doctrine. (Resp. at 30-31.) Because the Court concludes that the CAC does not contain other detailed allegations concerning Individual Defendants' exposure to the relevant factual information within LifeLock, the core operations inference is insufficient to establish scienter in this case. *South Ferry LP, No. 2 v. Killinger*, 542 F.3d 776, 784-85 (9th Cir. 2008) (stating that in the absence of other particularized supporting allegations of scienter, the "core operations" inference, by itself, is insufficient).

5 Plaintiffs also allege that Defendants made false or misleading statements concerning LifeLock's general ability to provide "a high level of data security protection" for its customers. (CAC ¶ 119.) The CAC fails to identify any specific statement made by Defendants concerning LifeLock's ability to provide "a high level of data security protection," and instead only identifies statements concerning LifeLock's PCI DSS compliance. *See* 15 U.S.C. 78u-4(b)(1)(B) (requiring a plaintiff to "specify each statement alleged to have been misleading). Accordingly, the Court will only consider those statements related to LifeLock's compliance with the PCI DSS Level 1 standard.

6 Plaintiffs have alleged that Defendants made a false and misleading statement in LifeLock's 2013 Form 10-K. (*See* CAC ¶ 137.) Because courts in the Ninth Circuit have routinely concluded that statements made outside of the class period are not themselves actionable, the Court will not consider whether Defendants are liable for an alleged false or misleading statement made in LifeLock's 2013 Form 10-K. *See, e.g., In re Clearly Canadian Sec. Litig.*, 875 F. Supp. 1410, 1420 (N.D. Cal. 1995); *Teamsters Local 617 Pension & Welfare Funds v. Apollo Grp., Inc.*, No. CIV 06-02674-PHX-RCB, 2011 WL 1253250, at *32 (D. Ariz. Mar. 31, 2011); *In re Applied Micro Circuits Corp. Sec. Litig.*, No. 01-CV-0649 KK AJB, 2002 WL 34716875, at *10 (S.D. Cal. Oct. 4, 2002). The Court also concludes that Plaintiffs' general allegation that "Defendants used various forms of the quoted language" from LifeLock's 2013 Form 10-K throughout the class period is insufficient to meet the PSLRA pleading requirements. (*See* CAC ¶ 138); 15 U.S.C. 78u-4(b)(1)(B).

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NOT FOR PUBLICATION
United States District Court, D. Arizona.

Miguel AVILA, et al., Plaintiffs,
v.
LIFELOCK INCORPORATED, et al., Defendants.

No. CV-15-01398-PHX-SRB
|
Signed 08/21/2017

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ORDER

Susan R. Bolton, United States District Judge

***1** At issue is Defendants' Motion to Dismiss Second Amended Class Action Complaint ("MTD") (Doc. 97). [1] The Court heard oral argument on this Motion on May 15, 2017. (Doc. 112, Minute Entry.)

I. BACKGROUND

The facts of this case have been summarized in a previous Order that is fully incorporated herein. (Doc. 80, Aug. 3, 2016 Order at 1-2.) Since their previous amended complaint was dismissed, Plaintiffs have added Hilary A. Schneider, President of LifeLock Inc. during the Class Period, as an individual Defendant to their Complaint. (Doc. 89, Second Amended Class Action Complaint ("SAC") ¶ 32). In the SAC, Plaintiffs have bolstered their allegations with statements from Confidential Witnesses 5 and 6 ("CW 5", "CW 6"). (*Id.* ¶¶ 82-83.) CW 5 was an Identity Alert Specialist with LifeLock from July 2007 to June 2015. (*Id.* ¶ 82.) Plaintiffs allege that CW 5 had knowledge of Defendants' scienter regarding the staleness rate of credit check alerts. (*Id.*) CW 6 was a Team Manager of Escalations and Identity Operations employed by LifeLock from July 2014 until February 2016 whom Plaintiffs allege had direct interaction with Defendants Davis and Schneider and confirmed that the issue of stale alerts was "elevated to LifeLocks's executive management...." (*Id.* ¶¶ 83, 123.) The SAC also clarifies a company's required actions under payment card industry data security standards ("PCI DSS") and continues to allege that Defendants failed to follow established guidelines. (*Id.* ¶¶ 140-45.) Defendants argue that Plaintiffs have again failed to establish scienter as required under 15 U.S.C. §§ 78u-4(a) *et seq.* and have failed to correct the deficiencies as outlined by this Court's prior August 3, 2016 Order. (MTD at 1.) Defendants therefore move to dismiss the SAC with prejudice. (*Id.*)

