IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF TEXAS
AUSTIN DIVISION

In re DELL INC. SECURITIES LITIGATION) Case No. A-06-CA-726-SS

DEFENDANTS' MOTION TO DISMISS AND MEMORANDUM IN SUPPORT

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INTRODUCTION

Plaintiff's lengthy Consolidated Amended Complaint ("Complaint") fails to plead a cognizable claim of securities fraud, and should therefore be dismissed. Most fundamentally, the loss causation element of a securities fraud claim is completely absent here: by plaintiff's own account, Dell's share price decline did not result from any revelation of the alleged fraud of which plaintiff complains. Rather, the decline was caused by disappointing financial results completely unconnected to the alleged fraud.

As the U.S. Supreme Court emphasized in *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005), a showing of loss causation is crucial, because a drop in stock price frequently results from factors that have nothing to do with any alleged fraud, such as "changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events." *Id.* at 343. Absent the requirement that a plaintiff demonstrate that the alleged fraud *caused* the claimed loss, free-floating allegations of fraud could too easily be used to turn the securities laws into "broad insurance against market losses" that are not caused by fraud. *Id.* at 345. The Complaint in this case is a prototypical example of that problem. In particular:

- The Complaint alleges that Dell shareholders' market losses were caused by announcements of disappointing financial projections and results, not by any revelation of the alleged fraud;
- Far from these announcements in some way revealing the alleged fraud, the Complaint alleges that the declines occurred without the Defendants ever having to expose the true nature of the fraud;
- The Complaint identifies numerous non-fraudulent causes for Dell's disappointing financial results, including multiple business problems and challenges affecting Dell's sales, margins, and market share in the relevant time period;

- The accounting restatement on which plaintiff relies makes clear that the accounting errors which the Complaint alleges – even if assumed, *arguendo*, to have resulted from fraud – affected a minuscule percentage of Dell's revenues; and

- The Complaint's sole effort to allege any connection between the losses and the alleged fraud is the wholly conclusory assertion that some unspecified portion of Dell's disappointing financial results resulted from "Dell's attempt to unwind" (in some fashion not specified in the Complaint) the alleged fraudulent scheme.

In short, the Complaint, for all its length, includes not a single factual allegation that connects Dell's share price decline to the alleged fraud – and, for good measure, it includes multiple allegations that point to non-fraud causes for the decline. Courts have routinely rejected such allegations as insufficient.

The Complaint also fails to plead particularized facts that give rise to a cogent and compelling inference that Dell's top executives responsible for public disclosure *knew* that any of the questioned statements were false when made or that they acted in a severely reckless manner as to the falsity of any such statement. Plaintiff cannot satisfy its strict threshold burden merely by pointing to Dell's restatement, or by making allegations that are not specific about particular Dell executives' knowledge concerning particular statements. A later restatement does not raise any inference about the state of mind of an executive at the time the earlier, allegedly false statement was made.

BACKGROUND

Dell is one of the world's leading suppliers of information technology and internet infrastructure products. Dell is a multi-billion dollar company; during the putative Class Period, from May 16, 2002 through September 8, 2006, Dell's available cash, cash equivalents, and investments grew from $8.2 billion (Q1FY03) to $12.4 billion (Q4FY07), its net revenues grew from $35.3 billion (FY03) to $57.4 billion (FY07), and its gross margin increased from $6.4 billion (FY03) to $9.5 billion (FY07). *See* Dell Inc., Annual Report (Form 10-K) at 21, 34 (Oct. 30, 2007) (Ex. 1).[1]

The Complaint alleges that, from 2002 to 2005, Dell's earnings grew – meeting or exceeding expectations – and its stock price accordingly rose from $27.85 at the start of the class period to a high of $42.57 on December 9, 2004. *See, e.g.*, Complaint ¶¶ 75, 339, 755. Also according to the Complaint, however, Dell's business model deteriorated, its profit margin declined, its growth was hamstrung by a limited consumer market, and its competitors surpassed it in sales of personal computers. *See, e.g.*, *id.* ¶¶ 17, 61, 64, 76. As a result of these business setbacks, Dell issued a number of allegedly disappointing earnings releases or downward revisions of its financial forecasts from August 2005 through August 2006. *See id.* ¶¶ 757-64. The Complaint alleges that these earnings reports caused the stock price to fall gradually over a year-long period and, by the end of the class period, Dell's stock price fell to $21.65. *See id.* ¶ 767.

Dell's Restatement. On August 17, 2006, Dell announced that the SEC was conducting an informal investigation into Dell's accounting practices. *See* Complaint ¶ 13. On September 11, 2006, Dell issued a press release stating that it would delay filing its Form 10-Q because the SEC investigation and an independent investigation by its audit committee

[1] On a motion to dismiss, courts may consider "public disclosure documents required by law to be, and that have been, filed with the SEC, and documents that the plaintiffs either possessed or knew about and upon which they relied in bringing the suit," *Fin. Acquisition Partners LP v. Blackwell*, 440 F.3d 278, 286 (5th Cir. 2006) (internal quotation marks omitted), as well as other matters of public record, such as stock prices. *In re Capstead Mortgage Corp. Sec. Litig.*, 258 F. Supp. 2d 533, 543 (N.D. Tex. 2003).

had raised questions about the Company's reported financial results. *See id.* ¶¶ 13, 765. On October 30, 2007, the Company restated its financials for the fiscal years 2003-2006 and the first quarter of fiscal 2007 ("Restatement Period"), reflecting both changes growing out of the independent investigation as well as additional changes identified by the Company in a review of its accounting. *See* Ex. 1. Dell restated earnings upwards for some quarters and downward for others, with the cumulative change to net income for the Restatement Period being a reduction of $106 million. *See id.* at 21. This restatement constituted less than 1% of Dell's net income of over $12 billion for the Restatement Period. *See id.* On the day after Dell released its restated financials, Dell stock closed at $30.60, up $0.80 from the previous day. *See* Chart of Dell Stock Prices (Ex 2).

Allegations of the Amended Complaint. Following the August 17, 2006 announcement, a number of securities-fraud actions were filed. This Court consolidated those actions on February 28, 2007 and chose Union Asset Management Holding AG as lead plaintiff of the consolidated action on April 9, 2007. Plaintiff filed the Complaint on January 11, 2008. Though lengthy at over three hundred pages, the Complaint essentially alleges that defendants: (1) engaged in accounting fraud; (2) knowingly made false statements to investors; and (3) profited on inside information.

First, plaintiff alleges that Dell engaged in erroneous accounting practices by accelerating and overstating revenue, mismanaging various accruals and reserves, and manipulating warranty liabilities. *See* Complaint ¶¶ 101, 103-42. Plaintiff claims that the individual defendants knew of the erroneous accounting because they "had unfettered access to all financial information and were intimately involved in the day-to-day management of the company," "had direct oversight of and actively managed accounting functions," and "implemented policies that encouraged the fraud." *Id.* ¶ 617. To support these claims, plaintiff relies on confidential informants for allegations that the individual defendants were "very hands on," *id.* ¶ 623, that they attended meetings at which revenue recognition and costs were discussed, *see id.* ¶¶ 627, 633, and that "[a]ll policy, accounting and reporting decisions were ultimately made at the highest level of the Company." *Id.* ¶ 634. Plaintiff also cites the Dell restatement for the allegation that unnamed "senior executives" directed some of the misstatements. *Id.* ¶ 14.

Second, the Complaint alleges that, beginning in 2002, defendants disseminated false and misleading information to the public touting the company's financial results based on its unique business model, when, in reality, Dell's successes were based on accounting fraud. In support of these allegations, the Complaint outlines positive statements made by defendants in each earnings press release, earnings call transcript, and SEC filing from Q1FY03 through Q2FY07. *See id.* ¶¶ 161-614. The allegedly false and misleading statements included assurances from Dell that the Company was excelling in key financial metrics, maintaining adequate internal financial accounting and disclosure controls, and implementing a successful direct sales business model. *See id.* ¶¶ 71-74. For each of these statements, plaintiff's sole contention is that they were "false and misleading when made" because, "as admitted by Dell's restatement, the Company improperly recognized revenue throughout the Class Period and 'used accounting adjustments … to compensate for earnings shortfalls that could not be closed through operational means.'" *E.g., id.* ¶¶ 164, 169, 177, 592, 605, 610 (alteration in original).

Plaintiff claims that, although the bottom-line impact of the restatement was small, Dell's violations were material. *See id.* ¶¶ 143-51. The Complaint identifies six quarters in which earnings were restated downwards, and alleges that in four of those quarters Dell retrospectively missed its earnings guidance to investors. *See id.* ¶¶ 143-44. For each of these quarters, Dell decreased earnings per share by one to three cents. *See id.* ¶ 146. The Complaint does not allege how much of the restatement of Dell's financials resulted from purportedly intentional fraudulent activity, as opposed to mere accounting errors.

Third, the Complaint alleges that defendants took advantage of the inflated stock prices to cash in some of their stocks and stock option grants. Specifically, plaintiff claims that during the Class Period of more than four years, Michael Dell sold 29.61% of his Dell stock, Rollins sold 13.65%, and Schneider sold 49.33%. *See id.* ¶ 666. These sales occurred consistently from November 2002 through August 2005. *See id.* ¶¶ 669-70.

Notably, plaintiff expressly alleged that Dell's stock price declined because of Dell's poor earnings results, even though the alleged fraud was not revealed. *See id.* ¶ 76. "As a result of a series of announcements of missed revenue and earnings targets from August 2005 through the beginning of August 2006, Dell's stock price declined precipitously from approximately $40.00 per share to $22.00 per share, without the Defendants ever having to expose the true nature of the fraud they had been committing for years." *Id.* ¶ 76. According to the Complaint, the earnings statements, "although not ostensibly disclosing fraud, began Dell's deceptive attempt to unwind its fraudulent scheme." *Id.* ¶ 758; *see also id.* ¶¶ 760, 762, 764.

