No. _____

In the Supreme Court of the United States

QUALITY SYSTEMS, INC.; STEVEN T. PLOCHOCKI; PAUL A. HOLT; SHELDON RAZIN,
Petitioners,

v.

CITY OF MIAMI FIRE FIGHTERS' AND POLICE OFFICERS' RETIREMENT TRUST; ARKANSAS TEACHER RETIREMENT SYSTEM,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT FOR THE NINTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

In order to give companies breathing room to make forecasts about the future and provide more information to investors, the Private Securities Litigation Reform Act of 1995 (PSLRA) contains a safe-harbor provision that shields from liability "forward-looking statements" that are "accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement." 15 U.S.C. § 78u-5(c)(1)(A)(i).

The courts of appeals are divided over the proper interpretation of the PSLRA's safe harbor. In this case, the Ninth Circuit held that the PSLRA's safe harbor does not apply when a company's forward-looking projection is accompanied by a non-forward-looking statement that the plaintiff alleges is false or misleading—unless the company expressly *admits* that the non-forward-looking statement is false or misleading. App. 27a-28a, 31a-32a. The Ninth Circuit's admission-of-falsity requirement establishes a new extreme among those circuits that have chipped away at the PSLRA's safe harbor.

The question presented is as follows:

Whether or in what circumstances a defendant must admit that *non*-forward-looking statements are false or misleading, in order to be protected by the PSLRA safe harbor for *forward*-looking statements.

RULE 29.6 STATEMENT

Quality Systems, Inc. is a publicly traded company and has no parent corporation. No publicly held corporation or other publicly held entity owns 10 percent or more of its stock.

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

Page

APPENDIX

TABLE OF AUTHORITIES

Page(s)

CASES

TABLE OF AUTHORITIES—Continued

Page(s)

TABLE OF AUTHORITIES—Continued

Page(s)

STATUTES

TABLE OF AUTHORITIES—Continued

Page(s)

LEGISLATIVE MATERIALS

OTHER AUTHORITIES

PETITION FOR A WRIT OF CERTIORARI

Petitioners Quality Systems, Inc.; Steven T. Plochocki; Paul A. Holt; and Sheldon Razin respectfully petition this Court for a writ of certiorari to review the judgment of the United Court of Appeals for the Ninth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. 1a-35a) is reported at 865 F.3d 1130. The opinion of the district court (App. 36a-60a) is available at 60 F. Supp. 3d 1095 (C.D. Cal. 2015). The order of the court of appeals denying rehearing (App. 61a-62a) is unreported.

JURISDICTION

The court of appeals entered its opinion on July 28, 2017. App. 1a. On September 29, 2017, the court of appeals denied a petition for rehearing en banc. *Id.* at 61a-62a. On December 5, 2017, Justice Kennedy granted petitioner's request for an extension to January 26, 2018, to file a petition for writ of certiorari. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The relevant provisions of the Private Securities Litigation Reform Act of 1995 are reproduced in the appendix to this petition. App. 67a-72a.

INTRODUCTION

Two decades ago, Congress enacted the Private Securities Litigation Reform Act of 1995 (PSLRA) to "protect investors and maintain confidence in our capital markets." H.R. Rep. No. 104-369, at 31 (1995) (Conf. Rep.), *as reprinted in* 1995

U.S.C.C.A.N. 730, 730 (Conf. Rep. No. 104-369). Among other objectives, Congress wanted to encourage companies to provide investors with important forecasts concerning their expected future performance, while also protecting those companies from frivolous lawsuits based on the projections.

To that end, the PSLRA contains a safe-harbor provision that shields from liability any projection about the future—which the Act describes as a "forward-looking statement"—that either (1) is "accompanied by *meaningful cautionary statements* identifying *important factors* that could cause actual results to differ materially from those in the forward-looking statement," or (2) is not "made with actual knowledge" that the statement is false. 15 U.S.C. § 78u-5(c)(1)(A), (B) (emphasis added). No such protection extends to *non*-forward-looking statements (*i.e.*, factual assertions about current or past performance). Non-forward-looking statements thus remain subject to liability under the standards set forth elsewhere in the securities laws.

Since the PSLRA became law, courts of appeals have struggled with how to determine whether the cautionary statements accompanying a defendant's forward-looking projections are sufficiently "meaningful" to trigger the safe harbor under the statute's first prong. Although the circuits generally agree that cautionary language need not identify *all* of the "important factors" that could keep a projection from materializing, they are divided over whether (and how) courts should look beyond the cautionary statements themselves in deciding whether the safe harbor applies. Whereas most courts confine their analysis to the factors identified in the cautionary language actually used by the

company (as Congress intended), some courts look beyond those warnings to consider whether the company failed to mention *other*, unstated risks that it faced when the forward-looking statement at issue was made (going beyond what Congress intended).

In this case, a panel of the Ninth Circuit (Reinhardt, Fletcher, and Paez, JJ.) took the latter approach to a new extreme. Specifically, the court held that the PSLRA safe harbor's "meaningful cautionary language" requirement is not satisfied when a company's forward-looking statement is accompanied by a *non*-forward-looking statement that the plaintiff alleges is false or misleading—unless the company actually admits the falsity of the non-forward-looking statement. App. 27a-28a, 31a-32a. The court reached that holding even though it also expressly recognized that the cautionary language *was* "meaningful"—and would have triggered the safe harbor—if considered solely on its own terms, without reference to the allegedly false non-forward-looking statements. *Id.* at 33a.

The Ninth Circuit's new and categorical rule is a stark outlier that departs from the tests applied by all other circuits and directly conflicts with results reached by other courts in materially identical circumstances. The Ninth Circuit's new rule is also wrong. The PSLRA only requires a company's cautionary language to address its *forward*-looking projections by identifying important factors that could undermine those projections. It does not require companies to identify all important factors, and it certainly does not categorically require them to admit the alleged falsity of *non*-forward-looking statements. The Ninth Circuit's approach has no

basis in the PSLRA's text or history, and it leads to anomalous results that Congress did not intend.

If allowed to stand, the Ninth Circuit's rule will effectively nullify the PSLRA's safe harbor for forward-looking statements. From now on, every time a company fails to meet its previously-disclosed projections and suffers a stock-price drop, securities plaintiffs will argue that the safe harbor does not apply to a company's forward-looking statements because they were accompanied by false non-forward-looking statements. The result will be to broaden the scope of liability in securities cases by eliminating the safe harbor's independent protection for forward-looking statements, and cause companies to stop providing investors with meaningful forecasts and projections. That is precisely the opposite of what Congress wanted the PSLRA to accomplish.

This Court has often granted certiorari to clarify the PSLRA's pleading standards and vindicate Congress's goal of reducing frivolous securities litigation. *See, e.g.*, *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27 (2011); *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008); *Tellabs, Inc. v. Makor Issues & Rights, Ltd.,* 551 U.S. 308 (2007). It should do the same thing here. The Ninth Circuit's rule deepens confusion among the circuits about an important protection designed to create breathing room for companies to make forecasts without fearing nuisance litigation by plaintiffs' lawyers. It also misinterprets one of the PSLRA's core innovations in a way that undermines Congress's main objectives. The petition for certiorari should be granted.

STATEMENT OF THE CASE

This case is a putative securities class action filed by Plaintiffs-Appellants City of Miami Fire Fighters' and Police Officers' Retirement Trust and Arkansas Teacher Retirement System (respondents) against Quality Systems, Inc. (QSI) and several of its executives and directors (collectively, petitioners). The district court granted petitioners' motion to dismiss after concluding that the statements at issue fall within the PSLRA's safe harbor for forward-looking statements, but the Ninth Circuit reversed.

A. Statutory Background

1. Both Congress and this Court have long recognized that private securities fraud actions "can be employed abusively to impose substantial costs on companies and individuals whose conduct conforms to the law." *Tellabs*, 551 U.S. at 313. The threat of such abusive litigation created perverse incentives for companies to avoid publicly disclosing projections about their future economic prospects, out of fear that such projections would trigger lawsuits if and when projections proved wrong. *See* Conf. Rep. No. 104-369, at 42-43. The result of this pernicious "muzzling effect" was to deprive shareholders and investors of some of the "most valuable information [they] could have about a firm"—and thus to undermine the efficient and informed exchange securities in our Nation's capital markets. *Id.* (quoting former SEC Chair Richard Breedan).

In 1995, Congress enacted the PSLRA to address these concerns. Among other reforms, the PSLRA imposed "heightened pleading requirements" for fraud claims, "limit[ed] recoverable damages and attorney's fees," restricted "the selection of (and

compensation awarded to) lead [class-action] plaintiffs," mandated "sanctions for frivolous litigation," and authorized "a stay of discovery pending resolution of any motion to dismiss. *Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 81 (2006). As this Court has recognized, these measures operate "[a]s a check" against "abusive litigation." *Tellabs*, 551 U.S. at 313.

Congress also used the PSLRA to reverse the longstanding incentives against more fulsome public disclosure of a company's financial performance and future prospects. It did so by creating a statutory safe harbor insulating companies from liability for certain forward-looking statements covered by the Securities and Exchange Act of 1934, including a company's press releases, its conference calls with analysts and investors, and its periodic filings with the Securities and Exchange Commission. *See* 15 U.S.C. § 78u-5; *see also id.* § 77z-2 (identical safe harbor applicable to statements covered by Securities Act of 1933). The proper interpretation of that safe harbor is the central issue in this case.

2. The PSLRA's safe-harbor provision defines "forward-looking statement" to encompass virtually any projection of a company's revenues, plans, or economic performance, as well as any assumptions underlying those projections. *Id.* § 78u-5(i)(1). Subject to certain exceptions, it shields such projections from liability so long as either (1) the projection is "accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement," or (2) the defendant has not made the projection "with actual knowledge" that it is false. *Id.* § 78u-5(c)(1)(A), (B).

Congress recognized that the two-prong safe harbor would "permit[] greater flexibility" to companies and their executives. Conf. Rep. No. 104-369, at 43. Under the first prong, a company can insulate its projections from liability by providing warnings ("meaningful cautionary statement[s]") indicating to the public that whether its projections will materialize will turn on variables ("important factors") outside the company's direct control or ability to forecast with certainty. *Id.*

Congress indicated that whether a projection is eligible for protection under the first prong entails a purely *objective* inquiry and does not permit any consideration of the speaker's subjective "state of mind." *Id.* at 44. It also noted that the first prong does *not* require the company to warn about *all* "important factors," and it specifically declared that "[f]ailure to include the particular factor that ultimately causes the forward-looking statement not to come true will not mean that the statement is not protected by the safe harbor." *Id.*

The safe harbor's second prong provides an alternative—and entirely independent—basis for rejecting securities liability based on a forward-looking statement. Unlike the first prong, the second prong requires a *subjective* analysis and requires a securities claim to be dismissed unless the plaintiff has plausibly alleged that the company made the forward-looking statement "with actual knowledge" that it was false. 15 U.S.C. § 78u-5(c)(1)(B)(i); *see* Conf. Rep. No. 104-369, at 44-45.

B. Facts and Procedural History

1. QSI develops electronic healthcare record software ("EHR") for medical and dental providers. Respondents allege that on at least 10 different occasions between May 26, 2011 and July 25, 2012 (the Class Period), petitioners violated Section 10(b) of the Securities Exchange Act of 1934 by making false or misleading statements relating to the company's economic performance. App. 1a, 19a-20a, 28a-30a, 32a (cataloguing allegations).

As relevant here, the complaint alleges that on seven of those occasions, petitioners made "mixed statements" incorporating independently-actionable forward-looking and non-forward-looking statements. *Id.* at 19a-20a, 28a-30a (noting statements made on 6/9/11, 10/27/11, 12/14/11, 1/26/12, 2/7/12, 5/9/12, and 5/17/12). The complaint further alleges that, on two occasions, petitioners made actionable forward-looking statements *without* accompanying non-forward-looking statements. *Id.* at 32a (noting statements made on 1/9/12 and 5/14/12). And on one occasion, petitioners allegedly made an actionable non-forward-looking statement without any corresponding forward-looking statement. *Id.* at 19a, 30a-32a (statement made on 11/7/11).

In general, the challenged *non*-forward-looking statements involved assertions about QSI's then-current operations and results. *Id.* at 19a-20a, 28a-30a. For example, the complaint points to various statements by respondents indicating that QSI's sales pipeline "keeps growing," "continues to build to record levels," and "has grown every quarter [since February 2009]." *See id.* at 19a-20a. The challenged *forward*-looking statements involved projections of

QSI's financial performance for the 2012 and 2013 fiscal years, including specific forecasts of its likely growth in revenue and earnings per share, as well as of the size of its sales pipeline. *Id.* at 28a-30a. Notably, petitioners qualified their forward-looking statements with cautionary language making clear that the projections were subject to a wide array of risks and uncertainties. App. 32a-33a, 46a-48a.

2. In October 2014, the district court granted petitioners' motion to dismiss for failure to state a claim. *See id. at* 43a-50a. As relevant here, the court concluded that, even accepting the allegations in the complaint as true, petitioners' forward-looking statements were protected by *both* prongs of the PSLRA safe harbor because (1) they were accompanied by meaningful cautionary language, and (2) respondents' allegations were "vague[]," "wholly conclusory," and "insufficient" to establish petitioners' "actual knowledge of falsity." *Id.* at 46a-49a.

As to the cautionary language, the district court emphasized that petitioners had properly

> identifie[d] specific factors that may affect the forward-looking statements including, *inter alia*, volume and timing of systems sales and installations, length of sales cycles and installation process, impact of incentive payments under the [American Recovery and Reinvestment Act] on sales, the development by competitors of new or superior technologies, and political or regulatory influences in the healthcare industry.

Id. at 47a. The court further noted that the cautionary statements were "specific to QSI's [electronic health record] business and do not constitute generic warnings that any general business or corporation could import," and it rejected respondents' assertion that they were mere "boilerplate." *Id.* at 47a-48a.