II. LEGAL STANDARDS AND ANALYSIS

A Rule 12(b)(6) dismissal for failure to state a claim can be based on either (1) the lack of a cognizable legal theory or (2) insufficient facts to support a cognizable legal claim. *Conservation Force v. Salazar*, 646 F.3d 1240, 1242 (9th Cir. 2011), *cert. denied*, *Blasquez v. Salazar*, 132 S. Ct. 1762 (2012). In determining whether an asserted claim can be sustained, "[a]ll of the facts alleged in the complaint are presumed true, and the pleadings are construed in the light most favorable to the nonmoving party." *Bates v. Mortg. Elec. Registration Sys., Inc.*, 694 F.3d 1076, 1080 (9th Cir. 2012). "[A] well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof of those facts is improbable, and 'that a recovery is very remote and unlikely.' " *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 556 (2007) (quoting *Scheuer v. Rhodes*, 416 U.S. 232, 236 (1974)). However, "for a complaint to survive a motion to dismiss, the nonconclusory 'factual content,' and reasonable inferences from that content, must be plausibly suggestive of a claim entitling the plaintiff to relief." *Moss v. U.S. Secret Serv.*, 572 F.3d 962, 969 (9th Cir. 2009) (quoting *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009)). In other words, the complaint must contain

enough factual content "to raise a reasonable expectation that discovery will reveal evidence" of the claim. *Twombly*, 550 U.S. at 556.

***2** Section 10(b) or Rule 10b-5 claims also must meet the particularity requirements of Federal Rule of Civil Procedure 9(b), which requires that "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." Fed. R. Civ. P. 9(b); *see also In re Daou Sys., Inc. Sec. Litig.*, 411 F.3d 1006, 1014 (9th Cir. 2005). Moreover, these claims must meet the heightened pleading standards of the Private Securities Litigation Reform Act ("PSLRA"). *See* 15 U.S.C. § 78u-4. The PSLRA requires a securities fraud complaint to "plead with particularity both falsity and scienter." *Gompper v. VISX, Inc.*, 298 F.3d 893, 895 (9th Cir. 2002). To properly allege falsity, a complaint must "specify each 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, ... state with particularity all facts on which that belief is formed." *Id.* (quoting 15 U.S.C. § 78u-4(b)(1)) (quotation marks omitted). To adequately plead scienter, the complaint must "state with particularity facts giving rise to a strong inference that defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2). To adequately demonstrate that the "defendant acted with the required state of mind," a complaint must "allege that the defendants made false or misleading statements either intentionally or with deliberate recklessness." *In re Daou Sys.*, 411 F.3d at 1014-15. "[A]n actor is [deliberately] reckless if he had reasonable grounds to believe material facts existed that were misstated or omitted, but nonetheless failed to obtain and disclose such facts although he could have done so without extraordinary effort." *In re Oracle Corp. Sec. Litig.*, 627 F.3d 376, 390 (9th Cir. 2010) (quoting *Howard v. Everex Sys., Inc.*, 228 F.3d 1057, 1064 (9th Cir. 2000)). The Supreme Court has emphasized that courts "must review 'all the allegations holistically' " when determining whether scienter has been sufficiently pled. *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 49 (2011) (quoting *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 326 (2007)). The relevant inquiry is "whether all of the facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegation, scrutinized in isolation, meets that standard." *Tellabs*, 551 U.S. at 323. In securities cases, falsity and scienter "are generally strongly inferred from the same set of facts" and the two requirements may be combined into a unitary inquiry under the PSLRA." *Ronconi v. Larkin*, 253 F.3d 423, 429 (9th Cir. 2011).

A. "Proactive and "Near Real-Time" Alert Services

Defendants argue that Plaintiffs have again failed to allege falsity and scienter with respect to individual Defendants' statements about proactive and near real-time alerts. (MTD at 13.) Plaintiffs must plead scienter "with respect to each act or omission alleged to have violated this chapter." 15 U.S.C. § 78u-4(b)(2); *see Zucco Partners, LLC v. Digimarc Corp.*, 552 F.3d 981, 998 (9th Cir. 2009) (holding the complaint could be dismissed under Fed. R. Civ. Pro. 12(b)(6) because scienter could not be established when viewed holistically or individually). Plaintiffs present a number of statements and documents from which they seek to establish scienter, including: (1) a PowerPoint presentation entitled "Project Granite" presented to "LifeLock executives" in March 2015; (2) statements of six confidential witnesses; (3) statements of former LifeLock employees; (4) an allegation that the false or misleading statements were related to the company's "core operations" so that the Court can infer corporate scienter without individual scienter; and (5) the resignation of senior executives. (*See* SAC ¶¶ 55-65, 77-84, 88-94, 105, 120-130; Doc. 103, Resp. in Opp'n to MTD ("Resp.") at 31-33.)