ARGUMENT

I. THE COMPLAINT FAILS TO SATISFY THE LOSS CAUSATION REQUIREMENT OF A SECURITIES FRAUD CLAIM.

The loss causation element of a Section 10(b) claim, codified in the Private Securities Litigation Reform Act ("PSLRA"), requires that a defendant's fraud "cause[ ] the loss for which the plaintiff seeks to recover damages." 15 U.S.C. § 78u-4(b)(4). Here, plaintiff alleges that Dell's share price dropped *not* because of revelation of the alleged fraud, but because Dell's earnings failed to meet expectations and the stock price declined. Plaintiff does not even allege a connection between the poor earnings reports and the alleged fraud, except by asserting, without explanation, that the reports somehow reflect Dell's alleged "unwind[ing]" of the fraud. Complaint ¶¶ 758, 760, 762, 764. There is no allegation of what this "unwinding" consisted of, what alleged misstatements were unwound, how it affected earnings, or how it could be going on (according to the Complaint) simultaneously with the alleged fraud itself.

In short, plaintiff seeks to satisfy the loss-causation requirement merely by alleging the existence of misstatements and a subsequent drop in stock price, with only a conclusory allegation to connect the two – a version of loss causation that would allow plaintiffs to use the securities laws as "insurance" for market losses simply by alleging a fraud at some point prior to a drop in stock price. These allegations are inadequate under *Dura*, as well as under numerous subsequent cases holding that a loss caused by disappointing earnings announcements cannot satisfy the requirement that the loss be caused by the alleged fraud. The allegations also fail to satisfy the principle, recognized in *Dura*, *Oscar Private Equity Invs. v. Allegiance Telecom, Inc.*, 487 F.3d 261, 262 (5th Cir. 2007), and many other cases, that loss causation requires a disclosure that *corrects* prior misstatements. None of the announcements identified in the Complaint as causing Dell's share price decline said anything related to – let alone corrected – the misstatements plaintiff alleges.

A. The Complaint's loss causation allegations fail at the threshold because they do not satisfy the particularity requirement of Rule 9(b).

As a threshold matter, the Complaint's conclusory loss causation allegations fail to satisfy Rule 9(b) of the Federal Rules of Civil Procedure, which states that "the circumstances constituting fraud or mistake shall be stated with particularity." Although the applicability of Rule 9(b) to loss causation was left open in *Dura*, the plain language of the rule applies to all of the "circumstances constituting fraud," and loss causation is one of the traditional elements of fraud. 544 U.S. at 346. Moreover, the sole circuit court to have addressed the issue has suggested that the particularity requirement does apply. *See Teachers' Retirement Sys. of La. v. Hunter*, 477 F.3d 162, 186 (4th Cir. 2007) ("A strong case can be made that … loss causation should be pleaded with particularity.") (internal citation omitted), and the SEC has stated that Rule 9(b) sets the standard for pleading loss causation. Brief of the United States as Amicus Curiae Supporting Petitioners at 15, *Dura* (No. 03-932) (Ex. 3).[2]

[2] The district courts are divided in their approach. *Compare In re First Union Corp. Sec. Litig.*, No. Civ. 3:99CV237-H, 2006 WL 163616, at *6 (W.D.N.C. Jan. 20, 2006) (plaintiff must plead loss causation with particularity); *Collier v. Aksys Ltd.*, No. 3:04CV1232 (MRK), 2005 WL 1949868, at *10 (D. Conn. Aug. 15, 2005) (same); *Joffee v. Lehman Bros., Inc.*, No. 04 Civ. 3507 RWS, 2005 WL 1492101, at *14 (S.D.N.Y. June 23, 2005) (same for common law fraud claim), *with In re Enron Corp. Sec., Derivative & "ERISA" Litig.*, 439 F. Supp. 2d 692, 702, 706 (S.D. Tex. 2006) (loss causation requires only notice pleading); *In re Sara Lee Corp. Sec. Litig.*, No. 03 C 2302, 2006 WL 1980199, at *7 (N.D. Ill. July 10, 2006) (same); *Sekuk Global Ent. v. KVH Indus., Inc.*, No. Civ. A. 04-306ML, 2005 WL 1924202, at *17 (D.R.I. Aug. 11, 2005) (same). The courts that hold Rule 9(b) does not apply to loss causation have generally come to this conclusion based on an overreading of *Dura* and without any further analysis. *See*

This conclusion is supported by the Fifth Circuit authority holding, in the Section 10(b) context, that Rule 9(b) applies to *all* of the required elements for making out a claim of fraud. *See Williams v. WMX Technologies, Inc.*, 112 F.3d 175, 177 (5th Cir. 1997); *see also Plotkin v. IP Axess Inc.*, 407 F.3d 690, 696 (5th Cir. 2005) (particularity requirement applies to proximate cause element of § 10(b) claim).

Accordingly, as the Complaint's conclusory efforts to connect Dell's earnings announcements with the alleged fraud contain not even a pretense of particularity, this, alone, requires the dismissal of the Complaint.

B. Independent of any particularity requirement, the Complaint's loss causation allegations fall far short of what is required.

In any event, entirely apart from Rule 9(b), the Complaint's loss causation allegations fail under well-established law. *Dura* itself makes clear that a plaintiff has the burden of pleading a cognizable theory of loss causation, and the Supreme Court more recently emphasized that – even aside from any Rule 9(b) requirements – a complaint must plead "enough factual matter" to make the plaintiff's entitlement to relief "plausible." *Bell Atlantic Corp. v. Twombly*, 127 S. Ct. 1955, 1965 (2007). This includes, at a minimum, alleging facts sufficient to cross "the line between the conclusory and the factual." *Id.* at 1966 n.5.

Here, plaintiff alleges that Dell's stock price decline was caused by four earnings-related announcements. *See* Complaint ¶¶ 758-64. Three of these statements – on

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Enron, 439 F. Supp. 2d at 702; *Sara Lee*, 2006 WL 1980199, at *7; *Sekuk*, 2005 WL 1924202, at *17.

August 11, 2005, February 16, 2006, and August 17, 2006 – announced results for the prior quarter that allegedly failed to meet analyst expectations. *See id.* ¶¶ 758-59, 763. The fourth – on May 8, 2006 – reduced Dell's earnings guidance for the quarter. *See id.* ¶ 761.[3] Plaintiff expressly alleges that the fraud was not disclosed in these statements – indeed, that "Dell's stock price declined precipitously from approximately $40.00 per share to $22.00 per share, without the Defendants ever having to expose the true nature of the fraud they had been committing for years." *Id.* ¶ 76. The Complaint's sole attempt to connect the fraud to this decline is the bald assertion that the earnings statements, "although not ostensibly disclosing fraud, began Dell's deceptive attempt to unwind its fraudulent scheme." *Id.* ¶ 758; *see also id.* ¶¶ 760, 762, 764.

As discussed below in greater detail, earnings announcements like these cannot show loss causation. Even if that general rule did not exist, however, the Complaint's perfunctory attempt to connect the alleged accounting fraud to the disappointing announcements would be inadequate to make out a Section 10(b) claim. The allegations are lacking in at least three ways: (1) plaintiff fails to allege how Dell purportedly "unwound" the scheme and how this caused disappointing results; (2) plaintiff fails to quantify the alleged effect of the fraud on these financial results; and (3) plaintiff fails to

[3] Plaintiff does point to one other statement, on September 11, 2006, but fails to allege any stock price decline caused by this statement, *see* Complaint ¶¶ 765-66, as the stock price in fact rose $0.68 the following day, *see* Ex. 2. Indeed, because plaintiff claims that the loss caused by the fraud occurred "between August 11, 2005 and September 8, 2006," Complaint ¶ 767, the subsequent September 11, 2006 statement is irrelevant to the loss causation analysis.

allege which specific alleged misstatements caused Dell to miss or lower its earnings projections. Each of these failings warrants dismissal under *Dura*.

First, the Complaint fails to allege what the characterization of "unwinding" actually means as a factual matter. Plaintiff does not identify any change in accounting made by Dell during the Class Period, who made the changes, when the changes occurred, and whether the changes were material. Plaintiff does not even say how the bottom-line revenue figures would have been different had Dell continued with the alleged fraud. And, while plaintiff alleges that the "unwinding" occurred because of the SEC inquiry, *see* Complaint ¶¶ 499, 518, 527, 607, plaintiff fails to allege that the people who knew about the inquiry were the same people who unwound the scheme.

Such an unexplained allegation does not suffice because it does not "provide[ ] the defendants with notice of … what the causal connection might be between th[e] loss and the misrepresentation," *Dura*, 544 U.S. at 347, and does not make plaintiff's theory of causation "plausible" as required by *Twombly*. Indeed, if this were enough, any plaintiff could simply point to financial statements and claim that poor results were caused by an "unwinding" of fraud without any explanation as to how the fraud affected the financial results.

Furthermore, there is a key contradiction between the "unwinding" theory and the facts alleged. During the same period in which Dell was allegedly "unwinding" the alleged fraud, Dell announced that it had, in fact, exceeded expectations for Q4FY07 – allegedly (according to the Complaint) because it was *still* engaging in the alleged accounting fraud. *See* Complaint ¶ 545 (discussing February 16, 2006 earnings release). In fact, for one earnings release occurring on November 10, 2005, plaintiff alleges *both* that Dell fraudulently inflated revenue and that it lowered revenue to unwind the scheme. *See id.* ¶¶ 523, 527. Thus, plaintiff alleges that Dell committed accounting fraud at the same time that it was unwinding the very same fraud. It is completely inconsistent to allege that the "'truth' began coming out" and to "simultaneously allege that Defendants concealed the true cause of [the company's] revenue drop." *In re Redback Networks, Inc. Sec. Litig.*, No. C03-5642 JF (HRL), 2007 WL 963958, at *4 (N.D. Cal. Mar. 30, 2007). This theory makes no sense, and it cannot support loss causation. *See id.*

Second, plaintiff fails to allege the quantitative effect of the unwinding of the fraud on earnings or the effect of that earnings reduction on the stock price. *Dura* expressly held the plaintiffs' complaint insufficient in part because it did not "provide[ ] the defendants with notice of what the relevant economic loss might be." 544 U.S. at 347. Since the Complaint does not even "ascribe some rough proportion of the whole loss to [the defendant's] misstatements," *Lattanzio v. Deloitte & Touche LLP*, 476 F.3d 147, 158 (2d Cir. 2007), it does not sufficiently allege loss causation.