The district court also rejected respondents' claims based on petitioners' non-forward-looking statements, explaining that those statements amounted to non-actionable puffery. *Id.* at 45a.

3. The Ninth Circuit reversed. The court first held that, accepting respondents' allegations as true, respondents had properly stated a claim with respect to the non-forward-looking statements. App. 12a, 16a-27a. The court rejected the district court's characterization of those statements as puffery, and it further held that respondents had sufficiently alleged petitioners' scienter with respect to the statements. *Id.* at 20a-27a. The court relied heavily on the assertions of various confidential witnesses, including some who had left QSI over a year before the Class Period, and some low-level employees who were unable to offer testimony concerning petitioners' state of mind in making the challenged statements. *See id.* at 9a-11a, 23a-27a.

The court then held that the PSLRA safe harbor did not protect the challenged forward-looking statements that were made as part of "mixed statements" alongside non-forward-looking statements. *Id.* at 27a-34a. In doing so, the court announced a new rule governing situations "[w]here a forward-looking statement is accompanied by a non-forward-looking factual statement that supports the forward-looking statement." *Id.* at 27a.

Specifically, the court declared that if the *non*-forward-looking statement is alleged to be false, the safe harbor will not protect the *forward*-looking statement unless the defendant's cautionary language actually *admits* that falsity:

> If the non-forward-looking statement is materially false or misleading, it is likely that no cautionary language—short of an outright admission of the false or misleading nature of the non-forward-looking statement—would be 'sufficiently meaningful' to qualify the statement for the safe harbor.

Id. at 27a-28a; *see also id.* at 31a. The court cited no statutory or other authority for this added, admission-of-falsity requirement.

Applying its new rule, the court held that, "[b]ecause [petitioners] made materially false or misleading non-forward-looking statements . . . , virtually no cautionary language short of an outright admission that the non-forward-looking statements were materially false or misleading would have been adequate." *Id.* at 32a. And lacking such an admission, the court found the cautionary language inadequate. The court rejected petitioners' alternative argument that the safe harbor's second prong—which eliminates liability unless plaintiff can establish defendant's "actual knowledge" that a forward-looking statement is false—protected their forward-looking statements. *Id.* at 33a-34a.

Finally, the court agreed with petitioners that the PSLRA safe harbor protected the freestanding forward-looking statements that were *not* accompanied by challenged non-forward-looking

statements. *Id.* at 32a-33a. The court held that the cautionary language accompanying *those* statements "was sufficiently meaningful to qualify for the safe harbor." *Id.* at 33a. It reached that conclusion even though that cautionary language was word-for-word identical to the language that had accompanied many of the other forward-looking statements, as to which the court had *rejected* the safe harbor. *Id.* (explaining that the language was sufficient due to "the absence of any materially false or misleading non-forward-looking statements").

REASONS FOR GRANTING THE WRIT

The Ninth Circuit's decision in this case not only injects additional confusion into an important area of securities law, but drives a stake into the PSLRA's safe harbor provision. Congress sought to protect companies and their employees from lawsuits based on forward-looking projections, subject only to the requirement that those projections be qualified by "meaningful cautionary language" identifying some of the "important factors" that might prevent the projections from materializing. The Ninth Circuit's admission-of-falsity requirement for *non*-forward-looking statements flouts that standard and renders inadequate cautionary language that—by the court's own admission—*does* identify such factors. Its analysis rewrites the statute, departs from the tests adopted by all other circuits, and will effectively nullify the safe harbor in practice. This Court should grant certiorari to promote uniformity and vindicate the PSLRA's text and purpose.

A. The Ninth Circuit's Interpretation Of The Safe Harbor Conflicts With Decisions Of Other Courts

As explained above, the first prong of the PSLRA safe harbor insulates a forward-looking statement from liability so long as it is accompanied by "*meaningful cautionary statements* identifying *important factors* that could cause actual results to differ materially from those in the forward-looking statement." 15 U.S.C. § 78u-5(c)(1)(A)(i) (emphasis added). The courts of appeals generally agree that cautionary language can be "meaningful" even if it only identifies some—but not all—"important factors" that could prevent a forward-looking statement from materializing in practice.[1]

Beyond that, however, there is significant confusion and disagreement among the circuits over how they should assess whether cautionary language is sufficiently "meaningful." In particular, the circuits have divided over whether they should (1) focus only on the factors identified by the cautionary language itself, or (2) instead also consider whether that language omits other important factors with the potential to undermine the projection.

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[1] *See, e.g.*, *Arkansas Pub. Emps. Ret. Sys. v. Harman Int'l Indus. Inc. (In re Harman Int'l Indus., Inc. Sec. Litig.)*, 791 F.3d 90, 103 (D.C. Cir. 2015), *cert. denied*, 136 S. Ct. 1167 (2016); *Slayton v. American Express Co.*, 604 F.3d 758, 771, 773 (2d Cir. 2010); *Institutional Investors Grp. v. Avaya, Inc.*, 564 F.3d 242, 256 n.23 (3d Cir. 2009); *Asher v. Baxter Int'l Inc.*, 377 F.3d 727, 732-33 (7th Cir. 2004), *cert. denied*, 544 U.S. 920 (2005); *Helwig v. Vencor, Inc.*, 251 F.3d 540, 558-59 (6th Cir. 2001), *cert. dismissed*, 536 U.S. 935 (2002); *Harris v. Ivax Corp.*, 182 F.3d 799, 807 (11th Cir. 1999).

In this case, the Ninth Circuit joined the circuits that follow the second approach—and then took it to a new extreme by adding a new requirement for situations in which a plaintiff claims that the defendant's forward-looking statement was accompanied by a false or misleading *non*-forward-looking statement. In such circumstances, the court held, cautionary language will only be "meaningful"—and the safe harbor will only apply—if the defendant expressly *admits* that the non-forward-looking statement is false or misleading. That admission-of-falsity requirement starkly deviates from the approach taken by all other courts.

1. When applying the safe harbor's first prong, at least four circuits follow the statutory text and focus *on the cautionary language itself*, examining that language and determining whether it identifies "important factors that could cause actual results to differ materially" from the projection in light of the company's circumstances. 15 U.S.C. § 78u-5(c)(1)(A)(i). Those circuits do not consider the defendant's state of mind or whether the defendant *omitted* important factors. In particular, the Third and Eleventh Circuits have explicitly embraced the PSLRA legislative history stating that "[t]he first prong of the safe harbor requires courts to examine *only the cautionary statement* accompanying the

forward-looking statement."[2] The Sixth and Eighth Circuits have followed the same basic approach.[3]

When analyzing the factors identified in the cautionary language at issue, these courts generally consider whether that language is "extensive," "specific," and "tailored" to the projections at issue—as opposed to being "vague" or "boilerplate."[4] As the Eleventh Circuit has explained, cautionary language will generally be "meaningful" under this analysis when it "warn[s] of risks of a significance similar to that actually realized." *Harris v. Ivax Corp.*, 182 F.3d 799, 807 (11th Cir. 1999); *see also Helwig v. Vencor, Inc.*, 251 F.3d 540, 559 (6th Cir. 2001) (embracing this test). In such circumstances, the language puts investors "sufficiently on notice of the danger of the investment to make an intelligent decision about it according to [their] own preferences for risk and reward." *Harris*, 182 F.3d at 807.

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[2] *See OFI Asset Mgmt. v. Cooper Tire & Rubber*, 834 F.3d 481, 503 (3d Cir. 2016) (emphasis added) (quoting Conf. Rep. No. 104-369, at 44); *Edward J. Goodman Life Income Tr. v. Jabil Circuit, Inc.*, 594 F.3d 783, 795 (11th Cir. 2010) (same); *Harris*, 182 F.3d at 803.

[3] *Miller v. Champion Enters. Inc.*, 346 F.3d 660, 671-72, 677-78 (6th Cir. 2003) (applying Eleventh Circuit's test from *Harris*, *supra*, and rejecting argument that cautionary language was not "meaningful" due to omission of additional information about the identified risk); *Julianello v. K-V Pharm. Co.*, 791 F.3d 915, 921-22 (8th Cir. 2015) (examining cautionary language only); *Rand-Heart of N.Y., Inc. v. Dolan*, 812 F.3d 1172, 1178-79 (8th Cir. 2016) (same).

[4] *See*, *e.g.*, *Avaya*, 564 F.3d at 256; *Helwig*, 251 F.3d at 558-59; *see also, e.g.*, *Julianello*, 791 F.3d at 921-22; *Rand-Hart*, 812 F.3d at 1178-79.

2. The Seventh and D.C. Circuits take a different approach. Instead of focusing exclusively on the contents of the cautionary statements that the defendant actually made and determining whether those statements identify "important factors" that could undermine the company's projections, the Seventh and D.C. Circuits also consider whether those statements *omitted* important considerations that the defendant faced at the time the forward-looking statement was made. *See Asher v. Baxter Int'l Inc.*, 377 F.3d 727, 729-34 (7th Cir. 2004); *Arkansas Pub. Emps. Ret. Sys. v. Harman Int'l Indus. Inc. (In re Harman Int'l Indus., Inc. Sec. Litig.)*, 791 F.3d 90, 101-08 (D.C. Cir. 2015), *cert. denied*, 136 S. Ct. 1167 (2016).

The Seventh Circuit will reject the safe harbor when the defendant's cautionary language "omit[s] important variables from the cautionary language and so made projections more certain than its internal estimates at the time warranted." *Asher*, 377 F.3d at 734. That court requires the defendant "to point to the *principal* contingencies that could cause actual results to depart from the projection," *i.e.*, "the major risks [the defendant] objectively faced when it made its forecasts." *Id.* (emphasis added). That test has been interpreted to support an examination of the risks about which the defendant was *subjectively* aware at the time it made the projection at issue. *Makor Issues & Rights, Ltd. v. Tellabs, Inc.*, 437 F.3d 588, 598-600 (7th Cir. 2006) (applying *Asher* and rejecting safe harbor based on risks actually known to defendant), *vacated and remanded*, 551 U.S. 308 (2007); *Slayton v. American Express Co.*, 604 F.3d 758, 771 n.8 (2d Cir. 2010) (interpreting *Asher* to require subjective inquiry).

The D.C Circuit embraced a similar approach in *Harman*, where it held that cautionary language cannot be "meaningful" if it is "misleading in light of historical fact[s]"—including if it is misleading *by omission*. 791 F.3d at 97, 102-04. The court rejected the safe harbor because the defendants' cautionary language had failed to warn about one particular factor—the obsolescence of the company's personal navigation device (PND) products—that was an "important factor [ ] that could cause actual results to differ materially from those in the forward-looking statement." *Id.* at 103 (alteration in original) (quoting 15 U.S.C. § 78u-5(c)(1)(A)(i)). The court explained that the defendants were "required to alert investors to the risk of [PND] obsolescence in order to gain safe harbor protection," and that its "*omission*" of such a warning "left a misleading picture" about the company's financial prospects. *Id.* at 103, 105 (emphasis added).

Thus, the D.C. Circuit—like the Seventh Circuit—denies safe harbor protection when a defendant's cautionary language omits a particular important factor, even if that language otherwise warns against other important factors that could undermine the defendant's projection.[5]

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[5] While the Second Circuit has not definitively resolved the extent to which courts should consider omissions when assessing whether cautionary language is "meaningful," it has acknowledged the circuit conflict and expressed support for the Seventh Circuit's approach. *Slayton*, 604 F.3d at 771 & nn.7-8 (stating that the "most sensible" way to determine whether cautionary language is "meaningful" is to follow the Seventh Circuit, and consider whether the language addresses "the major factors the defendants faced at the time the statement was made" by determining "what the defendants knew").

3. In this case, the Ninth Circuit took the Seventh and D.C. Circuit approach to a new extreme. Like those courts, the Ninth Circuit held that courts must assess whether cautionary language is "meaningful" by looking beyond the factors expressly identified in that language. App. 27a-28a, 31a-32a. But then the Ninth Circuit went even further by imposing an affirmative admission-of-falsity requirement. The court held that when a defendant makes false or misleading *non*-forward-looking statements, the safe harbor protects its *forward*-looking statements only if the defendant's cautionary language specifically admits that the non-forward-looking statement is false or misleading. *Id.* The court explained that the failure to make such an admission renders the cautionary language insufficiently "meaningful" and thus forecloses the safe harbor. *Id.*

Notably, the Ninth Circuit reached this conclusion even though it also acknowledged that the cautionary language at issue here itself—if considered on its own, without reference to the non-forward-looking statements—*was* sufficiently "meaningful" to trigger the safe harbor. *Id.* at 32a-33a. Indeed, the court applied the safe harbor to insulate petitioners from liability for the two forward-looking projections that were accompanied by that same cautionary language, but were *not* made together allegedly false or misleading non-forward-looking statements. *Id.*

a. The Ninth Circuit's approach directly contradicts the test adopted by the Third, Sixth, Eighth, and Eleventh Circuits. Whereas the Ninth Circuit will reject application of the safe harbor's first prong based on a defendant's omission (its

failure to admit the falsity of a forward-looking statement), the Third, Sixth, Eighth, and Eleventh Circuits do not consider omissions, and instead assess the meaningfulness of cautionary language by looking to that language and determining whether it identifies important factors capable of undermining the defendant's projection. *See supra* at 14-15.

Moreover, whereas the Ninth Circuit requires cautionary language to warn about a *specific* risk—the risk that an accompanying forward-looking statement is false or misleading—the Third, Sixth, Eighth, and Eleventh Circuits only consider whether the cautionary language "warn[s] of risks of a significance similar to that actually realized," *Harris*, 182 F.3d at 807; *Helwig*, 251 F.3d at 559. Indeed, the Third, Sixth, Eighth, and Eleventh Circuits go out of their way to emphasize that cautionary language is *not* required to identify all of the "important factors" that could interfere with the projection. *See supra* at 13 & n.1, 15.