Much of this information is a reiteration of allegations already deemed insufficient to plead scienter in Plaintiffs' earlier complaint. In particular, the "Project Granite" briefing and the statements of confidential witnesses CW 1, CW 2, CW 3, CW 4, and former employees were not enough to sufficiently plead Defendants acted with scienter. (Aug. 3, 2016 Order at 5-9.) Here, in addition to the earlier statements, Plaintiffs provide new confidential witness statements from CW 5 and CW 6 and public statements made at company events to prove scienter. The statements of CW 5 and CW 6 are the most significant additions to Plaintiffs' SAC, but the Court must evaluate these statements under the *Zucco*[2] test to determine their ability to satisfy the PSLRA's requirements.

i. *Zucco* Test and Confidential Witness Statements

Zucco requires that: (1) the confidential witnesses' statements must possess sufficient particularity to

illustrate reliability and personal knowledge, and (2) the reported statements, which illustrate sufficient reliability and personal knowledge, must also be indicative of scienter. *Zucco Partners, LLC*, 552 F.3d at 995. Even reviewing the statements of CW 5 holistically, they fail to pass the *Zucco* test. The allegations state that CW 5 was an Identity Alert Specialist at LifeLock throughout the class period, had regular contact with LifeLock executives, and managed Defendant Davis' personal LifeLock account. (SAC ¶ 82.) CW 5 was responsible for generating reports regarding alert trends and sending those reports to Vice President of Member Services Rob Ryan. (*Id.* ¶¶ 82, 121.) Plaintiffs allege these reports circulated throughout LifeLock's executive management team, including Defendant Schneider, based on information provided by Mr. Ryan to CW 5. (*Id.*) CW 5 asserts that Mr. Ryan told her that he not only provided Defendant Schneider the reports, but that he also held meetings with her regarding the data contained in the reports. (*Id.* ¶ 121.) Plaintiffs' allegations, however, fail to provide any concrete information about the level of discussion in regards to the data, the specific data discussed, the length of these meetings, or any other information about Mr. Ryan's access to the individual Defendants. Here, CW 5's allegations rely on statements to him/her from Mr. Ryan, but there is nothing in the SAC to allege Mr. Ryan's reliability and personal knowledge. While hearsay may be used to support a complaint, it must be "sufficiently reliable, plausible, or coherent" to be considered probative of scienter. *Lloyd v. CVB Financial Corp.*, 811 F.3d 1200, 1208 (9th Cir. 2016). Plaintiffs in this case fail to provide the foundational information that would show the information is sufficiently reliable to justify the use of hearsay. The allegations do not illustrate whether Mr. Ryan's position was in sufficient parity with Defendants to infer his communications would reach these individuals. Moreover, it is unknown if Mr. Ryan's position as "Vice President of Member Services" would require him to communicate this information directly to top executives. The SAC also fails to provide any details regarding the alleged conversations between Mr. Ryan and CW 5. Therefore, CW 5's allegations based on statements from Mr. Ryan are insufficient to establish scienter.

***3** In addition to statements from Mr. Ryan, CW 5 states Defendant Schneider acknowledged being aware of "stale" alerts transmitted to customers after a question from one of the attendees at a company lunch where CW 5 was present. (SAC ¶¶ 122, 130.) This statement may establish personal knowledge on the part of CW 5, however, Defendant Schneider's general awareness of "stale" alerts does not show knowledge of the systemic problem alleged by Plaintiffs. These statements by Plaintiffs' CW 5 also fail to satisfy the *Zucco* test.

The SAC states that CW 6 was an employee at LifeLock from July 2014 to February 2016 as a Member Services Team Manager, and later as a Manager of Escalations and Identity Operations. (*Id.* ¶ 83.) CW 6 alleges that "stale" alerts were continuous throughout the class period, and the issues were brought to the attention of "executive management" but fell on "deaf ears." (*Id.* ¶ 123.) The SAC indicates CW 6 reported the information to his or her supervisor who was multiple levels of authority below any named Defendant. (*Id.* ¶ 83.) The SAC fails to allege CW 6 had any personal contact with any named Defendant in regards to the issue of "stale" alerts. In fact, the Court can only infer CW 6 may have had direct communication with individual Defendants from a statement that CW 6 responded to customer complaints in Defendant Schneider's stead. (*Id.*) Such an inference, however, does not reasonably lead to an inference that CW 6 ever spoke to Defendant Schneider concerning stale alerts or that she was aware of the contents of the customer complaint letters. CW 6's statements fail the *Zucco* test.