Third, plaintiff fails to allege which specific misstatements caused Dell to miss or lower its earnings projections. To make out a Section 10(b) claim as to misstatements, loss causation must be pleaded as to each of those misstatements. For example, in a recent Seventh Circuit case, the plaintiffs alleged that a 1997 audit prepared by the defendant was fraudulent. *Tricontinental Indus., Ltd. v. PricewaterhouseCoopers, LLP*, 475 F.3d 824, 828 (7th Cir. 2007). While a public revelation only questioned the 1998 audit, the plaintiffs attempted to plead loss causation based on "the fact that the 1997 fraud was part of an on-going scheme to overrepresent revenue and that the 1998 audit relied in part on historic information." *Id.* at 842. The Seventh Circuit rejected this theory, dismissing the claims because they failed to show the plaintiffs "suffer[ed] a loss when th[e] material misrepresentation 'became generally known.'" *Id.* at 843.

Plaintiff here likewise attempts to show loss causation without linking it to a specific misrepresentation that became known to the market. Instead, plaintiff alleges that Dell "unw[ou]nd its fraudulent scheme," Complaint ¶ 758, but this "scheme" theory fails, just as it did in *Tricontinental*, because it fails to allege that a particular misstatement caused the loss. Indeed, the theory is even more deficient here because plaintiff does not even allege which misstatement or misstatements caused Dell to miss or lower its earnings estimates in the first place. Also, since plaintiff provides different scienter allegations for different misstatements, *see infra* Part II, it is crucial to make clear which misstatements allegedly caused plaintiff's loss. Because plaintiff has failed to do so, the Complaint does not sufficiently allege loss causation.

C. The Complaint fails to satisfy the "corrective disclosure" requirement of loss causation.

Even if plaintiff's allegations were not fatally conclusory, they would fail on the independent ground that they do not satisfy the requirement that there be a disclosure that *corrects* the prior misstatements. *Dura* itself found that the complaint at issue was insufficient because of its "failure to claim that Dura's share price fell significantly *after the truth became known*." *Dura*, 544 U.S. at 347 (emphasis added); *see also id.* at 342 ("If the purchaser sells later *after the truth makes its way into the marketplace*, an initially inflated purchase price *might* mean a later loss.") (first emphasis added). Even to the extent that *Dura* alludes to the possibility that there can be more than one corrective disclosure because "the relevant truth" can "leak out," *id.* at 342, it still requires that the "truth" emerge to cause the loss.[4] The Complaint here expressly pleads that there was no disclosure of the alleged fraud, and it therefore cannot satisfy the corrective disclosure requirement.

In applying *Dura*, the Courts have been clear that, to plead loss causation, a plaintiff must identify "the corrective disclosure," and cannot rely simply on general "negative disclosures." For example, the Seventh Circuit dismissed a Section 10(b) claim because plaintiffs failed to show that the stock price "suffer[ed] a loss when th[e] material misrepresentation 'became generally known'" rather than when other financial information was disclosed. *Tricontinental*, 475 F.3d at 843. Likewise, the Sixth Circuit dismissed a Section 10(b) claim because the complaint "did not plead that the alleged fraud became known to the market on any particular day" and "never alleged that [the bankruptcy announcement that caused the stock price to drop] disclosed any prior misrepresentations to the market." *D.E. & J. Ltd. P'ship v. Conaway*, 133 Fed. App. 994, 999-1000 (6th Cir. 2006). The Fourth Circuit has also held that "[i]t is only after the fraudulent conduct is disclosed to the investing public, followed by a drop in the value of the stock, that the hypothetical investor has suffered a 'loss' that is actionable after the Supreme Court's decision in *Dura*."

[4] The Fifth Circuit referred to this "corrective disclosure" requirement in a recent Section 10(b) case, denying class certification "for wont of any showing that the market reacted to the corrective disclosure." *Oscar*, 487 F.3d at 262. The plaintiffs there had alleged fraud related to the company's reporting of line-installation counts, and had attempted to prove loss causation based on quarterly announcements in which the company reported those counts, along with lower-than-expected earnings. The court rejected this approach because the plaintiffs had failed to make "a showing of loss causation that targets the corrective disclosure appearing among other negative disclosures made at the same time." *Id.*

Glaser v. Enzo Biochem, Inc., 464 F.3d 474, 479 (4th Cir. 2006). Finally, the Second Circuit affirmed the dismissal of a Section 10(b) claim where the plaintiffs argued that accounting fraud had caused the company to go into bankruptcy, holding that corrective disclosure through the materialization of a concealed risk did not occur because "it cannot be said that the risk of bankruptcy was altogether concealed" by the alleged accounting fraud. *Lattanzio*, 476 F.3d at 157. Thus, in the absence of a disclosure that actually *corrects* the fraudulent misstatements, the "[d]isclosure of financial losses generally – even if those financial losses are a result of the specific concealed fact – is not sufficient." *In re Rhodia S.A. Sec. Litig.*, No. 1:05 Civ. 5389 (DAB), 2007 WL 2826651, at *16 (S.D.N.Y. Sept. 26, 2007); *see also, e.g.*, *In re AOL Time Warner, Inc. Sec. Litig.*, 503 F. Supp. 2d 666, 678-79 (S.D.N.Y. 2007) ("[I]t is not enough to argue that E&Y's audit opinions concealed the risk that AOLTW would be unable to meet future revenue projections, because the mere failure to meet earnings forecasts is insufficient to establish loss causation.").[5]

[5] A host of district courts, including several from the Fifth Circuit, have held that the statement that purportedly caused the loss must correct the prior fraudulent statement. *See Romero v. US Unwired, Inc.*, No. 04-2312, 2006 WL 2366342, at *9 (E.D. La. Aug. 11, 2006) (loss causation is not sufficiently pleaded where the supposed disclosures did not "suggest that any of defendants' previous statements may have been misleading"); *In re Odyssey Healthcare, Inc. Sec. Litig.*, 424 F. Supp. 2d 880, 888 (N.D. Tex. 2005) ("the disclosure must at minimum be of a nature that would cause recipients to identify which representations were the false prior representations"); *In re Alamosa Holdings, Inc.*, 382 F. Supp. 2d 832, 862-63 (N.D. Tex. 2005) ("Because none of the other alleged misrepresentations or omissions beyond the May 1, 2002 subscriber number projections were the subject of a corrective disclosure followed by a drop in stock price, there can be no finding that such misrepresentations or omissions caused Plaintiffs' losses."); *see also, e.g.*, *In re Intelligroup Sec. Litig.*, No. 04-4980 (GEB), 2007 WL 3376743, at *47 (D.N.J. Nov. 13, 2007); *Marsden v. Select Medical Corp.*, No. 04-4020 2007 WL 518556, at *4 (E.D. Pa. Feb. 12, 2007); *In re Buca Inc. Sec. Litig.*, No. 05-1762, 2006 WL 3030886, at *9 (D. Minn. Oct. 16, 2006); *First Union*, 2006 WL 163616, at *6; *In re Tellium, Inc. Sec. Litig.*, No. Civ. A. 02CV5878FLW, 2005 WL 2090254, at *4 (D.N.J. Aug. 26, 2005); *In re Initial Public Offering Sec. Litig.*, 399 F .Supp. 2d 261, 266

In addition, the text of the PSLRA confirms this corrective disclosure requirement. In the PSLRA, Congress placed an upper limit on damages as follows:

> [T]he award of damages to the plaintiff shall not exceed the difference between the purchase or sale price …, as appropriate, by the plaintiff for the subject security and the mean trading price of that security during the 90-day period beginning on the date on which the information correcting the misstatement or omission that is the basis for the action is disseminated to the market."

15 U.S.C. § 78u-4(e)(1). Since the statute measures damages based on "the date on which the information *correcting the misstatement or omission* that is the basis for the action is disseminated to the market," 15 U.S.C. § 78u-4(e)(1) (emphasis added), it necessarily assumes that a disclosure that corrects the prior misstatement or omission causes a plaintiff's losses. If there were no requirement that a plaintiff identify "information correcting the misstatement or omission," the entire section would be nonsensical. *See, e.g., United Sav. Ass'n of Texas v. Timbers of Inwood Forest Associates, Ltd.*, 484 U.S. 365, 374 (1988) (rejecting "petitioner's interpretation of [11 U.S.C.] § 362(d)(1)" because it "makes nonsense of § 362(d)(2)").

Here, plaintiff does not allege that the earnings announcements revealed that any prior statement was false. Rather, plaintiff claims that the earnings statements began Dell's attempt to "unwind its fraudulent scheme and thus partially corrected the Defendants' misrepresentations." Complaint ¶ 758; *see also id.* ¶¶ 760, 762, 764. However, these so-called "partial corrections" did not mention anything about prior improper accounting; they simply

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(S.D.N.Y. 2005), *aff'd sub nom. Tenney v. Credit Suisse First Boston Corp., Inc.*, Nos. 05-3430cv, 05-4759cv, 05-4760cv, 2006 WL 1423785, at *1 (2d Cir. May 19, 2006).

stated Dell's financial performance in the prior quarter or estimated it for the current quarter. Indeed, the Complaint itself states that "Dell's stock price declined … without the Defendants ever having to expose the true nature of the fraud." *Id.* ¶ 76. And plaintiff does not identify a single third-party report or article suggesting that Dell's earnings reports made the market aware of prior false statements.

In short, Dell's earnings reports that allegedly led to the stock drops did not "correct[ ] the misstatement or omission that is the basis for the action," 15 U.S.C. § 78u-4(e)(1). As a recent case recognized, "a disclosure of lower than expected earnings" does not "constitute[ ] an admission that the company's prior positive statements about its financial health and business were false." *Congregation of Ezra Sholom v. Blockbuster, Inc.*, 504 F. Supp. 2d 151, 167 (N.D. Tex. 2007).