Unsurprisingly, the Ninth Circuit's approach will lead to different results from those reached in other circuits. For example, in *Institutional Investors Group v. Avaya, Inc.* (*Avaya*), the Third Circuit considered—and rejected—the plaintiff's allegation that false statements of current and historical fact "diluted" the sufficiency of cautionary language accompanying forward-looking projections. 564 F.3d 242, 258 (3d Cir. 2009). In doing so, the court found that the cautionary language at issue was sufficient to protect the defendant's forward-looking statements, even though that language did not address the falsity of accompanying non-forward-looking statements. *Id.* The court reached that conclusion despite later holding that the complaint

plausibly alleged that the non-forward-looking statements were fraudulent. *Id.* at 266-67.

The Third Circuit's decision in *Avaya* is squarely at odds with the Ninth Circuit's decision below. Under the Ninth Circuit's test, the cautionary language in *Avaya* would have been insufficient to trigger the safe harbor for the forward-looking statements, because it contained no admission that the non-forward-looking statements were false or misleading. And under the Third Circuit's test, the cautionary language here—which plainly warns against some important factors that could undermine QSI's projections, as even the Ninth Circuit agreed, *see* App. 33a—would have sufficed to protect petitioners' forward-looking statements.[6]

b. As noted above, the Ninth Circuit's test tracks the approach embraced by the Seventh and D.C. Circuits, insofar as it requires courts to assess whether a defendant's cautionary language has omitted certain factors. But the Ninth Circuit has gone even further than the Seventh and D.C. Circuits by requiring defendants to *expressly admit*

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[6] For other examples of cases in which the Ninth Circuit's rule would clearly require a different result, *see Pension Fund Grp. v. Tempur-Pedic Int'l, Inc.*, 614 F. App'x 237 (6th Cir. 2015); *In re Gold Res. Corp. Sec. Litig.*, 957 F. Supp. 2d 1284 (D. Colo. 2013) (same), *aff'd sub nom. Banker v. Gold Res. Corp. (In re Gold Res. Corp. Sec. Litig.)*, 776 F.3d 1103 (10th Cir. 2015). In both of those cases, the courts held that cautionary language was sufficient to insulate the defendant's forward-looking statements from liability, even though the cautionary language did *not* address (let alone admit the falsity of) the defendant's allegedly false *non*-forward-looking statements. *Pension Fund Grp.*, 614 F. App'x at 243-49 (applying *Miller*); *In re Gold Res. Corp.*, 957 F. Supp. 2d at 1296-97 (applying *Harris*).

the falsity of any false or misleading non-forward-looking statement. Op. 33. By contrast, the Seventh and D.C. Circuits will only deny safe-harbor protection based on an omission in the cautionary language if the omission is of great importance—*i.e.*, if it concerns one of the "major" or "principal" risks that the defendant actually faced. *Asher*, 377 F.3d at 734; *see also Harman*, 791 F.3d at 103-05.

In that respect, the Ninth Circuit's rigid and categorical rule is harsher on defendants than the Seventh and D.C. Circuit approaches and can result in the denial of safe-harbor protection even when the non-forward-looking statement is not especially significant. For obvious reasons, no company is going to include an affirmative *admission of falsity* in its cautionary language, so the Ninth Circuit rule guts the safe-harbor in these circumstances.

In re Akorn, Inc. Securities Litigation, 240 F. Supp. 3d 802 (N.D. Ill. 2017), illustrates how the Ninth Circuit's test will lead to different outcomes. There, the court applied Seventh Circuit precedent and held that the defendant's cautionary language was "meaningful"—and thus that its forward-looking statements were protected by the safe harbor—even though those statements were accompanied by allegedly false non-forward-looking statements. *Id.* at 816-18. The court reached that conclusion even though the cautionary language did not address (let alone admit the falsity of) the non-forward-looking statements. *Id.* at 817. The Ninth Circuit's test would mandate a different result.[7]

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[7] The Ninth Circuit's test is also at odds with the Second Circuit's recent analysis in *Miami Group v. Vivendi, S.A. (In re Vivendi, S.A. Securities Litigation)*, 838 F.3d 223 (2d Cir. 2016).

4. As explained above, the courts of appeals have now embraced at least three distinct interpretations of the PSLRA's safe harbor. The circuit split pre-dates the Ninth Circuit's decision in this case, and it has been widely acknowledged by courts and commentators alike. *See*, *e.g.*, *Slayton*, 604 F.3d at 771 & nn.7-8; Joseph De Simone *et al.*, Asher *to* Asher *and Dust to Dust: The Demise of the PSLRA Safe Harbor?*, 1 N.Y.U. J.L. & Bus. 799, 800 (2005) ("It is beyond cavil that the Seventh Circuit's decision in *Asher* diverges from the other recent circuit court cases . . . ."); Alfred Wang, Comment, *The Problem of Meaningful Language: Safe Harbor Protection in Securities Class Action Suits after* Asher v. Baxter, 100 Nw. U. L. Rev. 1907, 1928-32, 1936-37 (2006) (noting that Seventh Circuit's approach "is at odds . . . with the precedents in the other circuits"). The Ninth Circuit's decision only exacerbates the conflict and confusion.

As a result of the conflict, the same PSLRA provision will be applied to the same facts in fundamentally different ways, depending on the happenstance of where the case arises. To illustrate those disparate results, consider a hypothetical defense contractor whose principal business involves

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There, the court considered whether the safe harbor applied to forward-looking statements that appeared in the same document as allegedly false non-forward-looking statements. *Id.* at 222-23. Although the court rejected application of the safe harbor, it did *not* apply the Ninth Circuit's categorical rule that cautionary language is only sufficient if it admits the false or misleading nature of non-forward-looking statements—even though that rule would have been the most straightforward way of rejecting the defense. *Id.* at 246-47. Instead, the court simply examined the cautionary language itself and concluded that the language was insufficiently detailed and specific. *Id.*

selling armored vehicles to the government. Assume that the company's continued financial success depends on three important factors: (1) the government's strategic decision to focus defense spending on new equipment instead of personnel; (2) the government's decision to remain engaged in a particular armed conflict overseas; and (3) the company's leading competitor's engineering delays in bringing a new model tank to market.

In public statements, the company CEO erroneously states that "2017 was our most profitable year in history" (a non-forward-looking statement), when in fact 2017 was the company's *second* most profitable year. The CEO goes on to project revenue growth of 25% in 2018 (a forward-looking statement). The CEO adds cautionary language warning that the 25% projection is subject to numerous risks and uncertainties, including factors (1) and (2) (the government's focus on equipment and commitment to the armed conflict abroad), but not factor (3) (the engineering problems plaguing its leading rival).

As it turns out, the company ultimately underperforms the 25% growth projection. The company then faces a class action for securities fraud, based on the allegedly false 2018 projection. The company invokes the safe harbor's first prong to defend against liability and promptly terminate the suit. But whether the safe harbor applies would depend entirely on the circuit in which the case is brought.

(1) The Third, Sixth, Eighth, and Eleventh Circuits would say *yes*, the safe harbor applies, because the cautionary language expressly identified two "important factors"—the government's

equipment-vs.-personnel tradeoff, and its decision to stay engaged in the armed conflict—"that could cause actual results to differ materially from those in the forward-looking statement." 15 U.S.C. § 78u-5(c)(1)(A)(i); *see supra* at 14-15.

(2) The Seventh Circuit and D.C. Circuit would say *maybe*, depending on whether the omitted factor—the delays experienced by the contractor's rival in developing a new tank—was one of the "major risks" the contractor faced when the CEO made its projection, *Asher*, 377 F.3d at 734, or whether that omission was so glaring as to render the cautionary language "misleading," *Harman*, 791 F.3d at 97, 102-04. *See supra* at 16-17.

(3) And the Ninth Circuit would say *no*, simply because the 2018 projection was accompanied by a false statement of the contractor's 2017 financial performance—that the company did not *admit* was false. It would reach that conclusion, moreover, even if it also concluded that (1) the CEO's misstatement of 2017 performance was otherwise unintentional, and (2) the cautionary language was otherwise sufficiently "meaningful" (such that the safe harbor would apply but-for the inadvertent mistake with respect to 2017). *See supra* at 18-21.

It hardly takes a crystal ball to predict in which circuit plaintiffs' lawyers would file the suit. Yet Congress hardly intended to invite such forum shopping, and the protection afforded by the safe harbor must be uniform in order to be meaningful.

B. The Ninth Circuit's Interpretation Of The Safe Harbor Is Wrong

The Ninth Circuit's extreme position on the scope of the PSLRA safe harbor cannot be reconciled with the text, structure, or history of the PSLRA.

1. By its terms, the PSLRA safe harbor applies whenever a defendant provides "meaningful cautionary" language identifying "important factors" that could cause actual results to differ materially from a forward-looking projection. 15 U.S.C. § 78u-5(c). That language means what it says: So long as the cautionary language identifies such "important factors," the forward-looking projection is insulated from liability. *See Simmons v. Himmelreich*, 136 S. Ct. 1843, 1848 (2016) ("Congress says what it means and means what it says.").

When applying the safe harbor, courts should therefore take a straightforward approach. First, they should identify the cautionary language at issue. Next, they should consider whether that language itself identifies "important factors" that could keep the forward-looking projection from bearing fruit. If so, then the safe harbor applies. If not, the safe harbor does not apply. This is, as discussed, how the Third, Sixth, Eighth, and Eleventh Circuits approach the safe harbor.

When conducting this analysis, courts must of course ensure that the factors identified by the cautionary language are truly "important," and thus that the language is actually "meaningful." Vague or boilerplate warnings will not suffice, and the cautionary language must convey substantive information that will alert investors to the risk that the projection will not come to pass. But courts may

not conduct a subjective inquiry into the defendant's state of mind; such an inquiry is irrelevant to whether the cautionary language identifies the requisite "important factors." Nor may courts penalize the defendant for failing to identify any *particular* factor. The statute requires cautionary language to identify "important factors," not "*the* important factors" or "*all* important factors." 15 U.S.C. § 78u-5(c)(1)(A)(i).

The PSLRA's legislative history strongly supports this interpretation. As noted above, the purpose of the safe harbor's first prong is to allow courts to dismiss claims at the pleading stage, before discovery, without any inquiry into the defendant's subjective state of mind. As the Conference Report explains:

> The use of the words "meaningful" and "important factors" are intended to provide a standard for the types of cautionary statements upon which a court may, where appropriate, decide a motion to dismiss, without examining the state of mind of the defendant. *The first prong of the safe harbor requires courts to examine* ***only*** *the cautionary statement accompanying the forward-looking statement.*

Conf. Rep. No. 104-369, at 44 (emphasis added).

Elsewhere, the Report further emphasizes that the inquiry should focus on the actual factors identified by the cautionary language, and *not* on whether that language omitted any other factors:

> The Conference Committee expects that the cautionary statements identify

> important factors that could cause results to differ materially—*but not all factors*.

Id. (emphasis added).

Indeed, the Report makes clear that a projection can still be protected by the safe harbor even if it fails to warn about the most important type of factor imaginable—the one that actually impeded realization of the projection in practice:

> Failure to include the particular factor that ultimately causes the forward-looking statement not to come true will *not* mean that the statement is not protected by the safe harbor.

Id. (emphasis added).

2. The Ninth Circuit's approach is incompatible with the straightforward analysis set forth above. Under the Ninth Circuit's new rule, cautionary language that unambiguously identifies various "important factors" that could prevent the defendant's projection from materializing will nonetheless be deemed insufficient if it fails to admit the false or misleading nature of a non-forward-looking statement accompanying the projection. App. 27a-28a, 31a-32a. In this very case, the Ninth Circuit applied that rule and rejected the safe harbor for forward-looking projections accompanied by allegedly false non-forward-looking statements. *Id.* at 31a-32a. It did so even though the cautionary language warning about those projections *was* deemed sufficient to trigger safe-harbor liability for *other* projections that were not accompanied by such non-forward-looking statements. *Id.* at 32a-33a.

a. The Ninth Circuit's rule flatly contradicts the PSLRA. The rule imposes a categorical requirement that does not appear in the statutory text. Nothing in the safe-harbor provision requires a cautionary statement to warn against the particular risk associated with the defendant's *non*-forward-looking statements—even if those latter statements are false or misleading. Such non-forward-looking statements might (or might not) be independently actionable under the securities laws, but they do not categorically negate safe-harbor protection for defendant's forward-looking statements.

b. The Ninth Circuit did not provide any clear textual, historical, or other justification for its outlier interpretation of the safe harbor. The court appeared to believe that a cautionary statement can never qualify as "meaningful" if it does not admit the falsity of any false or misleading non-forward-looking statements. App. 27a-28a. The court justified this conclusion by noting that the falsity of the non-forward-looking statements "is clearly an 'important factor' of which investors should be made aware." *Id.* at 31a.

In doing so, the Ninth Circuit appeared to assume that the safe harbor requires cautionary statements to warn against *all* "important factors." But the statutory text imposes no such requirement. As noted above, the PSLRA's legislative history makes clear that the cautionary language must identify some—but "*not all*"—such factors. Conf. Rep. No. 104-369, at 44. And "[f]ailure to include the particular factor that ultimately causes the forward-looking statement not to come true" for the statement to be protected by the safe harbor. *Id.*; *see generally supra* at 7, 13 & n.1, 27.

c. To the extent the Ninth Circuit was motivated by a desire to punish defendants for making false or misleading *non*-forward-looking statements, its chosen means of doing so—an overly-restrictive interpretation of the safe harbor for *forward*-looking statements—is misplaced. Congress protected investors from false or misleading *non*-forward-looking statements by making such statements independently actionable, so long as the other elements of securities fraud are also established. But such statements are not a basis for denying safe-harbor protection to a defendant's *forward*-looking projections. *See* 15 U.S.C. § 78u-5(c)(1)(A)(i).