ii. Corporate Scienter

Plaintiffs argue that, in lieu of finding scienter for individual Defendants, this Court should impute corporate or collective scienter to LifeLock as a corporate entity. (Resp. at 37-38.) The Ninth Circuit may allow for some form of corporate scienter, but only in situations where "a company's public statements were so important and so dramatically false that they would create a strong inference that at least *some* corporate officials knew of the falsity upon publication." *Glazer Capital Mgmt., LP v. Magistri*, 549 F.3d 736, 744 (9th Cir. 2008). In coming to this tentative conclusion, the Ninth Circuit relied on a hypothetical given by the Seventh Circuit in which a car manufacturer announced it had sold one million SUVs in a year when it had actually sold zero. *Id.* at 743-44 (citing *Makor Issues & Rights, Ltd. v. Tellabs, Inc.*, 513 F.3d 702, 710 (7th Cir. 2008)). Therefore, the doctrine of corporate scienter is limited only to situations in which statements are so dramatically false that their

falsity should be obvious to corporate officials with reasonable knowledge about their companies. *See In re Volkswagen "Clean Diesel" Marketing, Sales Practices, and Products Liab. Litigation*, No. 3:15-md-2672-CRB, 2017 WL 66281, 14-15 (N.D. Ca. Jan. 4, 2017) (finding that the alleged fraud regarding Volkswagen's diesel engines was so widespread and integral to the company's business strategy that it was highly unlikely that executive management could have been unaware of it). Here, Plaintiffs alleged the credit alerts were one of the most important aspects of LifeLock's business and were one of the driving factors leading customers to purchase more expensive plans. (SAC ¶¶ 45-47, 120.) These alerts, however, were only a single element of the service provided by the company and the SAC provides only passing statements by CW 5 that they were a primary driver in customer purchases of the "Ultimate Plus" package. (*Id.* ¶ 120.) This distinguishes this case from other cases where the falsity was so vast and vital to a company's operations that a court could impute scienter to the corporate entity. The SAC does not sufficiently allege corporate scienter to defeat Defendants' Motion to Dismiss under Federal Rule of Civil Procedure 12(b)(6).

iii. Resignations

***4** Plaintiffs argue that the resignations of Defendants Davis and Power three and five months respectively after the FTC settlement supports an inference of scienter. (Resp. at 38-39.) In order for a resignation to support an inference of scienter, a plaintiff must allege "that the resignation at issue was uncharacteristic when compared to the defendant's typical hiring and termination patterns or was accompanied by suspicious circumstances." *Zucco Partners, LLC*, 552 F.3d at 1002. Absent such allegations, "the inference that the defendant corporation forced certain employees to resign because of its knowledge of the employee's role in the fraudulent representations will never be as cogent or as compelling as the inference that the employees resigned or were terminated for unrelated personal or business reasons." *Id.* Plaintiffs have failed to allege that the resignations of Defendants Davis and Powers were uncharacteristic or accompanied by suspicious circumstances. (*See* SAC ¶¶ 176-80.) Indeed, it is neither surprising nor suspicious that the CEO and CFO of a company would resign following a lawsuit and settlement with the FTC. Therefore, the Court concludes that Plaintiffs have failed to allege an adequate inference of scienter with regard to statements about proactive and near real-time alerts. [3]

B. Payment Card Industry Data Security Standard Compliance

This Court previously held that the PCI DSS certification LifeLock received just prior to the Class Period negates any inference of scienter in statements made that LifeLock complied with or would comply with PCI DSS standards. (Aug. 3, 2016 Order at 10-11.) Moreover, the statements made by the Defendants were not promises or assurances that the company was operating within PCI DSS standards at all times, but were statements that the company strives to operate at that level or had already received the certification. (*See* SAC ¶¶ 132-33). The SAC does not make any new allegations that contribute to the scienter of the Defendants. The new amendments further clarify the PCI DSS certification requirements and illustrate how the company failed to operate at that level, but they do not show scienter on behalf of the individual Defendants. (*See id.* ¶¶ 139-44.) While Plaintiffs allege that Defendant Schneider did acknowledge issues related to enrollment of new LifeLock customers and problems faced with the automation process, that alone does not establish scienter in regards to the PCI DSS compliance (*See id.* ¶ 146.) These acknowledgements related to issues with the entire system rather than PCI DSS compliance alone and are insufficient to show that Defendant Schneider was aware of the specific failures alleged. (*See id.* ¶¶ 140-44.) Therefore, the Court concludes that Plaintiffs failed to adequately plead scienter on the part of Defendants with regards to PCI DSS compliance.