In fact, the language plaintiff uses, *i.e.*, that Dell was "unwind[ing] its fraudulent scheme," *e.g.*, Complaint ¶ 758, is almost identical to the allegations rejected by the district court in *Powell v. Idacorp, Inc.*, Nos. Civ. 04-249-S-EJL, 04-322-S-EJL, 2007 WL 1498881, at *4 (D. Idaho May 21, 2007). In *Powell*, the court held that "[e]ven if the forecast reductions were 'partial revelations' of the 'impact' of the Defendants' misconduct on the company, the Court finds that loss causation has not been pled because the amended complaint still alleges that the Defendants continued to conceal the misconduct and, therefore, any market reaction was not caused by knowledge of the improper activity." *Id.* at

*5. Simply put, unless the market learns the truth concealed by the fraud, a drop in the stock price cannot be tied to the fraud itself.[6]

D. Disappointing earnings reports do not show that the loss was caused by any prior misstatement, particularly where, as here, there is no direct connection between the misstatement and the earnings results.

Recognizing that *Dura* would mean little if the mere announcement of poor financial results could establish loss causation, numerous courts have explicitly held that financial statements cannot support an allegation of loss causation unless they specifically identify a prior false statement. *See, e.g.*, *Tellium*, 2005 WL 2090254, at *4; *Initial Public Offering*, 399 F. Supp. 2d at 266-67. A recent case from the Northern District of Texas dismissed a Section 10(b) claim for this reason, explaining that a contrary ruling would unmoor securities fraud claims from Congress's intent to compensate only losses caused by the fraud:

> If a decline in stock price caused by a company's failure to meet forecasts were legally sufficient to constitute a corrective disclosure, "then any investor who loses money in the stock market could sue to recover for those losses without alleging that a fraudulent scheme was ever disclosed and that the disclosure cause [sic] their loses [sic]." *In re Initial Public Offering Sec. Litig.*, 399 F. Supp. 2d 261, 267 (S.D.N.Y. 2005). In addition to discouraging candor and inhibiting the flow of accurate information, this standard would, in effect, "provide investors with broad insurance against market loss," rather than simply "protect them against those economic losses that misrepresentations actually cause." *Dura*, 544 U.S. at 345 … . Such a standard would directly contravene *Dura* and clearly is not the result Congress intended.

Blockbuster, 504 F. Supp. 2d at 168. Another Northern District of Texas case likewise rejected Plaintiff's argument that financial statements revealed the company's true financial

[6] In this case, the announcement of Dell's restatement, which plaintiff relies on repeatedly as "admitting" that prior statements were false, resulted in a stock price *increase.*

condition, and thereby showed loss causation, where the fraudulent conduct was not itself revealed. *See Ryan v. Flowserve Corp.*, 245 F.R.D. 560, 573-74 (N.D. Tex. 2007). Plaintiff's contrary argument "leads the Court to a dangerous precipice" because "[t]he 'true financial condition' theory, if accepted, threatens to undermine the objective of securities law and disregards precedent." *Id.*

Under plaintiff's theory – that earnings reports implicitly "unwind" past earnings misstatements – *every* disappointing financial statement (and any stock price drop that results therefrom) would be caused by *every* inaccuracy in any prior financial statement. Such a result makes a mockery of the loss-causation requirement and contravenes *Dura*. As *Dura* explained, "[w]hen the purchaser subsequently resells such shares, even at a lower price, that lower price may reflect, not the earlier misrepresentation, but changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events, which taken separately or together account for some or all of that lower price." 544 U.S. at 342-43. Because of the effects of these other factors on the stock price, "the most logic alone permits us to say is that the higher purchase price will *sometimes* play a role in bringing about a future loss," but this "is insufficient" to show loss causation. *Id.* at 343. Indeed, the goal of the PSLRA loss-causation requirement was to require "that plaintiffs prove that the loss in the value of their stock was caused by the Section 10(b) violation *and not by other factors.*" S. Rep. 104-98, at 7 (1995), *as reprinted in* 1995 U.S.C.C.A.N. 679, 686 (emphasis added). Thus, earnings data – which incorporate many factors – cannot be the basis for loss causation.

Even if earnings statements could suffice under some circumstances, they are plainly inadequate where, as here, the plaintiff's allegations fail to show that poor earnings reports were proximately *caused* by the alleged misstatements. Loss causation requires that the misstatements "proximately cause" the loss. *Dura*, 544 U.S. at 342; *see Huddleston v. Herman & MacLean*, 640 F.2d 534, 549 (5th Cir. 1981), *aff'd in part, rev'd in part on other grounds*, 459 U.S. 375 (1983) ("The plaintiff must prove … that the untruth was in some reasonably direct, or proximate, way responsible for his loss."). *Dura* relied on the common law concept of proximate causation in defining the scope of loss causation. 544 U.S. at 343-45. And, the Court has recognized in the closely analogous RICO context, which also applies the common-law proximate causation standard, that an intermediary step necessary for the chain of causation negates a claim of fraud because "[t]he general tendency of the law, in regard to damages at least, is not to go beyond the first step." *Holmes v. Sec. Investor Protection Corp.*, 503 U.S. 258, 271 (1992) (internal citation omitted). Moreover, there is no proximate causation where the plaintiff's loss "could have resulted from factors other than [the defendants'] alleged acts of fraud … and it would require a complex assessment to establish what portion of [the loss] were the product of [the defendants' actions]." *Anza v. Ideal Steel Supply Corp.*, 547 U.S. 451, 459 (2006).

Applying these basic proximate cause principles here, plaintiff fails to allege loss causation. Plaintiff's loss causation theory rests on the idea that Dell committed accounting fraud, then found out it was being investigated by the SEC, so it started to unwind its scheme, which caused the company to miss or lower its earnings targets, and then the stock price dropped gradually. *See, e.g.*, Complaint ¶¶ 518, 758. Plaintiff thus stretches well beyond "the first step," *Holmes*, 503 U.S. at 271, in trying to connect the loss to the alleged misstatements.

Moreover, plaintiff fails to make any factual allegations to support the idea that the fraud, rather than other intervening factors, caused the stock price to drop. The other factors are evident based on the allegations in the Complaint itself, which claims that Dell's revenue growth decreased because of purported problems with Dell's business model, a limited consumer market, and increased competition in the industry. *See, e.g.*, Complaint ¶¶ 17, 61, 76. Plaintiff makes no attempt to separate out the effect of the alleged fraud from these other factors, which go to the heart of Dell's business. As the Second Circuit recognized in *Lattanzio*, loss causation is not sufficiently pleaded where the "[p]laintiffs have not alleged facts to show that [relevant] misstatements, among others … that were much more consequential and numerous, were the proximate cause of plaintiffs' loss." 476 F.3d at 158.

The business downturn was plainly the more consequential factor here because the size of the restatement is far smaller than the size of the later earnings disappointments. The restatement (which itself resulted only in part from the independent investigation) involved downward adjustments of 2-12% in earnings per share for six quarters, *see* Complaint ¶ 146, and upward adjustments in several other quarters, *see id.* ¶ 670. But the earnings announcements that caused the stock to decline involved far greater numbers. For example, the February 16, 2006 announcement "predicted revenue of $14.2 to $14.6 billion, representing only a six to nine percent growth rate over the prior year," which "fell far short of the 16 and 21 percent year-over-year growth that Dell posted in the two immediately preceding first quarters." *Id.* ¶ 759. Similarly, the May 8, 2006 announcement stated that Dell "would miss the street's earnings expectations for the quarter by five cents per share," *id.* ¶ 761; by comparison, earnings per share were not restated by more than three cents for any prior quarter. *See id.* ¶ 146.

Moreover, the stock price did not decline in response to the restatement itself, which shows that the market did not consider the accounting issues to be of great significance to the stock price. On August 16, 2007, when Dell's stock closed at $25.93 (*see* Ex. 2), Dell issued a press release in which it said that it would restate its previously-issued financial statements relating to fiscal 2003-06 and Q1FY07. *See* Complaint ¶ 86. Following this announcement, Dell's stock began to climb and reached a peak of $28.25 on August 31, 2007. (*See* Ex. 2). Then, after Dell filed the restated financial statements on October 30, 2007, the stock price increased even more. *Id.* As several courts have recognized, where the stock price increases after a restatement, the "reasonable inference" is that the previous price decline was based not on the alleged fraud, but on the overall financial outlook for the company. *Weiss v. Amkor Tech., Inc.*, No. CV 07-0278 PHX-PGR, 2007 WL 2808224, at *8 (D. Ariz. Sept. 25, 2007) (dismissing claim partially on this basis); *see also In re Acterna Corp. Sec. Litig.*, 378 F. Supp. 2d 561, 588 (D. Md. 2005) ("Plaintiffs' allegation that '[b]y the time the Company belatedly admitted the truth … the price of Acterna's common stock had already fallen' is a clear indicator that Defendants' alleged fraudulent conduct did not cause the precipitous decline in Acterna's share price during the Class Period."). This deficiency is especially problematic here because the stock price decline occurred over a period of years, thereby increasing the likelihood that the loss was caused by market forces rather than by the alleged fraud. *See Dura*, 544 U.S. at 345 ("Other things being equal, the longer the time between purchase and sale, the more likely that this is so, *i.e.,* the more likely that other factors caused the loss."). Since defendants are not responsible for these other causes of plaintiff's loss, plaintiff must untangle these factors from the loss it alleges is compensable under Section 10(b). Plaintiff's failure to do so here requires dismissal of the Complaint.