Indeed, the PSLRA's structure makes clear that the first prong of the safe harbor does not turn on whether the defendant has been fully truthful or forthcoming with relevant information. As noted above, the safe harbor contains two prongs: (1) the "meaningful cautionary" language prong at issue here, *id.*; and (2) the "actual knowledge" prong, which protects any forward-looking projection that is made without "actual knowledge" of its false or misleading nature, *id.* § 78u-5(c)(1)(B)(i). The two prongs are disjunctive and provide *independent* sources of protection. As a result, the first prong will only matter in cases where the defendant is unable to take advantage of the second prong—*i.e.*, in cases where he *did* have actual knowledge that the projection is false. As a result, it makes little sense to deny protection under the first prong simply because the defendant may have made a false *non*-forward-looking statement.

d. The Ninth Circuit's rule also creates other anomalies. For example, that rule deprives

defendants of safe-harbor protection for forward-looking projections even where the defendant does not *know* that the non-forward looking statement is false or misleading when it is made. But there is no reason Congress would have wanted to penalize defendants—by exposing them to securities liability for *forward*-looking projections—simply because they made an innocent mistake with respect to a present or historical (i.e., *non*-forward-looking) fact.

Nor does it make sense to deprive defendants of safe-harbor protection when the allegedly-false non-forward-looking statement is entirely unrelated to the forward-looking projection or the reasons why that projection is not fulfilled. Yet that is the apparent consequence of the Ninth Circuit's rule, which holds that when a "non-forward-looking statement is materially false or misleading," cautionary language will be insufficient unless it includes "an outright admission of the false or misleading nature of the non-forward-looking statement." Op. 30, 34.

C. The Question Presented Is Important, And This Case Is An Ideal Vehicle For Resolving It

1. The proper interpretation of the PSLRA safe harbor is undeniably important. Congress enacted the safe harbor as part of a package of reforms intended to "encourage issuers to disseminate relevant information to the market without fear of open-ended liability" by providing "procedural protections to discourage frivolous litigation." Conf. Rep. No. 104-369, at 32; *see also* 141 Cong. Rec. H14040 (daily ed. Dec. 6, 1995) (statement of Rep. Tom Bliley).

The longstanding circuit split over how to interpret the PSLRA threatens those objectives. Indeed, the Second Circuit has already recognized the need for clarity and urged Congress to provide "further direction" on the "thorny" question of whether "an issuer [can] be protected by the meaningful cautionary language prong of the safe harbor even where his cautionary statement omitted a major risk that he knew about at the time he made the statement." *Slayton*, 604 F.3d at 772.

The Ninth Circuit's decision only makes things worse. Not only does it deepen the pre-existing conflict, but its outlier admission-of-falsity requirement creates a new—and textually indefensible—barrier to applying the safe harbor to protect a company's forward-looking projections.

Under the Ninth Circuit's decision, the path forward for securities plaintiffs—often repeat players represented by the same handful of attorneys—is clear. Every time a company fails to meet its previously-disclosed projections and suffers a stock-price drop, securities plaintiffs will argue that the safe harbor does not protect those projections because they were "accompanied" by false or misleading *non*-forward-looking statements, and defendants failed to make an "outright admission" to this effect. App. 27a-28a, 31a-32a.

This will not be hard to do. Companies' forward-looking projections are often accompanied by numerous and varied statements of present and historical fact. Plaintiffs' counsel will often be able to claim that one or more such facts are false or misleading, and thus that the defendants' projections are outside the scope of the safe harbor.

Of course, no real-world defendant will ever make the "outright admission" that its non-forward-looking statement is false. *Id.* And so the actual result of the panel's decision will be to nullify the safe harbor in practice. That will chill voluntary corporate disclosures and recreate the very problem that Congress wanted the PSLRA to solve. *See* 141 Cong. Rec. S8894 (daily ed. June 22, 1995) (statement of Sen. Christopher Dodd). Just like before the PSLRA, companies will "muzzl[e]" themselves and "release only the minimum information required by law so that they will not be held liable for any innocent, forward-looking statement that they may make." Conf. Rep. No. 104-369, at 42-43; 141 Cong. Rec. S8894 (statement of Sen. Dodd). As a result, investors will lose access to "much-needed" information helping them "mak[e] decisions about whether to invest or not." *See* 141 Cong. Rec. S8894-95 (statement of Sen. Dodd).

The Ninth Circuit's decision will therefore end up harming not only corporate defendants, but investors themselves. In doing so, the decision will neuter one of the PSLRA's core reforms of securities litigation in the United States. The undeniable importance of the question presented is yet another reason for this Court to grant review.

2. Finally, this case is an ideal vehicle for this Court to resolve the confusion over the proper interpretation of the PSLRA safe harbor. As explained above, the district court dismissed this case on the basis of the safe harbor, and the Ninth Circuit's rule resurrected respondents' fraud claim with respect to seven forward-looking statements. *See supra* at 11. A decision from this Court

overturning the Ninth Circuit's analysis will resolve those claims once and for all.

This case is an especially good vehicle because here there is no question that the Ninth Circuit's rule was outcome determinative in allowing the claims at issue to proceed. The Ninth Circuit expressly recognized that the cautionary language at issue *did* affirmatively identify "important factors that could cause actual results to differ materially from those in the forward-looking statement." 15 U.S.C. § 78u-5(c)(1)(A)(i); App. 33a (granting safe harbor protection to some of petitioners' forward-looking statements based on same cautionary language). The only reason the court held that the safe harbor did not also apply to the seven forward-looking projections at issue in this petition is that the cautionary language failed to admit that certain statements of present or historical fact made alongside those particular projections were false or misleading. App. 31a-33a.

This case therefore cleanly presents the validity of the Ninth Circuit's flawed interpretation of the PSLRA safe harbor. If this Court grants certiorari, it will have no difficulty confronting—and resolving—the question presented.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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January 26, 2018

APPENDIX

APPENDIX TABLE OF CONTENTS

Page

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

IN RE QUALITY SYSTEMS, INC. SECURITIES LITIGATION,

Debtor.

City of Miami Fire Fighters' and Police Officers' Retirement Trust; Arkansas Teacher Retirement System, Plaintiffs-Appellants,

v.

Quality Systems, Inc.; Steven T. Plochocki; Paul A. Holt; Sheldon Razin, Defendants-Appellees.

No. 15-55173

Filed July 28, 2017
865 F.3d 1130

OPINION

W. FLETCHER, Circuit Judge:

Lead Plaintiffs City of Miami Fire Fighters' and Police Officers' Retirement Trust and Arkansas Teacher Retirement System brought this would-be class action on behalf of all persons or entities who purchased or otherwise acquired the common stock of Quality Systems, Inc. ("QSI") between May 26, 2011, and July 25, 2012 ("the Class Period"). Plaintiffs allege that during the Class Period defendant QSI and several of its officers ("Defendants") made false or misleading statements about the current and past state of QSI's sales "pipeline," and used those statements to support public guidance to investors about QSI's projected growth and revenue. Individual defendants are Sheldon Razin, QSI's founder and Chairman of the

Board; Steven Plochocki, QSI's Chief Executive Officer ("CEO"); and Paul Holt, QSI's Chief Financial Officer ("CFO"). Plaintiffs allege that the individual defendants had real-time sales information showing a decline in sales due to market saturation beginning as early as April 2011, and that individual defendants knew that their public statements denying any decline were false or misleading.

The district court dismissed Plaintiffs' complaint with prejudice, finding that Defendants' non-forward-looking statements about the past and current state of QSI's sales pipeline were non-actionable puffery, and that their forward-looking statements about projected growth and revenue were protected by the safe harbor provision of the Private Securities Litigation Reform Act, 15 U.S.C. § 78u-5. We reverse and remand for further proceedings.

I. BACKGROUND

QSI is a California corporation that "develops and markets practice management and electronic health records ('EHR') software to medical and dental care providers." QSI was founded in 1974 by defendant Sheldon Razin, who was President and CEO until 2000. QSI benefited significantly from the passage of the 2009 American Recovery and Reinvestment Act, which provided $60 billion in incentives for healthcare providers to convert from paper to electronic records. During the Class Period, QSI's stock price largely depended on investors' belief that its revenues were growing rapidly. QSI's growth largely depended, in turn, on sales and maintenance of new software systems for healthcare providers, which "included software, hardware, third-party software, supplies and implementation and training

services components." New system sales were particularly important because they "included the promise of future, high-margin maintenance revenue." During QSI's Fiscal Year 2012 (April 2011 through March 2012), over 66 percent of QSI's total revenues came from sales and maintenance of such new software systems.

QSI's largest division, NextGen, develops and sells software systems for medical offices. During FY 2012, NextGen accounted for 75 percent of QSI's total revenue. During that same period, NextGen accounted for 83 percent of QSI's revenue from software systems sales and 84 percent of its revenue from software systems maintenance.

QSI's primary source of growth was sales of software systems to healthcare providers who were adopting electronic healthcare systems for the first time, referred to as "greenfield" sales. QSI's most profitable source of revenue was new practice management and electronic health records software. Sales and maintenance of this software had gross margins of 75.7 percent and 61.6 percent, respectively.

During the Class Period, QSI kept continuous track, in real time, of its sales "pipeline." The pipeline comprised four categories. Category 1 included deals that were expected, with 70 percent certainty, to close within three to four months. Category 2 included deals that were expected, with 70 percent certainty, to close within six to eight months. Categories 3 and 4 included deals that were not expected to close within eight months.

The gravamen of Plaintiffs' suit is that the individual defendants knew during the Class Period

that the market for healthcare software systems was becoming increasingly saturated, and that greenfield sales opportunities were decreasing. The complaint alleges that from late 2011 through mid-2012 (roughly, from the beginning of the second half of FY 2012 through the first quarter of FY 2013), Defendants misrepresented the state of QSI's current and past sales pipeline and used the misrepresentations to support projections of growth in revenue and earnings. The complaint alleges that QSI's projected growth "lacked any objective basis and . . [was] totally inconsistent with QSI's actual business performance." (Quotation marks omitted).

On July 26, 2012, QSI issued a press release finally admitting publicly that the company's business was in steep decline. As a result of this announcement, QSI stock prices dropped precipitously, causing Plaintiffs significant losses.

A. False or Misleading Statements

The following narrative is taken from Plaintiffs' amended complaint. We take as true the complaint's plausible and properly pleaded allegations, which we recount below. *Zucco Partners, LLC v. Digimarc Corp.*, 552 F.3d 981, 989 (9th Cir. 2009).

The complaint alleges that on a number of occasions Defendants, particularly CEO Plochocki, made false or misleading statements of current and past facts, as well as false or misleading statements of projected growth in revenue and earnings per share.

On June 9, 2011, at a Goldman Sachs Global Healthcare Conference, CFO Holt stated that the market for QSI's products in ambulatory health care facilities was "greenfield for the most part" and that

he thought "it's going to be that way for a while."

On October 27, 2011, QSI held an analyst conference call. When asked whether the electronic health records market was becoming saturated, Plochocki responded that "the greenfield opportunities are plentiful. [M]ore than half the large practice market, more than 75% of the midsize practice market is still fair game for new system sales." During that call, Plochocki predicted a "revenue range of growth of 21% to 24% for the year and an EPS [earnings per share] growth of 29% to 33% for the year."

On November 7, 2011, *Investor's Business Daily* published an interview with Plochocki entitled "Quality Systems Chief Says Boom Just Getting Started." Plochocki was quoted as saying, "There is nothing drying up and there is nothing slowing down."

On December 14, 2011, Plochocki participated in an Oppenheimer & Company, Inc., Healthcare Conference. At that conference, he stated, "So the bottom line is that our pipeline current and our pipeline future are very robust." In response to a comment that large and mid-size medical practices may be totally penetrated, Plochocki stated, "You wouldn't know that by our pipeline and you certainly would not know that by our categories three and four in our pipeline."

On January 9, 2012, at a J.P. Morgan Healthcare Conference, Plochocki stated that QSI had "given analysts prognostications for . . . earnings per share growth [in the] 29% to 34% range."

On January 26, 2012, in a conference call with analysts, Plochocki stated, "Our pipeline continues

to build to record levels." In that same conference call, after stating that he had access to current internal data, NextGen President Scott Decker stated, "[W]e haven't changed any of the model in our reporting pipeline, so it's very consistent, and there's nothing out of character in the pipeline that we're reporting today versus what we have seen there the past couple of years."

On February 7, 2012, Plochocki participated in a UBS Global Healthcare Services Conference. At that conference, he stated, "[W]e have $183 million worth of pipeline, the business we intend to close within the next six to eight months. That sales pipeline has grown every quarter since the announcement of the stimulus bill back in February of 2009 and we view it as continually growing[.]"

On May 7, 2012, Plochocki participated in a Deutsche Bank Healthcare Conference. At that conference, he stated that he had access to up-to-the-minute sales information that showed that "[t]he deals are elongated." "[T]he deals are taking a little bit longer to get done." On May 8, J.P Morgan characterized Plochocki's commentary as "downbeat."

On May 9, 2012, in response to J.P. Morgan's negative characterization, Decker appeared before investors at a Robert W. Baird & Co. Growth Stock Conference. In response to a question about Plochocki's statement two days earlier, Decker said, "[S]ome comments earlier this week at another conference were made . . . that [the sales cycle] may be lengthening. . . . [I]t is absolutely not a macro trend we are seeing. In fact, I went back through the data over the last few days and objectively looked at it. Sales cycle has not lengthened for us across the

board, and in fact, over the last year, you've seen a compression of it."

On May 10, 2012, QSI issued a press release that was filed that same day with the Securities and Exchange Commission on Form 8-K. In the press release, QSI announced that it expected to miss by material amounts its previously announced guidance for FY 2012. The press release attributed the declining sales to delays in closing deals. The press release provided optimistic guidance for FY 2013, stating that "earnings per share are expected to grow between 20 and 25 percent versus the 2012 fiscal year."