C. FTC Investigation

Plaintiffs made minimal changes to the SAC's allegations regarding the FTC investigation. (*See* SAC ¶¶ 155, 165, 167, 178-180.) Plaintiffs stated they re-pled these allegations in order to preserve them for appeal in accordance with Ninth Circuit case law. (Resp. at 9); *see Lacy v. Maricopa Cnty.*, 693 F.3d 869 (9th Cir. 2012) (holding a claim dismissed with leave for amend must be re-pled to preserve for appeal). Because there have been no meaningful changes, the Court dismisses the allegations related to the FTC Investigation.

D. Dismissal with Prejudice

Defendants argue the Court should dismiss the SAC with prejudice. (MTD at 1.) Plaintiffs request this Court permit them leave to amend their complaint. (Resp. at 40.) Federal Rule of Civil Procedure 15 provides that a party may amend its pleading with leave of court, and "[t]he court should freely give leave when justice so requires." Fed. R. Civ. P. 15(a)(2). "In deciding whether justice requires granting leave to amend, factors to be considered include 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." *Moore v. Kayport Package Express, Inc.*, 885 F.2d 531, 538 (9th Cir. 1989) (citing *Foman v. Davis*, 371 U.S. 178, 182 (1962)).

***5** Further leave to amend is not warranted because Plaintiffs have repeatedly failed to cure deficiencies in their Complaint. Plaintiffs acknowledge they made minimal changes to their claim regarding the FTC investigation. Plaintiffs clarified the PCI DSS requirements for companies in their SAC, but failed to address that Defendant received the certification just prior to the start of the class period. Moreover, the only new statement from an individual Defendant is stating that a system upgrade would cost $100 million and LifeLock "can't afford that." (SAC ¶ 146.) This statement, however, appears to discuss the costs of correcting issues related to enrollment, automation, and reduction of system downtime and were not directly related to the data security standard. (*Id.*) These statements are not indicative of scienter and there is no indication that further leave to amend will provide the requisite scienter. Finally, Plaintiffs have repeatedly failed to cure deficiencies in their attempts to plead scienter with respect to Lifelock's alleged failure to provide near real-time alerts. Therefore, the Court grants Defendants' Motion to Dismiss with prejudice.

III. CONCLUSION

The Court grants Defendants' Motion to Dismiss the SAC because it fails to sufficiently allege that Defendants made statements concerning LifeLock's alert services and PCI DSS compliance with scienter. Moreover, Plaintiffs acknowledge they made no substantial changes to the FTC complaints and only sought to preserve those claims for appeal. Additionally, the facts of this case do not allow for an inference of corporate scienter. This was Plaintiff's third opportunity to submit a complaint with sufficient facts to support a cognizable legal claim, but they have failed to fulfill this requirement. Therefore, the Court grants Defendants' request to dismiss the SAC with prejudice.

IT IS ORDERED granting Defendants' Motion to Dismiss Second Amended Class Action Complaint with prejudice (Doc 97).

IT IS FURTHER ORDERED granting Defendants' Request for Judicial Notice in Support of Motion to Dismiss Second Amended Class Action Complaint (Doc. 99).

IT IS FURTHER ORDERED directing the Clerk to enter judgment accordingly.

All Citations

Slip Copy, 2017 WL 3669615

Footnotes

1 In deciding this Motion, the Court considered the contents of the Second Amended Class Action Complaint and Defendants' exhibits submitted with their Motion. The Court concludes, and Plaintiffs do not dispute, that these exhibits are properly noticeable on a motion to dismiss because they are either incorporated by reference in the Second Amended Class Action Complaint or are "matters of public record." (*See* Doc. 99, Defs.' Req. for Judicial Notice ISO MTD); *Lee v. City of L.A.*, 250 F.3d 668, 688-89 (9th Cir. 2001).

2 552 F.3d at 995.

3 Plaintiffs again argue that scienter may be imputed in this case under the "core operations" doctrine. (Resp. at 37.) The Court rejects this argument for the same reasons it rejected it previously; in the absence of other particularized supporting allegations of scienter, the "core operations" inference, by itself, is insufficient. (Aug. 3, 2016 Order at 9 n.4); *South Ferry LP, No. 2 v. Killinger*, 542 F.3d 776, 784-85 (9th Cir. 2008).

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