II. PLAINTIFF HAS FAILED TO ALLEGE PARTICULARIZED FACTS SUPPORTING A STRONG INFERENCE OF SCIENTER.

Under the PSLRA, a plaintiff must plead scienter allegations of a Section 10(b) action "with *particularity*" as to *each defendant* and as to "'*each act or omission* sufficient to give rise to a *strong inference* that the defendant acted with the required state of mind.'" *Southland Sec. Corp. v. INSpire Ins. Solutions, Inc.*, 365 F.3d 353, 364 (5th Cir. 2004) (citing 15 U.S.C. § 78u-4(b)) (emphasis added). The Supreme Court recently clarified that the "inference of scienter must be *more than merely plausible or reasonable* – it must be *cogent* and *at least as compelling* as any opposing inference of nonfraudulent intent." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S. Ct. 2499, 2504-05 (2007) (emphasis added). Plaintiff must show that the defendants had "intent to deceive, manipulate, or defraud" or acted with "severe recklessness." *Nathenson v. Zonagen Inc.*, 267 F.3d 400, 408 (5th Cir. 2001) (internal quotations and citations omitted). "Severe recklessness" can only be shown by "highly unreasonable omissions or misrepresentations that involve not merely simple or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and that present a danger of misleading buyers or sellers which is either *known* to the defendant or is *so obvious* that the defendant *must have been aware* of it." *Cent. Laborers' Pension Fund v. Integrated Elec. Servs., Inc.*, 497 F.3d 546, 551 (5th Cir. 2007) (emphasis added). If a plaintiff fails to meet these strict pleading requirements, then the district court "shall," on the defendants' motion, "dismiss the complaint." 15 U.S.C. § 78u-4(b)(3)(A).

Plaintiff fails to establish the requisite state of mind for each defendant with respect to any of the alleged misstatements. Nowhere in its 304-page Complaint does plaintiff provide a sufficient factual basis to show that defendants knew that any of Dell's public statements were false. The Complaint does not allege the existence of any internal documents that defendants saw that contradicted the public statements. It does not allege that defendants attended any meetings where they learned of any improper accounting. Instead, plaintiff relies on the idea that defendants must have known of misstatements based on their positions in the company, an approach frequently rejected by the Fifth Circuit. The Complaint's allegations of motive – based on Dell's performance-based compensation and the defendants' routine stock sales – are similarly unavailing under Fifth Circuit precedent. Indeed, the *only* specific scienter allegation concerns not the individual defendants, but unnamed "senior executives." And, plaintiff fails to show that the alleged scienter of these unidentified individuals can be imputed to Dell, or even which misstatements were known by these individuals. Accordingly, plaintiff fails to meet the strict PSLRA pleading standards mandated by the Supreme Court, and this Court should dismiss the Complaint.

A. Plaintiff's arguments based on "collective knowledge" and defendants' roles in the company do not raise a strong inference of scienter.

Plaintiff fails to allege a strong inference of scienter by lumping together instances in which defendants purportedly became acquainted with portions of Company finances through their corporate roles. To begin with, the Fifth Circuit has condemned group pleading as insufficient to raise a strong inference of scienter. *Fin. Acquisition*, 440

F.3d at 287. Fifth Circuit precedent also makes clear that a strong inference of scienter cannot arise from "the collective knowledge of all the corporation's officers and employees acquired in the course of their employment." *Southland*, 365 F.3d at 366. In particular, a "pleading of scienter may not rest on the inference that defendants must have been aware of the misstatement based on their positions within the company." *Abrams v. Baker Hughes Inc.*, 292 F.3d 424, 432 (5th Cir. 2002). The reason is simple: when a complaint "fails to identify exactly who supplied the information or when they knew the information," it "fall[s] far short of the who, what, when, where, and how required under 9(b) and … the PSLRA." *Rosenzweig v. Azurix Corp.*, 332 F.3d 854, 868 (5th Cir. 2003) (internal quotation marks and citation omitted).

Plaintiff side-steps any discussion of the defendants' *specific* roles at meetings, the *specific* financial information or documents accessed or received by each, or any financial decisions *expressly* attributable to each defendant. Instead, plaintiff alleges that defendants "had unfettered access to all financial information and were intimately involved in the day-to-day management of the Company" and "had direct oversight of and actively managed accounting functions." Complaint ¶ 617. To support these claims, plaintiff relies on confidential witnesses for allegations that the individual defendants were "very hands on," *id.* ¶ 623, that they attended meetings at which revenue recognition and costs were discussed, *see, e.g., id.* ¶¶ 627, 633, and that "[a]ll policy, accounting and reporting decisions were ultimately made at the highest level of the Company," *id.* ¶ 634.[7] These sweeping assertions are merely

[7] Even if the confidential-witness statements gave more than generalized assertions of the defendants' involvement, under the Supreme Court's *Tellabs* standard, confidential-witness statements provide little, if any, basis to create a strong inference of scienter. Courts "must

"collective knowledge" and group-pleading allegations that do not give rise to a strong inference of scienter.

While plaintiff claims that defendants were "ultimately responsible" for every high-level financial decision, *see id.* ¶ 622, it fails to establish that any defendant knew of, or personally made decisions regarding, the *specific* alleged financial matters that made the public statements allegedly false at the time they were made. The closest the Complaint comes is the report of one witness, CS4, that Rollins and Schneider attended monthly product meetings where warranty revenue recognition adjustments were addressed. *See id.* ¶¶ 627, 633. Even this allegation, though, fails to raise a strong inference of scienter because the witness fails to allege "what was said at the meeting[s], to whom it was said, or in what context." *Garfield v. NDC Health Corp.*, 466 F.3d 1255, 1265 (11th Cir. 2006); *see also Southland*, 365 F.3d at 365 (noting that corporate officers may not be liable for unattributed corporate documents absent "specific factual allegations link[ing] the individual to the statement at issue"); *In re Goodyear Tire & Rubber Co. Sec. Litig.*, 436 F. Supp. 2d 873, 897 (N.D. Ohio 2006) (finding allegations "lacking" that showed only that defendants attended

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discount allegations that the complaint attributes to … 'confidential witnesses.'" *Higginbotham v. Baxter Int'l.*, 495 F.3d 753, 756 (7th Cir. 2007). "Usually *that discount will be steep*." *Id.* at 757 (emphasis added). Both the allegations by the confidential witness and the "qualifications" of that witness to provide the information must be largely free from omission and ambiguity. *See Tellabs*, 127 S. Ct. at 2511; *Higginbotham*, 495 F.3d at 756-57. "Concealing names at the complaint stage … does nothing but obstruct the judiciary's ability to implement the PSLRA." *Higginbotham*, 495 F.3d at 757. The Complaint fails to meet this strict standard; rather, it is riddled with omissions undermining the bases for the witnesses' statements and ambiguity regarding sustainable inferences of scienter.

"'weekly meetings'" because, *inter alia*, there were no specific facts demonstrating that "any wrongdoing was discussed" at those meetings).

Moreover, plaintiff fails to provide any facts showing that the defendants accessed or reviewed the *particular* financial information or documents that would have alerted them to any potential material public misrepresentations. *See e.g.,* Complaint ¶¶ 628, 633. Indeed, "even if a corporate officer's position supports a reasonable inference that he likely would be negligent in not being involved in the preparation of a document or aware of its contents, the PSLRA state of mind requirement is severe recklessness or actual knowledge." *Southland,* 365 F.3d at 365. Defendants' routine actions cannot raise a strong inference of scienter because they are "normal functions of a corporate executive and do not amount to allegations of intent or recklessness." *In re BearingPoint, Inc. Sec. Litig.*, 525 F. Supp. 2d 759, 773 (E.D. Va. 2007). In short, the Complaint fails to raise a strong inference of scienter because it does not allege "what each Defendant knew, who specifically knew it, and when each learned of it." *Alamosa Holdings*, 382 F. Supp. 2d at 858.[8]

In another failed attempt to establish scienter as to defendants, plaintiff alleges, "[t]he Individual Defendants each signed SEC filings and made statements that contained materially false and misleading facts and/or omitted material facts" which "further bolsters

[8] Plaintiff similarly asks this Court to infer – to no avail – that Rollins' and Schneider's departures from the Company occurred at suspicious times, raising a strong inference of scienter. Neither the reason nor the timing of their resignations can give rise to such an inference because plaintiff fails to allege any reason for the resignations related to the alleged fraud. *See Southland*, 365 F.3d at 382-83 (finding subsequent resignations of executives "unavailing as proof of commission of fraud by these or other individuals"); *accord Abrams*, 292 F.3d at 434 (finding that company officials resigning to "pursue other interests" had no scienter implications).

the already strong inference of scienter." Complaint ¶ 617; *see also id.* ¶¶ 618-21. The lone court of appeals to publish an opinion on the issue held that such certifications are only probative of scienter if the certifications themselves were signed with knowledge of or severe recklessness as to their falsity. *See Garfield*, 466 F.3d at 1266.[9] In other words, if the defendants do not know the certification to be false, then the fact of its falsity does not show anything about the defendants' mental state. If the law were otherwise, the certifications would become a tool for reducing the scienter requirement, and as *Garfield* explains, "[t]he plain meaning of the language contained in Sarbanes-Oxley, 18 U.S.C. § 1350, does not indicate any intent to change the requirements for pleading scienter set forth in the PSLRA." 466 F.3d at 1266.[10] Indeed, as discussed in a dismissal affirmed by the Fifth Circuit, "mere certification, without more, is insufficient to establish a strong inference of scienter, for if otherwise the Court would be hard pressed to avoid finding scienter in any case that contained internal controls allegations." *In re SourceCorp Sec. Litig.*, No. 3:04-CV-2351-N, slip

[9] The Fifth Circuit discussed the issue in *Central Laborers'*, but did not decide whether to adopt *Garfield*'s approach; instead, it held that the certifications did not support scienter because the plaintiff "does not clearly explain the link between these statements about the internal controls and the actual accounting and reporting problems that arose." 497 F.3d at 555.