On May 14, 2012, Holt appeared at a JMP Securities Research Conference. He reiterated the guidance provided in the press release four days earlier. He stated, "[W]e tried to be very thoughtful about it and I think it's certainly—we're confident I think in the guidance that we gave."

On May 17, 2012, in a conference call, Plochocki told analysts that the poor FY 2012 results were a one-time event. He attributed the poor results to "delays in both the closing of several fourth-quarter opportunities, as well as recognition of revenue related to a large customer implementation." He emphasized the current state of QSI's sales pipeline: "Our pipeline is deep. Our categories one and two are strong. . . . [I]f the fundamentals have changed, that would be a different story. But our fundamentals haven't changed. Our pipeline keeps growing, categories one and two are very deep and vibrant for us this quarter. We haven't seen any fundamental change to any of the dynamics that have been feeding into our system for the last two to three years." Plochocki stated that "we remain

confident about the growth opportunities, as evidenced by our recent guidance in the 2013 fiscal year. We have stated that we expect . . . earnings per share to grow 20% to 25%." During that same conference call, CFO Holt also emphasized the current state of QSI's sales pipeline: "We are confident in our ability to deliver on this guidance. . . . Supporting our confidence in this guidance range are a number of factors, including our current sales pipeline[.]"

On June 26, 2012, QSI filed with the SEC an Open Letter to Shareholders, signed by Plochocki and Razin, as part of proxy materials. Plochocki's and Razin's letter stated, "We are also confident about our growth prospects. For fiscal 2013, we expect . . . earnings per share to grow by 20–25%." On June 30, 2012, four days later, the first quarter of QSI's FY 2013 ended. During that quarter, QSI's earnings per share had declined by 19 percent compared to the same quarter one year earlier. QSI did not release this information publicly at that time. On July 9, 10, 13, and 23, 2012, QSI submitted proxy materials to the SEC, signed by Plochocki and Razin, in which it repeated the statement that it expected earnings and earnings per share to grow by 20–25 percent.

On July 26, 2012, QSI issued a press release announcing that its earnings per share had declined by 19 percent as compared to the first quarter of FY 2011. Plochocki stated publicly that "we are not affirming our previous guidance nor providing revised guidance."

B. Scienter

The complaint alleges that the individual defendants were aware in real time of QSI's financial information, and knew that their statements about the current and past state of QSI's sales pipeline as well as their projections of future revenue and earnings were inconsistent with this information.

The complaint includes information about Defendants' knowledge provided by three high-level officers of QSI. First, Ahmed Hussein is a major shareholder of QSI. He was a member of the Board of Directors beginning in 1999. He resigned as a Director in May 2013. In his letter of resignation submitted to the Board, Hussein described what he characterized as securities laws violations by QSI, Plochocki, and Razin. He subsequently filed a verified complaint in California state court against QSI, Plochocki, and Razin. During his time as a Director, Hussein routinely interacted with Defendants Plochocki, Razin, and Holt. According to Hussein, QSI engaged in a "'continuous reforecasting process' based on real-time information concerning QSI revenues and income," "business performance [and] sales pipeline." According to Hussein, Defendants "were aware of real time data that contradicted their public statements."

Second, Confidential Witness 6 ("CW6") was a QSI Director from June 2008 through September 2009, and was QSI's Chief Operating Officer from September 2009 through May 2010. CW6 stated that Salesforce reports were available "at the push of a button." CW6 stated that he could see in early 2010 that the market was going to a recurring revenue model and that the big license sales that

had fueled QSI's growth were no longer going to work. CW6 warned Razin that changes needed to be made in QSI's business model to take this into account.

Third, Confidential Witness 7 ("CW7") was a QSI Director from 2004 to September 2009. CW7 stated that QSI's senior executives continually monitored QSI's revenues and earnings. According to CW7, QSI management knew on a monthly basis how QSI was doing.

The complaint also contains information about Defendants' knowledge provided by five lower-level QSI employees. First, Confidential Witness 1 ("CW1") was a product manager in Pennsylvania, between approximately November 2010 and September 2013, in QSI's NextGen division. CW1 noticed a slowdown in QSI's business beginning in April 2011, and noticed that "new sales opportunities had gone away." CW1 stated that QSI communicated to its employees that QSI was entering a "replacement market whereby QSI sought to replace competitors' systems." About 15 percent of CW1's compensation was based on NextGen sales figures. Between November 2010 and November 2011, QSI cut back and then stopped paying this portion of his compensation because QSI "was failing to hit its sales targets."

Second, Confidential Witness 2 ("CW2") was the Chief Information Officer ("CIO") of Practice Management Partners, a company acquired by QSI in late 2008. CW2 became CIO of QSI's Revenue Cycle Management division. CW2 stated that NextGen had experienced a slowdown in business by April 2011. CW2 recounted that Plochocki explained in internal conference calls sometime around March

2011 that the market for new systems "had become saturated, and that any sales QSI was making were largely to replace existing EHR [electronic health record] systems."

Third, Confidential Witness 3 ("CW3") was a NextGen Sales Executive from September 2011 to September 2012 for a sales region in California. According to CW3, everyone in his region was missing their sales targets, often by more than 50 percent. CW3 believed that other regions were also missing their sales targets by about 50 percent.

Fourth, Confidential Witness 4 ("CW4") was a NextGen Sales Executive from 2008 to December 2011, with responsibilities for sales in Virginia, Pennsylvania, and West Virginia. According to CW4, all executives at QSI had access to sales data that were compiled on the company's Salesforce software. QSI executives became increasingly involved with prospective deals in the pipeline as the end of a quarter approached.

Fifth, Confidential Witness 5 ("CW5"), based in Pennsylvania, was a Sales Analyst at NextGen from July 2010 to October 2012. CW5 compiled reports of booked and forecasted business, and arranged for the reports to be automatically delivered to the office of defendant Holt on a weekly or monthly basis. According to CW5, QSI officials monitored NextGen closely because it provided the vast majority of QSI's revenue.

C. Declines in Share Price

During the Class Period, QSI stock traded at a high of $50.04 on September 27, 2011.

On Friday, May 4, 2012, QSI stock traded at $36.99 per share. On Monday, May 7, Plochocki

disclosed that "deals are taking a little bit longer to get done." On Tuesday, May 8, analysts cut their forecasts for QSI earnings. At the end of the day on Tuesday, QSI stock had fallen to $30.99 per share, a decline of about 16 percent.

On July 26, 2012, QSI announced that its earnings per share during the first quarter of FY 2013 had fallen 19 percent, and Plochocki withdrew his earlier guidance. QSI's stock price immediately dropped from $23.63 per share to $15.95, a decline of about 33 percent.

D. Stock Sale by Plochocki

On February 24, 2012, Plochocki sold 88,500 shares of QSI stock at a price of $43.99 per share. The sale represented 87 percent of Plochocki's holdings of QSI stock. The proceeds of the sale were more than seven times Plochocki's FY 2012 salary.

II. Standard of Review

We review de novo a district court's dismissal for failure to state a claim. "We take all allegations of material fact as true and construe them in the light most favorable to the nonmoving party." *Parks Sch. of Bus., Inc. v. Symington*, 51 F.3d 1480, 1484 (9th Cir. 1995). A complaint alleging a violation of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), must meet both the heightened pleading requirements for fraud claims under Fed. R. Civ. P. 9(b), which requires that the complaint "state with particularity the circumstances constituting fraud," and the "exacting pleading requirements," *Tellabs, Inc. v. Makor Issues & Rights, Ltd.* (*Tellabs*), 551 U.S. 308, 313, 127 S.Ct. 2499, 168 L.Ed.2d 179 (2007), of the Private Securities Litigation Reform Act ("PSLRA"), which

require that the complaint "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind," 15 U.S.C. § 78u-4(b)(2)(A). In determining whether the complaint has satisfied these standards, we "consider the complaint in its entirety, as well as . . . documents incorporated into the complaint by reference, and matters of which a court may take judicial notice." *Tellabs*, 551 U.S. at 322–23, 127 S.Ct. 2499.

III. Discussion

The complaint alleges that Defendants' non-forward-looking statements about the current and past state of QSI's sales pipeline were materially false or misleading. The complaint also alleges that Defendants' forward-looking statements about projected revenue and earnings were materially false or misleading, were made without adequate cautionary statements, and were made with actual knowledge of their false or misleading nature. The complaint alleges that Defendants' statements—both non-forward-looking and forward-looking—violated Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and SEC Rule 10b-5, 17 C.F.R. § 240.10b-5.

As we have explained,

> Section 10(b) of the Securities Exchange Act of 1934 makes it unlawful '[t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe.' 15 U.S.C. § 78j(b). Pursuant to this section, the Securities and Exchange

> Commission promulgated Rule 10b-5, which makes it unlawful . . . '[t]o make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.' 17 C.F.R. § 240.10b-5(b).

In re Cutera Securities Litigation, 610 F.3d 1103, 1108 (9th Cir. 2010).

"To recover damages for violations of section 10(b) and Rule 10b-5, a plaintiff must prove (1) a material misrepresentation or omission by the defendant; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance upon the misrepresentation or omission; (5) economic loss; and (6) loss causation." *Halliburton Co. v. Erica P. John Fund, Inc.*, —— U.S. ——, 134 S.Ct. 2398, 2407, 189 L.Ed.2d 339 (2014) (internal quotation marks omitted). Only the first two elements are at issue here.

Even where a plaintiff has properly pleaded all six elements of a Section 10(b) violation, the allegedly false or misleading statement may still be shielded from liability by the "safe harbor" provision of the PSLRA. The PSLRA exempts from liability any forward-looking statement that is "identified as a forward-looking statement, and is accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement," or that the plaintiff fails to prove was made "with actual knowledge . . . that the statement was false or misleading." 15 U.S.C. § 78u-5(c)(1).

That is, a defendant will not be liable for a false or misleading statement if it is forward-looking and *either* is accompanied by cautionary language *or* is made without actual knowledge that it is false or misleading. *Cutera*, 610 F.3d at 1112–13.

The district court found that some of Defendants' allegedly false or misleading statements were not forward-looking, but found these statements to be "non-actionable puffery." The district court found that the remainder of Defendants' allegedly false or misleading statements were forward-looking, were accompanied by appropriate cautionary language, and were made without actual knowledge of their falsity. In reaching its conclusion about cautionary language, the district court took judicial notice of a number of PowerPoint slides containing cautionary language that Defendants contend were displayed during presentations at six health care conferences.

We disagree with the district court. First, some of Defendants' statements were "mixed statements," containing non-forward-looking statements as well as forward-looking statements of projected revenue and earnings. We hold a defendant may not transform non-forward-looking statements into forward-looking statements that are protected by the safe harbor provisions of the PSLRA by combining non-forward-looking statements about past or current facts with forward-looking statements about projected revenues and earnings. Second, we hold that many of Defendants' non-forward-looking statements were materially false or misleading. Third, we hold that some of Defendants' forward-looking statements were materially false or misleading, were not accompanied by appropriate

cautionary statements, and were made with actual knowledge of their false or misleading nature.

We therefore reverse and remand for further proceedings.

A. Non-Forward-Looking Statements

1. Mixed Statements

Plaintiffs contend that a number of Defendants' statements were "mixed," containing non-forward-looking statements about current and past facts as well as forward-looking statements about projected growth in revenue and earnings. They contend that the non-forward-looking parts of Defendants' statements reciting current and past facts are not protected by the safe harbor provision of the PSLRA.

We have not previously addressed in this circuit the status of mixed statements under the PSRLA. In *Police Retirement System of St. Louis v. Intuitive Surgical, Inc.*, 759 F.3d 1051 (9th Cir. 2014), plaintiffs contended that the non-forward-looking portions of mixed statements were not protected by the safe harbor provision. However, we did not need to "resolve whether the safe harbor covers non-forward-looking portions of forward-looking statements" in that case because "examined as a whole" the statements were forward-looking statements. *Id.* at 1059.

Several of our sister circuits have, however, addressed mixed statements. The First, Second, Third, Fifth, and Seventh Circuits have all concluded that where defendants make mixed statements containing non-forward-looking statements as well as forward-looking statements, the non-forward-looking statements are not protected by the safe harbor of the PSLRA. *See In re*

Stone & Webster, Inc., Securities Litigation, 414 F.3d 187, 211–13 (1st Cir. 2005); *In re Vivendi, S.A., Securities Litigation*, 838 F.3d 223, 246 (2d Cir. 2016); *Institutional Investors Group v. Avaya, Inc.*, 564 F.3d 242, 255 (3d Cir. 2009); *Spitzberg v. Houston American Energy Corp.*, 758 F.3d 676, 691–92 (5th Cir. 2014); *Makor Issues & Rights, Ltd. v. Tellabs Inc.* (*Tellabs II*), 513 F.3d 702, 705 (7th Cir. 2008). We agree with these circuits.

The PSLRA's safe harbor is designed to protect companies and their officials from suit when optimistic projections of growth in revenues and earnings are not borne out by events. But the safe harbor is not designed to protect companies and their officials when they knowingly make a materially false or misleading statement about current or past facts. Nor is the safe harbor designed to protect them when they make a materially false or misleading statement about current or past facts, and combine that statement with a forward-looking statement. As the First Circuit observed:

> The mere fact that a statement contains some reference to a projection of future events cannot sensibly bring the statement within the safe harbor if the allegation of falsehood relates to non-forward-looking aspects of the statement. The safe harbor, we believe, is intended to apply only to allegations of falsehood as to the forward-looking aspects of the statement.

Stone & Webster, 414 F.3d at 213.

Stone & Webster provides a useful example of an unprotected false or misleading non-forward-looking

statement embedded in a mixed statement. Company representatives had repeatedly stated, with slight variations in wording, that the company "has on hand and has access to sufficient sources of funds to meet its anticipated operating, dividend and capital expenditure needs." *Id.* at 211. The First Circuit held that the portion of the statement referring to accessible funds was not protected:

> [T]he alleged falsehood was in the fact that the statement claimed that the Company had access to ample cash at a time when the Company was suffering a dire cash shortage. The claim was not that the Company was understating its future cash needs. In our view the safe harbor of the PSLRA does not confer a *carte blanche* to lie in such representations of current fact.

Id. at 213.

Tellabs II provides another useful example. In that case, the company had stated that sales were "still going strong." *Tellabs II*, 513 F.3d at 705. The Seventh Circuit held that this statement was not protected by the safe harbor:

> [A] mixed present/future statement is not entitled to the safe harbor with respect to the part of the statement that refers to the present. When Tellabs told the world that sales of its 5500 system were "still going strong," it was saying both that the current sales were strong and that they would continue to be so, at least for a time, since the statement would be misleading if Tellabs knew that its sales were about to collapse. The element of prediction in saying that the

> sales are "still going strong" does not entitle Tellabs to a safe harbor with regard to the statement's representation concerning current sales.

Id.

2. Non-Forward-Looking Statements

On eight separate occasions, QSI officers knowingly made materially false or misleading non-forward-looking statements about the state of QSI's sales pipeline.

On June 9, 2011, at a Goldman Sachs Healthcare Conference, CFO Holt stated that the market for QSI's products in ambulatory health care facilities was "greenfield for the most part." On an October 27, 2011, conference call, in response to a question whether the electronic health records market was becoming saturated, CEO Plochocki stated that "more than half the large practice market, more than 75% of the midsize practice market is still fair game for new system sales." On November 7, 2011, Plochocki was quoted in *Investor's Business Daily* as saying, "There is nothing drying up and there is nothing slowing down." On December 14, 2011, at an Oppenheimer Healthcare Conference, in response to a comment that the large and mid-sized medical practices may be totally penetrated, Plochocki stated, "You wouldn't know that by our pipeline." On a January 26, 2012, conference call, Plochocki stated, "Our pipeline continues to build to record levels." During that conference call, NextGen President Decker stated, "[I]t's very consistent, and there's nothing out of character in the pipeline that we're reporting today versus what we have seen there the past couple of years." On February 7,

2012, at a UBS Healthcare Conference, Plochocki stated, "Th[e] pipeline has grown every quarter since the announcement of the stimulus bill back in February of 2009." On May 9, 2012, at a Robert W. Baird & Co. Growth Stock Conference, responding to concerns that the sales cycle might be lengthening, Decker stated, "I went back through the data . . . and objectively looked at it. Sales cycle has not lengthened for us across the board, and in fact, over the last year, you've seen a compression of it." On a May 17, 2012, conference call, Plochocki stated, "Our pipeline is deep. Our categories one and two are strong. . . . [O]ur fundamentals haven't changed. Our pipeline keeps growing, categories one and two are very deep and vibrant for us this quarter. We haven't seen any fundamental change to any of the dynamics that have been feeding into our system for the last two or three years."

During the Class Period, no one at QSI corrected the foregoing non-forward-looking statements about the state of QSI's sales pipeline.

a. Materiality

The district court concluded that any non-forward-looking statements were mere puffery, and therefore non-material. We disagree.

"When valuing corporations, . . . investors do not rely on vague statements of optimism like 'good,' 'well-regarded,' or other feel good monikers . . . . [P]rofessional investors, and most amateur investors as well, know how to devalue the optimism of corporate executives." *Cutera*, 610 F.3d at 1111 (internal quotation marks omitted). Examples of "mere corporate puffery" include statements such as "the opportunity for system placement at hospitals

'is still very, very large,'" and that a company "'will come out stronger' and 'is in a pretty good position' despite the economic crisis." *Intuitive Surgical*, 759 F.3d at 1060. But even "general statements of optimism, when taken in context, may form a basis for a securities fraud claim" when those statements address specific aspects of a company's operation that the speaker knows to be performing poorly. *Warshaw v. Xoma Corp.*, 74 F.3d 955, 959 (9th Cir. 1996). For example, reassuring investors that "everything [was] going fine" with FDA approval when the company knew FDA approval would never come was materially misleading. *Id.*; *see also In re Syntex Corp. Sec. Litig.*, 95 F.3d 922, 927–28 (9th Cir. 1996) (analyzing *Xoma*). Similarly, a statement that the company "anticipates a continuation of its accelerated expansion schedule" when the expansion had already failed was materially misleading. *Fecht v. Price Co.*, 70 F.3d 1078, 1081 (9th Cir. 1995).

The non-forward-looking statements, recounted above, about the current and past state of QSI's pipeline went beyond "feel good" optimistic statements. Plochocki and the others did not just describe the pipeline in subjective or emotive terms. Rather, they provided a concrete description of the past and present state of the pipeline. They repeatedly reassured investors during the class period that the number and type of prospective sales in the pipeline was unchanged, or even growing, compared to previous quarters. Plochocki did not just say that he believed plenty of opportunities for new system sales existed; he told investors what proportion of the large and mid-sized practice markets he believed were greenfield, and reassured them that the pipeline was full and growing. These

statements "affirmatively create[d] an impression of a state of affairs that differ[ed] in a material way from the one that actually exist[ed]." *Brody v. Transitional Hosps. Corp.*, 280 F.3d 997, 1006 (9th Cir. 2002).

b. False or Misleading

The non-forward-looking statements of Plochocki and other QSI officers were inconsistent with real-time financial information and were materially false or misleading. CW2, the Chief Information Officer of a division acquired by QSI in 2008, recounted that Plochocki explained in internal QSI conference calls as early as March 2011 that the market for new systems "had become saturated, and that any sales QSI was making were largely to replace existing EHR [electronic health record] systems." CW2 described a slowdown in NextGen's business beginning in April 2011. CW2 stated that Plochocki personally explained on conference calls as early as April 2011 that the market had become saturated after a "bubble" and that QSI would be forced to switch from greenfield sales to replacement systems. CW1, a product manager in NextGen, reported that the bonus portion of CW1's compensation, which was based on NextGen sales figures, had been eliminated by November 2011. Ahmed Hussein, a member of QSI's Board of Directors until May 2013, stated that "QSI's sales pipeline had been declining in the fourth quarter of fiscal 2012 [beginning January 1, 2012]." CW3, a NextGen Sales Executive from September 2011 to September 2012, stated that in CW3's region, sales executives were falling short "often by more than 50%" and that CW3 "believed other regions were similarly missing their targets by about 50%."

c. Scienter

Plaintiffs' complaint has adequately pleaded scienter. Under the PSLRA, Plaintiffs 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)(A). In this circuit, the "required state of mind" is a mental state that not only covers "'intent to deceive, manipulate, or defraud,' but also 'deliberate recklessness.'" *Schueneman v. Arena Pharamceuticals*, 840 F.3d 698, 705 (9th Cir. 2016) (citations omitted). To assess whether the complaint meets this standard, we "must ask: When the allegations are accepted as true and taken collectively, would a reasonable person deem the inference of scienter at least as strong as any opposing inference?" *Tellabs*, 551 U.S. at 326, 127 S.Ct. 2499. Where the plaintiff relies upon statements by confidential witnesses, the complaint must also pass two additional hurdles: "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*, 552 F.3d at 995 (citations omitted).

The complaint describes the confidential witnesses on whose statements Plaintiffs rely "with sufficient particularity to support the probability that a person in the position occupied by the source would possess the information alleged." *In re Daou Sys., Inc.*, 411 F.3d 1006, 1015 (9th Cir. 2005) (quoting *Novak v. Kasaks*, 216 F.3d 300, 314 (2d Cir.

2000)). As in *Daou*, the complaint includes each confidential witness's job description and responsibilities, and, in some instances, the witness's "exact title and to which [QSI] executive the witness reported." *Id.* at 1016. For example, CW6 was a QSI director who served as the Company's COO from September 2009 through May 2010. Although CW6 was not at QSI during the Class Period, as COO CW6 had personal knowledge of executive-level management's real-time access to Salesforce reports forecasting quarterly sales. CW2 was Chief Information Officer of one of QSI's divisions. In that capacity, CW2 was on a conference call during which Plochocki stated in March 2011 that the market for electronic health records software (produced and sold by the NextGen division) had become saturated. *See Zucco Partners*, 552 F.3d at 999 (confidential witness report of statement made directly to CW by defendant can be "indicative of scienter"). CW5, a NextGen Sales Analyst during the Class Period, personally compiled sales reports using Salesforce, NextGen's sales management software, and "arranged for sales reports to be automatically delivered to . . . the CFO [Holt]'s office, either on a weekly or a monthly basis."

"Taken collectively," statements by confidential witnesses establish that members of executive-level management, including individual defendants, had access to and used reports documenting in real time the decline in sales during the Class Period. *See Tellabs*, 551 U.S. at 323, 127 S.Ct. 2499. The complaint includes multiple statements from confidential witnesses with personal knowledge of QSI's declining sales during the Class Period. CW1's and CW4's statements establish the existence of

"funnel reports" and sales forecasts through the Salesforce software that were available to executives. CW5 had personal knowledge of the fact that sales reports were "automatically delivered to the management team." And CW7 "confirm[s] that QSI's senior executives" were in the habit of "continually monitor[ing] the Company's revenues and earnings." These "particularized allegations that defendants had 'actual access to the disputed information,' . . . raise a strong inference of scienter." *City of Dearborn Heights Act 345 Police & Fire Retirement Sys. v. Align Tech., Inc.*, 856 F.3d 605, 620 (9th Cir. 2017) (quoting *Reese v. Malone*, 747 F.3d 557, 575 (9th Cir. 2014)).

QSI's executives themselves told investors they had real-time access to, and knowledge of, sales information. Plochocki and Decker repeatedly described the state of QSI's sales pipeline to analysts and investors. For example, Plochocki told analysts on the May 26, 2011, conference call that QSI used information maintained in Salesforce databases to report its sales pipeline and make revenue forecasts for its SEC filings. His statement is comparable to statements in *Nursing Home Pension Fund, Local 144 v. Oracle Corp.*, 380 F.3d 1226, 1231 (9th Cir. 2004), where "top executives admit[ted] to having monitored [a] database" of sales data, and "Plaintiffs . . . [made] specific allegations regarding large portions of" that sales data that contradict those same executives' public statements. In its SEC filings, QSI stated that it "continually updated" its revenue estimates using Salesforce software.

A showing of scienter specific to Plochocki is reinforced by his sale of 87 percent of his QSI stock holdings on February 24, 2012, netting him proceeds

of more than seven times his FY 2012 salary. "'Unusual' or 'suspicious' stock sales by corporate insiders may constitute circumstantial evidence of scienter . . . ." *In re Silicon Graphics Inc. Securities Litigation*, 183 F.3d 970, 986 (9th Cir. 1999), *superseded by statute on other grounds* (citation omitted). "To evaluate suspiciousness of stock sales, we consider, *inter alia*, three factors: (1) the amount and percentage of shares sold; (2) timing of the sales; and (3) consistency with prior trading history." *Oracle Corp.*, 380 F.3d at 1232. Plochocki's massive and uncharacteristic sale in February, made near the apogee of QSI's stock price during the Class Period, and shortly before the stock went into a steep decline (bottoming out on July 26, 2012) is, to say the least, "suspicious." *Compare Silicon Graphics*, 183 F.3d at 987 (sale of 43.6 and 75.3 percent of respective holdings "somewhat suspicious"). Plochocki's sale came approximately a month after he had personally reaffirmed earnings per share guidance on January 26, 2012, stating that QSI's "pipeline continues to build to record levels." A mere two weeks before the sale, he had told audiences at the UBS Global Healthcare Services Conference that "we view [the pipeline] as continually growing." That Plochocki chose to sell the vast majority of his shares in QSI shortly after boasting to investors that QSI anticipated record levels of sales in the next six to eight months gives rise to a "strong inference" that Plochocki knew adverse information about the state of QSI's sales he was not sharing with the general public. *See* 15 U.S.C. § 78u-4(b)(2)(A); *No. 84 Employer-Teamster Joint Council Pension Trust Fund v. Am. W. Holding Corp.*, 320 F.3d 920, 939–40 (9th Cir. 2003) (sales of large percentages of various

executives' holdings, more than twenty months after the previous sale and near the stock's peak price gives rise to a "strong inference of scienter").

B. Forward-Looking Statements

During the Class Period, Defendants repeatedly made revenue and earnings projections. Such projections are, by definition, forward-looking statements. 15 U.S.C. § 78u-5(i)(1)(A), *see also Cutera*, 610 F.3d at 1111. The district court found that all of Defendants' forward-looking statements were accompanied by "sufficiently meaningful" cautionary language, and that plaintiffs "fail[ed] to 'state with particularity facts giving rise to a strong inference that defendant[s] acted with the required state of mind'" for forward-looking statements. (Quoting *In re Vantive Corp. Sec. Litig.*, 283 F.3d 1079, 1085 (9th Cir. 2002).) The district court therefore concluded that all of Defendants' forward-looking statements were protected by the PSLRA's safe harbor. We disagree.

Defendants' forward-looking statements may be divided into two groups: forward-looking statements made as part of mixed statements in which the non-forward-looking statements were materially false or misleading; and free-standing forward-looking statements. We take them in turn.

1. Forward-Looking Statements as Part of Mixed Statements

Where a forward-looking statement is accompanied by a non-forward-looking factual statement that supports the forward-looking statement, cautionary language must be understood in the light of the non-forward-looking statement. If the non-forward-looking statement is materially

false or misleading, it is likely that no cautionary language—short of an outright admission of the false or misleading nature of the non-forward-looking statement—would be "sufficiently meaningful" to qualify the statement for the safe harbor.

Defendants made a number of forward-looking statements as part of mixed statements. Some were made on conference calls, and some were made at conferences.