[10] Even if the certifications were relevant here, they would provide at most a minimal indication of scienter. While district courts vary in their use of Sarbanes-Oxley certifications for scienter purposes, none considers them more than a secondary factor in the analysis, and most have held the strong-inference requirement was not satisfied despite the certifications. *See, e.g.*, *In re ConAgra Foods, Inc. Sec. Litig.*, No. 8:05-CV-292 *et al.*, 2006 WL 3247199, at *3-4 (D. Neb. Sept. 19, 2006); *Ley v. Visteon Corp.*, No. 05-CV-70737-DT, 2006 WL 2559795, at *9 (E.D. Mich. Aug. 31, 2006); *Zucco Partners, LLC v. Digimarc Corp.*, 445 F. Supp. 2d 1201, 1208-09 (D. Or. 2006); *In re Bally Total Fitness Sec. Litig.*, No. 04-C-3530 *et al.*, 2006 WL 3714708, at *8 (N.D. Ill. July 12, 2006); *In re Watchguard Sec. Litig.*, No. MASTER FILE C05-678J, 2006 WL 2038656, at *10-11 (W.D. Wash. Apr. 21, 2006); *In re Invision Techs., Inc. Sec. Litig.*, No. C04-03181-MJJ, 2006 WL 538752, at *7 n.3 (N.D. Cal. Jan. 24, 2006).

op. at 6 (N.D. Tex. Nov. 7, 2006), *aff'd. sub nom. Templin v. ScourceCorp, Inc.*, No. 06-11368, 2007 U.S. App. Lexis 26306, at *2 (5th Cir. Nov. 12, 2007) (Ex. 4). Thus, the certifications cannot create a strong inference here since plaintiff fails to allege particularized facts to show that the certifications themselves were knowingly falsified.

B. Defendants' performance-based compensation plan does not raise a strong inference of scienter.

Similarly, general allegations about defendants' performance-based compensation are insufficient to raise a strong inference of scienter. "[B]are allegations of motive and opportunity will not suffice to demonstrate scienter because, to hold otherwise, 'would effectively eliminate the state of mind requirement as to all corporate officers and defendants.'" *Rosenzweig*, 332 F.3d at 867 (quoting *Melder v. Morris*, 27 F.3d 1097, 1102 (5th Cir. 1994)). Plaintiff does not properly allege motive here because it fails to plead with particularity what the person alleged to have made the misrepresentation obtained by making it. *Williams*, 112 F.3d at 177. Plaintiff also fails to plead particular facts tying defendants' alleged motive to any knowledge that the public statements were false.

Plaintiff contends that the defendants intentionally instituted and manipulated a bonus plan tied directly to revenue-related numbers that provided them the motive to engage in fraud. *See* Complaint ¶ 637. Motive by – and opportunity for – incentive compensation "can hardly be the basis on which an allegation of fraud is predicated." *Tuchman v. DSC Communications Corp.*, 14 F.3d 1061, 1068 (5th Cir. 1994) (internal quotation marks and citation omitted). Otherwise, "the executives of virtually every corporation in the United States would be subject to fraud allegations. It does not follow that because executives have components of their compensation keyed to performance, one can infer fraudulent intent." *Id.* (internal quotation marks and citation omitted). Yet that is precisely what plaintiff asks this Court to infer. The Complaint sets out the bonus plan and defendants' compensation in great detail, but wholly fails to tie the plan to any facts showing the defendants' culpability in issuing any contemporaneous financial misrepresentations. Plaintiff also fails to provide particularized facts demonstrating that keying lower-level executives' compensation to Company performance in any way raises a strong inference of scienter. *See e.g., Abrams*, 292 F.3d at 434. The simple act of management setting aggressive goals does not raise a strong inference of scienter. *See Alamosa Holdings*, 382 F. Supp. 2d at 858; *see In re Alpharma Inc. Sec. Litig.,* 372 F.3d 137, 150 (3d Cir. 2004).

C. Plaintiff's insider-trading allegations fail to raise a strong inference of scienter.

Plaintiff also attempts to plead scienter based on defendants' alleged insider trading. Specifically, plaintiff claims that from May 16, 2002 to September 8, 2006, Michael Dell sold 29.61% of his Dell stock, Rollins sold 13.65%, and Schneider sold 49.33%. *See* Complaint ¶ 666. Just as this Court found for the similar insider-trading allegations in the Dell derivative case, *see In re Dell Derivative Litigation*, No. A-06-CA-839-SS, Order at 5-9 (W.D. Tex. Oct. 9, 2007) (Ex. 5),[11] these allegations plainly fail to show suspicious trading.

The Fifth Circuit has recognized that "[i]nsider trading alone cannot create a strong inference of scienter." *Central Laborers'*, 497 F.3d at 553. Rather, it can simply "enhance the strength of the inference of scienter," and it does so only "if the trading occurs at suspicious times or in suspicious amounts." *Id.* at 552-53 (internal quotation marks

[11] While Schneider's sales were not at issue there, the derivative plaintiffs had alleged even greater sales by other defendants.

omitted). "Suspicious" generally equates to "sales [that] are out of line with prior trading practices or at times calculated to maximize personal profit." *Id.* at 553. In examining this issue, "the court must consider plausible nonculpable explanations for such officer trading, as well as inferences that favor" the plaintiff. *Id.* (citing *Tellabs*, 127 S. Ct. at 2510).

To begin with, defendants did not sell in suspicious amounts as a percentage of their total holdings, particularly given the exceedingly long Class Period. *See* Order at 8-9 (Ex. 5). Other courts have likewise held that sales of this magnitude do not suggest an inference of scienter. For example, the Ninth Circuit has rejected insider-trading allegations as support for scienter where several officers sold as much as 55% of their holdings in a little over a year. *See In re Vantive Corp. Sec. Litig.*, 283 F.3d 1079, 1092-96 (9th Cir. 2002). The court noted that the trading was not suggestive of fraud given the "unusually long class period of sixty-three weeks." *Id.* at 1092; *see also Teachers'*, 477 F.3d 162 at 185 (rejecting insider-trading allegations in part because "[a]lleging such a lengthy class period [of 46 months] weakens any inference of scienter that could be drawn from the timing of defendants' trades"). Here, the much longer class period – more than four years – belies any suggestion that the officers' sales of 13%, 29%, and 49% of their holdings are suspicious. Indeed, the allegations are particularly deficient given that plaintiff fails to allege that these amounts differ from defendants' prior trading history. *See, e.g.*, *Central Laborers'*, 497 F.3d at 553 (recognizing that inconsistency with prior trading, while not a per se requirement, is a key factor in the analysis).

Plaintiff's allegations also fail to show anything suspicious about the timing of the sales. Plaintiff alleges that the timing was suspicious because "the Individual

Defendants' trades all followed fraudulent earnings announcements." Complaint ¶ 667. Defendants sold stock at many different times throughout the Class Period, however, often weeks or months after the earnings announcements. *See id.* ¶ 670. Of course, if sales two months after quarterly announcements were to qualify as suspicious, *see, e.g., id.* ¶ 670(e), then a sale at *any time* would be suspicious. Furthermore, defendants sold just as consistently after Dell had allegedly *understated* earnings as when it allegedly overstated earnings. *See id.* ¶¶ 670(a), (e), (f), (h). If defendants knew of the alleged fraud, then it would make no sense for them to sell stock after understating Dell's earnings, which would presumably depress Dell's stock price. Since the sales were spread out over the entire Class Period without any relationship to the statements that supposedly fraudulently increased the stock price, the sales negate scienter. *See Nathenson*, 267 F.3d at 420 (rejecting insider-trading claims where a director sold his stock "at times that were unrelated to any Company announcements"). As in *Vantive*, "the class period alleged is so long, and the virtually identical allegations recycled throughout the complaint so many times, that it becomes difficult to see how particular stock sales would strengthen allegations that particular statements were uttered with [scienter] at the times they were made." 283 F.3d at 1093.

Plaintiff also argues that the trades were suspicious because "during the 'peak' of the fraud, all three Individual Defendants traded consistently and in the same quarters, including the quarter in which the Company's stock price reached its highest point in the Class Period." Complaint ¶ 667. The facts alleged demonstrate, however, that the sales were consistent, and were no greater at the "peak" than in prior quarters. *Compare id.* ¶ 670(c) *and* (d) *with* (h) (showing that trading at the "peak" in December 2004 was virtually identical to trading in the summer and fall of 2003). Indeed, the average stock price for defendants' sales during the class period was $32.78 for Michael Dell, $34.30 for Rollins, and $33.60 for Schneider, all well below the high of $42.57. *See id.* ¶ 666. The numerous sales that occurred at lower prices, "when the price of stock continued to increase in the several months following these sales," creates "further doubt that [defendants were] operating on 'inside knowledge.'" *Vantive*, 283 F.3d at 1093-94.

Plaintiff's last argument for suspicious timing is that "all three Individual Defendants stopped selling stock before the SEC investigation began in August 2005." Complaint ¶ 667. In reality, though, Michael Dell had stopped selling in November 2004; Rollins in December 2004; and Schneider in May 2005. *See id.* ¶ 670 & App. 3. As this Court found in the derivative litigation, this gap belies the idea of suspicious timing. *See In re Dell Derivative Litig.*, Order at 9 (Ex. 5). In addition, "the complaint fails to address whether the [defendants] traded because options were expiring or other restrictions on liquidity dictated the timing of the trades." *Id.* (internal citation omitted). In any event, if, as Plaintiff contends, defendants knew of the fraud and planned to unwind the scheme when they found out about the SEC investigation, then they would have sold stock after learning of the investigation. Instead, each of the defendants retained his Dell holdings, which "indicates that [they] did not possess scienter regarding the alleged fraud, because otherwise [they] would have sold these shares before the price fell." *Central Laborers'*, 497 F.3d at 553.

Finally, plaintiff points to the sales of non-defendant officers and directors, *see* Complaint ¶ 666, which are irrelevant because the Complaint does not allege that these individuals made or knew of any misstatements. *See In re Cyberonics Inc. Sec. Litig.*, 523 F.

Supp. 2d 547, 554 n.10 (S.D. Tex. 2007). Moreover, for these non-defendants, plaintiff fails to allege anything about the percentage of holdings sold, the timing of sales, or prior trading history to suggest suspicious trading. As for the SEC proceedings against certain Dell employees for alleged insider trading, *see* Complaint ¶ 666, these proceedings have nothing to do with fraudulent misstatements, but rather with purportedly selling in advance of poor earnings announcements. *See id.*, App. 2. Thus, the SEC proceedings provide no support for the alleged fraud here.

In sum, defendants sold consistently, often at far below the high price, even when they were supposedly understating earnings; they retained a majority of their holdings throughout the four-year class period; and they made no sales after learning of an SEC inquiry. The allegations wholly fail to support a cogent and compelling inference of scienter. Instead, the most plausible inference from such trading is that they had no knowledge of any alleged misstatements.

D. Plaintiff's reliance on Dell's restatement fails to raise a strong inference of scienter.

The existence of the restatement does not absolve plaintiff of its burden to plead facts with sufficient particularity to show that defendants actually knew that the public statements were wrong. The Fifth Circuit has made clear that "the mere publication of inaccurate accounting figures or failure to follow GAAP, without more, does not establish scienter. The party must know that it is publishing materially false information, or must be severely reckless in publishing such information." *Abrams*, 292 F.3d at 432; *accord Central Laborers'*, 497 F.3d at 549, 552 (affirming dismissal of 10b-5 action despite company's restatement of two-and-a-half years of financials); *Fin. Acquisition,* 440 F.3d at 290 (affirming dismissals of 10b-5 action involving restatement relying solely on failure to follow accounting standards). The only allegation regarding the restatement that actually touches on scienter is that "account balances were reviewed, sometimes at the request or with the knowledge of senior executives, with the goal of seeking adjustments so that quarterly performance objectives could be met." Complaint ¶ 14 (quoting Dell Inc., Annual Report (Form 10-K) at 37 (Oct. 30, 2007). As explained below, however, this allegation does not raise a strong inference of scienter against any of the defendants.

1. The restatement does not identify any of the individual defendants as having knowledge of the alleged fraud.

The restatement never says that Michael Dell, Rollins, or Schneider had any knowledge of the alleged fraud, and the restatement disclosures' reference to "senior executives" cannot support an allegation of scienter against the named defendants. Critically, plaintiff fails to identify those "senior executives" or to otherwise tie this allegation specifically to the defendants. In *Southland*, the Fifth Circuit held that allegations against "defendants" and "[Company] management" were insufficient to give rise to a strong inference of scienter. 365 F.3d at 374-75. Similarly, the Northern District of Texas dismissed a plaintiffs' complaint for failing to raise an inference of scienter, because it "allege[d] that irregularities were reported to unnamed 'senior management,' but d[id] not allege that irregularities were reported to the Individual Defendants." *Odyssey Healthcare*, 424 F. Supp. 2d. at 889; *see also BearingPoint*, 525 F. Supp. 2d at 772 (dismissing complaint involving financial restatement because allegations against groups, including "senior managers," were insufficient to allege scienter for securities fraud). Here, plaintiff's allegations similarly fall short of establishing scienter.

2. Plaintiff cannot impute knowledge to the Company from unnamed "senior executives" as to unidentified misstatements.

The Complaint fails to establish a strong inference of scienter against Dell because it fails to plead sufficiently particularized facts to establish the same inference as to Michael Dell, Rollins, Schneider, or any other specific individual. Plaintiff relies on the restatement disclosures to allege scienter as to "senior executives," but it cannot use these unidentified persons to establish the scienter of the Company. This lack of specificity does not satisfy the PSLRA's particularity requirement. *See Southland*, 365 F.3d at 362 ("plaintiffs must … identify the speaker"). Also, as the Seventh Circuit recently explained, plaintiffs cannot "name 'management' as a defendant or, less absurdly, name each corporate officer" because it would violate the bar on group pleading. *Makor Issues & Rights Ltd. v. Tellabs Inc.*, 513 F.3d 702, 710 (7th Cir. 2008) (*Tellabs II).*[12] Indeed, if plaintiff could use allegations against "senior executives" to show corporate scienter, it would completely subvert the group-pleading restrictions.

Furthermore, even if the "senior executives" need not be identified, plaintiff fails to allege which misstatements were known to be false. Plaintiff's allegation refers to "account balances" that were "sometimes" knowingly reviewed, Complaint ¶ 14, but it does not state which account balances it concerns, the amounts, or whether or when any such

[12] While the court states that "it is *possible* to draw a strong inference of corporate scienter without being able to name the individuals who concocted and disseminated the fraud," it only recognizes such a possibility where there is "so dramatic an announcement [that it] would have been approved by corporate officials sufficiently knowledgeable about the company to know the announcement was false." *Tellabs II*, 513 F.3d at 710. As an example, the Court notes that "General Motors announced that it had sold one million SUVs in 2006, and the actual number was zero." *Id.* There are no such "dramatic" announcements alleged in the Complaint, which Dell officials would have to know were false; to the contrary, the restatement involved less than 1% of total revenue over the Restatement Period.

resulting adjustments took place. This lack of specificity does not satisfy the PSLRA's particularity requirement. *See Southland*, 365 F.3d at 362 (plaintiffs must "state not only the time, place, the identity of the speaker, and the content of the alleged misrepresentation, but also … explain why the challenged statement or omission is false or misleading"). Indeed, the PSLRA makes clear that plaintiff must, "*with respect to each act or omission* alleged to violate [the 1934 Act], 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) (emphasis added).

Where, as here, there are numerous misstatements alleged over a period of several years, plaintiff must specify the particular statement for which scienter is being alleged. *See Trendsetter Investors, LLC v. Hyperdynamics Corp.*, No. H-06-0746, 2007 WL 172627, at *14 (S.D. Tex. Jan. 18, 2007) ("[T]he plaintiff must plead facts to support a strong inference of scienter as to each defendant for each alleged false or misleading statement… . In cases in which the plaintiff alleges multiple misstatements or omissions, a factual allegation suggesting that a defendant knew that one particular statement was false or misleading might be irrelevant to the question of whether that defendant knew that a different statement was false or misleading."); *accord In re OCA, Inc. Sec. and Derivative Litig.*, No. 05-2165, 2006 WL 3747560, at *17 n.7 (E.D. La. Dec. 14, 2006). Moreover, plaintiff fails to allege that the misstatements at issue – i.e., those for which the "senior executives" had scienter – were material. The knowledge of unidentified statements, which are not alleged to be material, cannot form the basis of a Section 10(b) claim.

E. Plaintiff fails to show that defendants knowingly or recklessly violated a duty to immediately disclose the existence of an informal SEC investigation.

Plaintiff's allegation that defendants failed to disclose the SEC informal inquiry, *see* Complaint ¶¶ 13, 17, 77, 615-16, provides no basis for an inference that defendants knowingly or recklessly ignored a duty to disclose such an informal inquiry.[13] Indeed, there is no clear authority establishing a duty of immediate disclosure for informal SEC inquiries. *See Basic Inc. v. Levinson*, 108 S.Ct. 978, 987 n.17 (1987) (noting that "[s]ilence, absent a duty to disclose, is not misleading under Rule 10b-5.") To the contrary, the timing of such disclosures is generally a matter of business judgment, *see, e.g. Berger v. Beletic,* 248 F. Supp. 2d 597, 604 (N.D. Tex. 2003); *In re N. Telecom Ltd. Sec. Litig.,* 116 F. Supp. 2d 446, 458 (S.D.N.Y. 2000), and there certainly is no established duty of immediate disclosure sufficient to give rise to an inference that defendants knowingly or recklessly misled shareholders by failing to disclose the informal inquiry.[14]

Furthermore, plaintiff does not identify what, if any, information defendants had regarding the SEC inquiry that would have warranted immediate disclosure. Plaintiff fails to allege what defendants understood about the nature of the informal inquiry, whether it was material, or that it needed to be disclosed. Nor does plaintiff allege that the informal

[13] "The sources of a person's duty to disclose information under the federal securities laws are found either in express mandates of the statutes and rules promulgated under them or in the general antifraud provisions of the statutes and rules." Victor Brudney, *A Note on Materiality and Soft Information Under the Federal Securities Laws*, 75 VA. L. REV. 723, 726-27 (1989) (footnotes omitted).

[14] *See, e.g.*, Commissioner Paul S. Atkins, Remarks before the U.S. Chamber Institute for Legal Reform (Feb. 16, 2006) (available at http://www.sec.gov/news/speech/spch021606 psa.htm.).

inquiry provided defendants with knowledge of any of the specific accounting issues alleged in the Complaint. Without such particularized allegations, there can be no inference of scienter from the mere existence of an investigation. *See e.g., In re Abbot Labs. Sec. Litig.,* 813 F. Supp. 1315, 1319 (N.D. Ill. 1992) (in the absence of allegations regarding "purpose or scope of the investigation" that allegedly should have been disclosed, "there is no way of knowing whether [the defendant] knew, or should have known, that the investigation warranted discussion or disclosure"). In short, here, too, the Complaint fails to satisfy the scienter requirement of the PSLRA.

III. PLAINTIFF'S ALLEGATIONS REGARDING DEFENDANTS' POSITIVE OPINIONS AND PROJECTIONS ABOUT DELL DO NOT STATE A SECURITIES FRAUD CLAIM.

In addition to the foregoing bases for dismissal of the Complaint, a number of the statements alleged as fraudulent in the Complaint are not actionable because they amount to nothing more than defendants' positive opinions and projections about Dell's business. Such statements cannot establish securities fraud, which requires a plaintiff to prove the falsehood of historical facts, not hopes and beliefs. *See Rosenzweig*, 332 F.3d at 869 (noting that investors' reliance on facts, and statements of sweeping corporate optimism are insufficient to perpetrate a fraud on the market). Specifically, plaintiff's allegations regarding defendants' generalized optimism are not actionable as a matter of law for at least two reasons: (1) they are vague statements of corporate puffery and/or (2) they are forward-looking statements protected by the safe harbor provisions of the PSLRA.