Defendants made mixed statements on three conference calls. On the October 27, 2011, conference call, at the same time Plochocki stated that "greenfield opportunities are plentiful," he predicted a "revenue range of growth of 21% to 24% for the year and an EPS growth of 29% to 33% for the year." Plochocki characterized these predictions as "quite conservative" given QSI's "large" pipeline of future business. On the January 26, 2012, conference call Plochocki provided an "update" on guidance for FY 2012, predicting that QSI would report "21% to 24% revenue growth for the year . . . that will be ending in two months" and that they had "upgraded" their earnings per share predictions to increases of 29% to 34% with "a pretty good shot at 35%." In support of these predictions, Plochocki characterized the pipeline as "growing," and Decker stated that "there's nothing out of character in the pipeline that we're reporting today versus what we have seen there in the past couple of years." On the May 17, 2012, conference call, Plochocki reaffirmed his prediction that QSI earnings per share would grow 20 percent to 25 percent, and Holt attributed QSI's confidence in the prediction to the state of the current sales pipeline. The predictions made during these conference calls were not borne out by events.

QSI announced earnings per share for FY 2012 that were 36 percent less than had been predicted. Rather than increasing, earnings per share in the first quarter of FY 2013 declined by 19 percent from the previous year.

The October 27, 2011, and May 17, 2012, conference calls were prefaced by the following identical cautionary language:

> Please note that the comments made on this call may include statements that are forward-looking within the meaning of securities laws, including, without limitation, statements related to anticipated industry trends, the Company's plans, products, perspectives, and strategies, preliminary and projected, and capital equity initiatives in the implementation of potential impacts of legal, regulatory, or accounting principles.

There is nothing before us to show what, if any, cautionary language accompanied the January 26, 2012, conference call.

Defendants also made mixed statements at four conferences. At the June 9, 2011, Goldman Sachs Global Healthcare Conference, Holt stated that the market for QSI's products in ambulatory health care facilities was "greenfield for the most part" and that he thought "it's going to be that way for a while." At the December 14, 2011, Oppenheimer Healthcare Conference, Plochocki stated that "our pipeline current and our pipeline future are very robust." In response to a comment that large and mid-size medical practices might be totally penetrated, Plochocki responded, "You wouldn't know that by our pipeline[.]" At the February 7, 2012, UBS Global

Healthcare Conference, Plochocki stated, "[W]e have $183 million worth of pipeline, the business we intend to close within the next six to eight months. That sales pipeline has grown every quarter since . . . February of 2009 and we view it as continually growing[.]" At the May 9, 2012, Robert W. Baird Growth Stock Conference, Decker stated, "I went back through the data . . . and objectively looked at it. Sales cycle has not lengthened for us across the board, and in fact, over the last year, you've seen a compression of it."

The parties dispute whether a PowerPoint slide that contained cautionary language was shown at these conferences, but there is no dispute about the language on the slide. The print on the slide was relatively small, necessitated by the 372-word length of the cautionary statement. *Inter alia*, the cautionary language provided:

> [T]hese forward-looking statements are subject to a number of risks and uncertainties, some of which are outlined below. As a result, actual results may vary substantially from those anticipated by the forward-looking statements. Among the important factors that could cause actual results to differ materially from those indicated by such forward-looking statements are: the volume and timing of systems sales and installations; length of sales cycles and the installation process; the possibility that products will not achieve or sustain market acceptance; [followed by fifteen more "important factors"].

That the non-forward-looking statement accompanying the forward-looking statement might

be false or misleading was not mentioned. For present purposes, we will assume that the slide containing the cautionary language was shown in a manner that gave conference attendees a reasonable opportunity to read and understand it.

Adequate cautionary language under the PSLRA must identify "important factors that could cause actual results to differ materially from those in the forward-looking statement." *See* 15 U.S.C. § 78u-5(c)(1)(A)(i). For cautionary language accompanying a forward-looking portion of a mixed statement to be adequate under the PSLRA, that language must accurately convey appropriate, meaningful information about not only the forward-looking statement but also the non-forward-looking statement. Where, as here, forward-looking statements are accompanied by non-forward-looking statements about current or past facts, that the non-forward-looking statements are, or may be, untrue is clearly an "important factor" of which investors should be made aware.

In both the conference calls and at the conferences, Defendants repeatedly told investors that they could rely on predictions of growth in revenue and earnings because the current state of QSI's sales pipeline was consistent with, or better than, the state of the pipeline in previous quarters. The cautionary language used by Defendants failed to correct these materially false or misleading non-forward-looking statements. We need not delve deeply into what might, in other cases, constitute adequate cautionary language for mixed statements, for the answer is clear in the case now before us. Because Defendants made materially false or misleading non-forward-looking statements about

the state of QSI's sales pipeline, virtually no cautionary language short of an outright admission that the non-forward-looking statements were materially false or misleading would have been adequate. No such cautionary language was provided.

2. Free-Standing Forward-Looking Statements

It appears from the materials now before us that Defendants made only two free-standing forward-looking statements, unaccompanied by non-forward-looking statements. Both were at conferences. First, at the January 9, 2012, J.P. Morgan Healthcare Conference, Plochocki predicted "earnings per share in the 29% to 34% range." The complaint does not allege that any non-forward-looking statement accompanied Plochocki's statement. Second, at the May 14, 2012, JMP Securities Research Conference, Holt reaffirmed the guidance given in a press release four days earlier predicting FY 2013 growth in earnings per share of between 20 percent and 25 percent. The complaint does not allege that any non-forward-looking statement accompanied Holt's statement.

The district court took judicial notice of a PowerPoint slide, containing cautionary language described above, that Defendants contend were shown at the conferences. Defendants submitted copies of the slide to the court, accompanied by a statement by one of Defendants' attorneys that he had "personal knowledge" of the fact that the printouts were "true and correct cop[ies] of the written presentation materials" at the conferences. The statement does not say that the slide was actually shown at the conferences. A different

defense attorney represented to the district court during oral argument in support of Defendants' motion to dismiss that it was his "understanding" that these materials "were . . . up on a screen projected while the speaker was speaking" and "also posted to the website." The district court concluded, "At each conference, an entire written slide dedicated to the safe harbor provision was shown. Thus, the oral statements were accompanied by cautionary language, by way of the printed slide."

Plaintiffs argue vigorously that the district court erred in taking judicial notice of the fact that the PowerPoint slides containing cautionary language were shown in a meaningful way at the conferences as part of Plochocki's and Holt's presentations. We need not decide whether the district court erred. As described above, there were numerous other statements by Defendants—both non-forward-looking statements and forward-looking statements embedded in mixed statements—upon which to premise Defendants' liability if it turns out that the allegations in the complaint are true. We therefore assume without deciding that the PowerPoint slide containing the cautionary language accompanied Plochocki's and Holt's forward-looking statements on January 9 and May 14, 2012. In the absence of any materially false or misleading non-forward-looking statements, the cautionary language was sufficiently meaningful to qualify for safe harbor.

3. Actual Knowledge

Even if a forward-looking statement is not accompanied by adequate cautionary language, it is protected by PSLRA's safe harbor if the speaker did not have "actual knowledge" that the statement was

false or misleading. *See Cutera*, 610 F.3d at 1112–13 ("actual knowledge" and "cautionary language" safe harbor prongs are disjunctive). As described above, Defendants had actual knowledge that their non-forward-looking statements were false and misleading. Their forward-looking statements were premised on those non-forward-looking statements. It necessarily follows that they also had actual knowledge that their forward-looking statements were false or misleading.

IV. Control Person Liability

The complaint alleges that individual defendants Razin, Plochocki, and Holt are liable under Section 20(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78t, which assigns joint and several liability for any person who "controls any person liable" under Section 10(b). The district court dismissed the complaint in its entirety based on its conclusion that Plaintiffs had failed to state a claim for relief under Section 10(b). The court thus did not address individual defendants' liability under Section 20(a), which is derivative of liability under Section 10(b). We leave it to the district court to address in the first instance whether Razin, Plochocki, and Holt were control persons within the meaning of Section 20(a).

Conclusion

We hold that non-forward-looking portions of mixed statements are not eligible for the safe harbor provisions of the PSLRA, 15 U.S.C. § 78u-5. In the case before us, Defendants made a number of mixed statements that included projections of growth in revenue and earnings based on the state of QSI's sales pipeline. For the reasons given above, both the non-forward-looking and the forward-looking

portions of these statements were materially false or misleading. We reverse and remand for further proceedings consistent with this opinion.

REVERSED AND REMANDED.

UNITED STATES DISTRICT COURT,
C.D. CALIFORNIA,
SOUTHERN DIVISION.

IN RE QUALITY SYSTEMS, INC. SECURITIES LITIGATION, Debtor.

Case No. SACV 13–01818–CJC(JPRx).

Signed Oct. 20, 2014
Order Denying Reconsideration
Jan. 5, 2015

60 F. Supp. 3d 1095

ORDER GRANTING DEFENDANTS' MOTION TO DISMISS WITH PREJUDICE

CORMAC J. CARNEY, District Judge.

I. INTRODUCTION

This is a shareholder securities class action brought against Quality Systems, Inc. ("QSI") and its high-ranking directors and officers, Sheldon Razin, Steven Plochocki, and Paul Holt (collectively, "Defendants"). The claims are asserted on behalf of all persons or entities who, during May 26, 2011 through July 25, 2012 (the "Class Period"), purchased or otherwise acquired the common stock of QSI (collectively, "Plaintiffs"). The Amended Complaint alleges violations of sections 10(b) and 20(a) of the Securities Exchange Act of 1934 ("SEA"), 15 U.S.C. §§ 78j(b), 78t(a), and Rule 10b–5, 17 C.F.R. § 240.10b–5, in connection with Defendants' purportedly false and misleading statements regarding revenue forecasts, sales pipeline figures, and greenfield sales projections. (Dkt. No. 26

Amended Compl. ["AC"].) Before the Court is Defendants' motion to dismiss the Amended Complaint. (Dkt. No. 29 ["Defs.' Mot."].) Defendants argue that the Amended Complaint fails to meet the heightened pleading requirements of Federal Rule of Civil Procedure 9(b) and the Private Securities Litigation Reform Act of 1995 ("PSLRA"), 15 U.S.C. § 78u–4(b). For the following reasons, Defendants' motion is GRANTED WITH PREJUDICE.

I. BACKGROUND

QSI is a publicly-traded company that develops and markets practice management and electronic health records ("EHR") software to medical and dental care providers, including scheduling and billing related software. (AC ¶ 23.) Defendant Plochocki served as the Chief Executive Officer and a member of the Board during the Class Period; he has also been serving as President since January 25, 2012. (AC ¶ 24.) Defendant Holt served as the Chief Financial Officer during the Class Period. (AC ¶ 25.) Defendant Razin is the founder of QSI and served as the Chairman of the Board during the Class Period. (AC ¶ 26.) The Amended Complaint alleges that, as high-ranking officers and directors, Defendants Plochocki, Holt, and Razin (the "Individual Defendants") had direct involvement and control in the day-to-day operations of QSI and had access to "real-time" data about QSI's business and sales. (AC ¶ 2, 27.)

In 2009, Congress passed the American Recovery and Reinvestment Act ("ARRA"), which provided $60 billion in government funds to incentivize healthcare providers to transition from paper to electronically

based practices.[1] (AC ¶ 30.) QSI referred to the ARRA as the "number one market driver" in the healthcare information technology industry. (AC ¶ 31.) QSI's business is heavily dependent on its ability to book new systems sales, which in turn expands its installed base to earn maintenance revenue. (AC ¶ 34.) In light of the ARRA, QSI particularly relied on "greenfield" sales—sales made to customers who previously had no EHR system in place at all. (AC ¶ 38.) The Amended Complaint alleges that, in connection with its favorable projections, QSI frequently cited the high potential for sales in the greenfield market. (AC ¶¶ 38–39.) In addition to greenfield sales, QSI tracked its sales pipeline, which represents the value of all deals that QSI believes it will close within four to eight months.[2] (AC ¶ 41.)

Plaintiffs contend that, during the Class Period, Defendants misrepresented the strength of QSI's sales figures, sales prospects, greenfield sales, and pipeline figures, and issued highly favorable earnings per share (EPS) guidance for fiscal years

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[1] For the first five years of the ARRA, healthcare providers adopting certified electronic management and health record systems are eligible for government subsidies; beginning in 2015, healthcare providers who have not adopted certified systems will receive a reduction in government reimbursement. (AC ¶ 30.)

[2] The sales pipeline is divided into four categories. Deals in Category 1 are expected to close in three to four months with 70% certainty; Category 2, six to eight months with 70% certainty; Categories 3 and 4 contain deals that are not expected to close within eight months and are not included in the publicly reported pipeline number. (AC ¶ 41.)

2012 ("FY2012") and 2013 ("FY2013").[3] (AC ¶ 44.) Plaintiffs point to approximately thirty allegedly fraudulent statements made during the Class Period at various conferences and earnings calls and in written publications, including a shareholder letter. For example, at the Goldman Sachs Global Healthcare Conference on June 9, 2011, Defendant Holt, in response to a question about the greenfield market, stated, "it's greenfield for the most part . . . and I think it's going to be that way for a while." (AC ¶ 60.) In regards to QSI's pipeline, Scott Decker, President of QSI's NextGen division, stated at the October 27, 2011 earnings call, "[I]f you look out 12—12 months and further, it's unprecedented with the amount of demand we see coming for our clients for rollout levels to the extent they never talked to us about the past, so it is flat but I wouldn't read much into that." (AC ¶ 66.) The Amended Complaint contends that these and similar statements were false and misleading because QSI had already begun to experience a slowdown in its greenfield sales starting in April 2011 and a decline in the sales pipeline beginning in the fourth quarter of FY2012.[4] (AC ¶ 63, 72, 81, 104.)

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[3] QSI's fiscal year runs from April 1 through March 31. (AC ¶ 7 n. 3.)