A. The allegedly false statements concerning Dell's business model are immaterial puffery.

Many of the alleged false and misleading statements constitute what the law characterizes as mere puffery. It is Fifth Circuit law that "generalized, positive statements about the company's competitive strengths, experienced management, and future prospects are not actionable because they are immaterial." *Southland*, 365 F.3d at 372; *see also Rosenzweig*, 332 F.3d at 869. Puffery cannot support a securities fraud claim because investors and analysts "rely on facts in determining the value of a security," and generalized statements "are certainly not specific enough to perpetrate a fraud on the market." *Southland*, 365 F.3d at 372 (quoting *Raab v. Gen. Physics Corp.*, 4 F.3d 286, 290 (4th Cir. 1993)); *see also Rosenzweig*, 332 F.3d at 869 (holding plaintiff's puffery allegations inactionable, and noting that a company is "under no duty to cast its business in a pejorative, rather than a positive, light").

For example, plaintiff asserts that defendants "tout[ed] the Company's continued financial success as the result of its unique business model." Complaint ¶ 10. In support of their allegations, plaintiff cites to statements made by defendants regarding (1) the strengths of Dell's business model, (2) the Company's strategy for growth and profitability, and (3) Dell's goal to maximize benefits for investors and customers. Examples of the types of alleged misrepresentations include the following:

- "'[W]e are confident that our financial and operating model will allow us to outperform the market yet again, as we maintain our focus on profitably taking share and maximizing operating income.'" *Id.* ¶ 179.
- "'Management believes that the strength of Dell's direct-to-customer business model, as well as its strong liquidity position, makes Dell better positioned than its competitors to continue profitable market share growth in any business climate.'" *Id.* ¶ 319.

- "'No one has higher expectations for Dell over time than we do, and we're constantly driving for excellence on behalf of customers and shareholders.'" *Id.* ¶ 434. [15]

Such generalized statements of business prospects and objectives cannot serve as the basis for a securities fraud claim. In fact, courts in this circuit have consistently dismissed similar allegations based on the principles outlined above. *See, e.g., Taubenfeld v. Hotels.com*, 385 F. Supp. 2d 587, 592-93 (N.D. Tex. 2004) (holding that no reasonable investor could rely on disclosures such as "'we're seeing very strong growth'" and "'we are extremely profitable'"); *In re Blockbuster Inc. Sec. Litig.*, No. 3:03-CV-0398, 2004 WL 884308, *7-8 (N.D. Tex. April 26, 2004) (dismissing vague expressions of corporate optimism such as "'[w]e undertook a number of key initiatives to strengthen our core business'" and "'[o]ur first quarter performance speaks to the strengths of our business and validates the strategy that we implemented last year'"); *In re Sec. Litig. BMC Software, Inc.*, 183 F. Supp. 2d 860, 891-92 (S.D. Tex. 2001) (finding that statements characterizing the company's business performance as "'better than expected'" and "'encourag[ing]'" were inactionable puffery).

B. The allegedly false statements concerning predictions of Dell's future performance are protected by the safe-harbor provision of the PSLRA.

Plaintiff also attacks defendants' predictions of future business performance, but projections of this type are protected by the PSLRA's safe harbor provision. Congress enacted the safe harbor "to allow public companies to disclose their projections and plans without the threat of abusive litigation." *Alamosa Holdings,* 382 F. Supp. 2d at 844. Under

[15] *See also, e.g.,* Complaint ¶¶ 161, 166, 178, 185, 196-99, 204, 213, 218, 223, 247, 249, 250, 268, 289, 294, 310, 313, 316, 340, 348, 349, 369, 373, 381, 383, 402, 409, 412, 441, 460, 464, 473, 493, 521, 526, 546, 584, 587, and 606 (containing similarly generalized and immaterial statements regarding Defendant's competitive strengths and future prospects).

the PSLRA, forward-looking statements[16] are not actionable to the extent that (1) they are immaterial or identified as forward-looking and accompanied by meaningful cautionary language, or (2) plaintiffs fail to prove that the forward-looking statement was made with knowledge of its falsity. *Southland*, 365 F.3d at 371 (clarifying that the safe harbor consists of "two independent prongs") (citing 15 U.S.C. § 78u-5(c)(1)); *see also In re Administaff, Inc. Sec. Litig.*, No. Civ. A. H-03-2082, 2006 WL 846378, at *6-9 (S.D. Tex. Mar. 30, 2006) (applying safe harbor to allegedly misleading statements and dismissing plaintiff's claims); *Alamosa Holdings*, 382 F. Supp. 2d at 844-47 (same). The predictive statements relied upon by plaintiff fail both prongs.

The Complaint cites to financial projections in Dell press releases, quarterly earnings conference calls, and SEC filings, but each such statement was identified as forward-looking and accompanied by meaningful cautionary language.[17] The PSLRA's requirement that a forward-looking statement include "meaningful" cautionary language "calls for 'substantive' company-specific warnings based on a realistic description of the risks applicable to the particular circumstances." *Southland*, 365 F. 3d at 372. Cautionary language must "detail what kind of misfortunes could befall the company," but it "need not list the specific risk factor alleged to have rendered the forward-looking statement false." *Blockbuster*, 2004 WL 884308, at *5 (internal quotations and citations omitted).

[16] *See* 15 U.S.C. § 78u-5(i)(1) (defining forward-looking statements to include statements "containing a projection of revenues, income (including income loss), earnings (including earnings loss) per share, capital expenditures, dividends, capital structure, or other financial items").

[17] *See, e.g.*, Complaint ¶¶ 161, 180, 216, 224, 244, 289, 311, 374, 403, 408, 410, 411, 434, 463, 465, 494, 510, 517, 522, 537, 547, 552, 564, 599, and 606 (containing references to Dell's expected, anticipated, and projected financial results for Q2 FY03 through Q2 FY07).

Each 10-K identified by plaintiff contains a lengthy discussion of Dell's business risks, including not only a list of risk factors, but also a paragraph explanation of how each factor could impact Dell's future performance. *See, e.g.*, Dell Inc., Annual Report (Form 10-K), at 7-9 (Apr. 28, 2003) (Ex. 6), Dell Inc., Annual Report (Form 10-K), at 7-9 (Apr. 12, 2004) (Ex. 7), Dell Inc., Annual Report (Form 10-K), at 7-10 (Mar. 8, 2005) (Ex. 8), and Dell Inc., Annual Report (Form 10-K), at 13-15 (Mar. 15, 2006) (Ex. 9). Furthermore, in addition to the list of company-specific risk factors commonly found in Dell's 10-Qs and earnings press releases, those disclosures always include a warning that "[a]ctual results in future periods may differ materially from those currently expected or desired because of a number of risks and uncertainties" and refer the reader to Dell's 10-Ks for further details on each risk. *See* Dell 10-Qs and Press Release excerpts for Q1FY03 through Q1FY07 (Exs. 10-11); *see In re Michaels Stores, Inc. Sec. Litig.*, No. Civ. A. 3:03-CV-0246, 2004 WL 2851782 at *5 (N.D. Tex. Dec. 10, 2004) (noting that cautionary language incorporated by reference in a written forward-looking statement is sufficient "when the reference is clear and explicit so that the referenced cautionary language can fairly be viewed as part of the context surrounding the written forward-looking statement"). And, each quarterly earnings conference call included a warning that outlook numbers are forward-looking and referred listeners to the cautionary statements contained in Dell's press releases and SEC filings. *See* Dell earnings call transcript excerpts for Q1FY03 through Q2FY07 (Ex. 12); *see Southland*, 365 F.3d at 372 (noting that oral statements are protected by the safe harbor if they include a statement that "additional information that could cause actual results to differ materially is contained in a readily-available written document … includ[ing] documents filed with the SEC").

Because Dell's forward-looking statements were accompanied by meaningful, company-specific warnings of potential risks, defendants' projections of future financial results are protected by the safe harbor's first prong. *See id.* As explained previously, plaintiff has likewise failed to plead with particularity that defendants acted with scienter, much less that they made their projections with actual knowledge that they were false. Accordingly, defendants are also protected by the second prong of the safe harbor.

IV. PLAINTIFF'S SECTION 20(a) AND SECTION 20A CLAIMS ARE LIKEWISE DEFICIENT.

A. Plaintiff's "control person" claims Section 20(a) should be dismissed because Plaintiff has failed to allege a predicate violation of Section 10(b).

Plaintiff's "control person" claims against Michael Dell, Rollins, and Schneider fail as a matter of law because plaintiff failed to state a "predicate" Section 10(b) claim, and thus "necessarily failed" to state a Section 20(a) claim. *Lovelace v. Software Spectrum, Inc.*, 78 F.3d 1015, 1021 n.8 (5th Cir. 1996).

B. Plaintiff's "insider trading" claims under Section 20A should be dismissed because plaintiff has failed to allege a predicate violation of Section 10(b).

Plaintiff's "insider trading" claims against Michael Dell, Rollins, and Schneider also fail as a matter of law because, like Section 20(a), liability under Section 20A requires "a requisite independent, predicate violation of the Exchange Act." *In re Enron Corp. Sec. Derivative & ERISA Litig.*, 258 F. Supp. 2d 576, 599 (S.D. Tex. 2003) (citing 15 U.S.C. § 78t-1(a)). Moreover, plaintiff must adequately allege an Exchange Act Violation against *each* *defendant*. *See In re Enron Corp. Sec., Derivative & ERISA Litig.*, No. MDL-1446, 2003 WL 21418157, at *7-8 (S.D. Tex. Apr. 24, 2003) (dismissing Section 20A claim against one defendant for failure to allege a predicate violation, while allowing Section 20A claims to go forward against other defendants). Here, plaintiff has failed to state an Exchange Act violation as to any of the individual defendants.

CONCLUSION

For the foregoing reasons, defendants Dell Inc., Michael S. Dell, Kevin B. Rollins, and James M. Schneider respectfully request that the Complaint be dismissed with prejudice and that judgment be entered in favor of defendants.

March 11, 2008

Respectfully submitted,

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