[4] The Amended Complaint relies in large part on pleadings in a separate lawsuit by a former QSI director and second largest shareholder, Ahmed Hussein. According to Mr. Hussein, Defendants' revenue and earnings projections during the Class Period "lacked any objective basis" as the Individual Defendants knew that "QSI's financial performance had begun slowing down in late 2011." (AC ¶ 46.) This decline in sales is purportedly corroborated by seven confidential witnesses ("CW") who were former QSI employees. (AC ¶ 48.)

Plaintiffs further allege that QSI issued fraudulent and misleading EPS guidance for FY2012 and FY2013. In late October 2011, Defendant Plochocki announced a projected revenue growth range of 21% to 24% and an EPS growth of 29% to 33% for FY2012. (AC ¶ 64.) These EPS projections were reaffirmed in January 2012. (AC ¶¶ 73, 75.) On May 17, 2012, QSI announced its results for FY2012—QSI had met its revenue growth projections at 22%, but "due to delays in closing several fourth-quarter opportunities, as well as recognition of revenue related to a large customer implementation," EPS growth was only 21%. (AC ¶ 93; Dkt. No. 29–1 Declaration of Katherine A. Rykken ISO Defendants' Motion to Dismiss ["Rykken Decl. 1"], Exh. 13.)[5] Looking ahead, QSI projected a 20% to 24% revenue growth and a 20% to 25% EPS growth for FY2013. (AC ¶ 93.) The

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[5] Defendants request that the Court take judicial notice of 43 documents submitted as exhibits in support of the motion to dismiss. (Dkt. Nos. 29–2, 35–1.) These documents include various Securities Exchange Commission ("SEC") filings by QSI, transcripts of QSI's earnings calls and statements made during healthcare conferences, proxy materials, and printouts of QSI's presentation slides. "Although generally the scope of review on a motion to dismiss for failure to state a claim is limited to the Complaint, a court may consider evidence on which the complaint necessarily relies if: (1) the complaint refers to the document; (2) the document is central to the plaintiffs' claim; and (3) no party questions the authenticity of the copy attached to the 12(b)(6) motion." *Daniels–Hall v. Nat'l Educ. Ass'n,* 629 F.3d 992, 998 (9th Cir.2010) (internal quotation marks and citations omitted). Here, the vast majority of the documents are referenced in the Amended Complaint and Plaintiffs neither oppose the requests for judicial notice nor question the authenticity of the documents. Thus, the Court takes judicial notice of these 43 exhibits.

FY2013 projections were re-stated in late June 2012 and early July 2012 in connection with proxy materials for a pending proxy contest. (AC ¶¶ 107–108.) On July 26, 2012, QSI issued a press release declining to affirm the FY2013 guidance, given that record revenues for the first quarter had come in at just 18% and there was a decline in EPS and net income from the previous year's quarter. (AC ¶ 110; Rykken Decl. 1, Exh. 24 ["July 26 Form 8–K"] at 621.) In the same press release, Defendant Plochocki explained that "overall results were impacted by lower than expected revenue from large, higher margin software system sales." (July 26 Form 8–K at 621.)

Plaintiffs generally allege that QSI's statements were fraudulent because they were issued contemporaneously while QSI's new bookings and sales pipeline were declining. (AC ¶ 46, 48–56.) The Amended Complaint alleges that each of the fraudulent statements was material to investors, pointing to the positive reviews and recommendations to purchase QSI stock by analysts that followed each of QSI's public statements. (AC ¶¶ 62, 78, 99, 102.) The Amended Complaint also alleges that the Individual Defendants possessed the requisite scienter because they were aware of QSI's flagging financial performance as of late 2011. In support of this allegation, Plaintiffs point to the Individual Defendants' involvement with the core operations of QSI and their access to real-time data about the sales cycle. (AC ¶¶ 14, 118–119, 145.) The Amended Complaint further points out Defendant Plochocki's sale of 87% of his QSI stock during the Class Period and letters from the SEC seeking

clarification of QSI's EPS projections as indicators of scienter. (AC ¶¶ 134–144.)

III. LEGAL STANDARD

A motion to dismiss under Federal Rule of Civil Procedure 12(b)(6) tests the legal sufficiency of the claims asserted in the complaint. The issue on a motion to dismiss for failure to state a claim is not whether the claimant will ultimately prevail, but whether the claimant is entitled to offer evidence to support the claims asserted. *Gilligan v. Jamco Dev. Corp.,* 108 F.3d 246, 249 (9th Cir.1997). Rule 12(b)(6) is read in conjunction with Rule 8(a), which requires only a short and plain statement of the claim showing that the pleader is entitled to relief. Fed.R.Civ.P. 8(a)(2). When evaluating a Rule 12(b)(6) motion, the district court must accept all material allegations in the complaint as true and construe them in the light most favorable to the non-moving party. *Moyo v. Gomez,* 32 F.3d 1382, 1384 (9th Cir.1994). However, "the tenet that a court must accept as true all of the allegations contained in a complaint is inapplicable to legal conclusions." *Ashcroft v. Iqbal,* 556 U.S. 662, 663, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009); *see also Bell Atl. Corp. v. Twombly,* 550 U.S. 544, 555, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007) (stating that while a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, courts "are not bound to accept as true a legal conclusion couched as a factual allegation" (citations and quotes omitted)). The district court should grant the plaintiff leave to amend if the complaint can possibly be cured by additional factual allegations. *Doe v. United States,* 58 F.3d 494, 497 (9th Cir.1995).

The PSLRA imposes a heightened pleading standard in private securities litigation and requires that the complaint "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, the complaint shall state with particularity all facts on which that belief is formed." 15 U.S.C. § 78u–4(b)(1). Plaintiffs must additionally state with particularity "facts evidencing scienter, *i.e.,* the defendant's intention to deceive, manipulate, or defraud." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.,* 551 U.S. 308, 313, 127 S.Ct. 2499, 168 L.Ed.2d 179 (2007) (internal quotation marks and citation omitted); *see also* 15 U.S.C. § 78u–4(b)(2).

IV. ANALYSIS

In this action, Plaintiffs assert two causes of action—one against all Defendants, and one against Defendant Plochocki individually—for violations under § 10(b) of the SEA and Rule 10b–5.[6] The basic elements of a claim under § 10(b) and Rule 10b–5 are: (1) a material misrepresentation or omission of fact; (2) scienter; (3) a connection with the purchase

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[6] Plaintiffs also plead a third cause of action against all Defendants for violations of § 20(a) of the SEA. Claims under § 20(a), which provides that certain "controlling" individuals will be liable for a primary violation of federal securities law, are derivative claims and are thus contingent upon a finding of a § 10(b) violation. *Zucco Partners, LLC v. Digimarc Corp.,* 552 F.3d 981, 990 (9th Cir.2009) ("Section 20(a) claims may be dismissed summarily, however, if a plaintiff fails to adequately plead a primary violation of section 10(b)."). Because the Amended Complaint fails to state a primary violation of section 10(b), *see infra,* the Court does not conduct a § 20(a) analysis.

or sale of a security; (4) transaction and loss causation; and (5) economic loss. *In re Daou Sys., Inc. Sec. Litig.,* 411 F.3d 1006, 1014 (9th Cir.2005).

The PSLRA, however, exempts from liability certain "forward-looking statements" through a safe harbor provision. *See* 15 U.S.C. § 78u–5(c). A forward-looking statement includes, *inter alia,* statements containing a projection of revenues, income, earnings per share, and other financial items; statements of plans and objectives of management for future operations; and statements of future economic performance. *Id.* § 78u–5(i)(1)(A)-(C). Additionally, "any statement of the assumptions underlying or relating to any [such] statement" is classified as forward-looking. *Id.* § 78u–5(i)(1)(D). Once it is determined that the statement is indeed forward-looking, the safe harbor provides two alternative paths to immunity where: (1) the statement was accompanied by meaningful cautionary language, *id.* § 78u–5(c)(1)(A); or (2) plaintiff fails to provide the projections were made with actual knowledge that they were false or misleading, *id.* § 78u–5(c)(1)(B). *See In re Cutera Sec. Litig.,* 610 F.3d 1103, 1112–13 (9th Cir.2010) (holding that the safe harbor provides two independent grounds for protection).

A. Forward-Looking Statements

The majority of Defendants' allegedly fraudulent statements are forward-looking. Statements containing a projection of revenues and earnings per share fall squarely within the PSLRA's definition of forward-looking statements. 15 U.S.C. § 78u–5(i)(1)(A). As such, any projections by Defendants about revenue growth or EPS growth for FY2012

and FY2013 are properly classified as forward-looking and may qualify for the safe harbor. For example, statements such as "earnings per share are expected to grow between 20 and 25 percent versus the 2012 fiscal year" and "[w]e're earmarked for a very strong year" are forecasts of future performance. (AC ¶¶ 73, 86.) Similarly, statements pertaining to the greenfield market and opportunities for growth in this area, as well as anticipatory statements about the future strength of pipeline sales, were also forward-looking expressions. For instance, statements about growing greenfield opportunities and the robust pipeline future amount to projections of future economic performance. (*See* AC ¶ 70; 15 U.S.C. § 78u–5(i)(1)(A).)

The Court recognizes that a few statements, particularly in reference to QSI's "current" pipeline may be classified as non-forward-looking, as they concern historical or current facts. *See In re Splash Tech. Holdings, Inc. Sec. Litig.,* 160 F.Supp.2d 1059, 1068 (N.D.Cal.2001). In regards to such statements, however, either Plaintiffs have not alleged that the historical results were incorrect, or the present statements amount to non-actionable puffery.[7]

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[7] For example, during the January 26, 2012 earnings call, Defendant Plochocki stated that QSI had $183 million worth of pipeline. (AC ¶ 77.) That same figure was repeated on February 7, 2012 at a UBS Global Healthcare Services Conference. (AC ¶ 79.) Plaintiffs do not allege that this figure was false or misleading. Other statements describing the pipeline as "strong" or "robust" are not actionable because "professional investors, and most amateur investors as well, know how to devalue the optimism of corporate executives." *Police Ret. Sys. of St. Louis v. Intuitive Surgical, Inc.,* 759 F.3d

Barring these few exceptions, the alleged statements are forward-looking and, as discussed below, qualify for the safe harbor under either ground.

B. Accompanying Meaningful Cautionary Language

The first ground of the safe harbor immunizes forward-looking statements that are accompanied by meaningful cautionary language that identifies "important factors that could cause actual results to differ materially." 15 U.S.C. § 78u–5(c)(1)(A)(i); *Employers Teamsters Local Nos. 175 and 505 Pension Trust Fund v. Clorox Co.,* 353 F.3d 1125, 1133 (9th Cir.2004). Although the PSLRA does not require a listing of all variables that may change predicted results, "boilerplate language warning that investments are risky or general language not pointing to specific risks" is insufficient. *In re Copper Mountain Sec. Litig.,* 311 F.Supp.2d 857, 882 (N.D.Cal.2004).

As a preliminary matter, Plaintiffs contend that several of the alleged oral misstatements by Defendants were not accompanied by *any* cautionary language. The challenged statements, however, were made by Individual Defendants during healthcare conferences and Defendants have provided the contemporaneous presentation slides that were used during these conferences. (*See* Dkt. No. 35–2 Declaration of Rykken Declaration ISO Defendants' Second for RJN ["Rykken Decl. 2"], Exhs. 39–43.) At each conference, an entire written slide dedicated to the safe harbor provision was

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1051, 1060 (9th Cir.2014) (internal citation and quotation marks omitted).

shown. (*Id.*) Thus, the oral statements were accompanied by cautionary language, by way of the printed slide. *See In re Broadcom Corp. Sec. Litig.,* No. SACV01275GLTMLGX, 2004 WL 3390052 (C.D.Cal. Nov. 23, 2004) (applying safe harbor to oral statements referencing SEC filings with cautionary language). Plaintiffs do not contend that the other forward-looking statements, such as those made during earnings calls or in SEC-filed press releases, lacked accompanying cautionary language.

The cautionary statements that accompanied each of Defendants' forward-looking statements were sufficiently meaningful. The included language warns that the statement contains forward-looking statements, upon which "undue reliance should not be placed," given the number of risks and uncertainties involved. (*See, e.g.,* Rykken Decl. 2, Exh. 3 at 41.) Moreover, each cautionary statement identifies specific factors that may affect the forward-looking statements including, *inter alia,* volume and timing of systems sales and installations, length of sales cycles and installation process, impact of incentive payments under the ARRA on sales, the development by competitors of new or superior technologies, and political or regulatory influences in the healthcare industry. (*See, e.g.,* Rykken Decl. 1, Exhs. 3, 5, 7, 9, 11–12, 14; Rykken Decl. 2, Exhs. 39–43.) These factors are specific to QSI's EHR business and do not constitute generic warnings that any general business or corporation could import. *See In re Cutera,* 610 F.3d at 1112 (cautionary language identifying statements as forward-looking and risk factors "like Cutera's 'ability to continue increasing sales performance worldwide' " was adequate). Contrary to Plaintiffs'

assertions, such warnings are not boilerplate; consequently, Defendants' forward-looking statements are protected by the safe harbor provision.

C. Actual Knowledge of Falsity

Additionally, the forward-looking statements fall under the second prong of the safe harbor because Plaintiffs fail to "state with particularity facts giving rise to a strong inference that defendant acted with the required state of mind." *See In re Vantive Corp. Sec. Litig.,* 283 F.3d 1079, 1085 (9th Cir.2002) (quoting 15 U.S.C. § 78u–4(b)(2)). In the case of forward-looking statements, the required state of mind is "*actual knowledge* that [the statements] were materially false or misleading." *In re Cutera,* 610 F.3d at 1112 (emphasis in original). No accompanying cautionary statement is required for this prong of the safe harbor. *See id.* at 1113.

Plaintiffs allege that Defendants had access to real-time data on QSI's revenues and earnings and thus knew that QSI's sales and sales prospects were declining as early as April 2011. (AC ¶ 119.) The Amended Complaint further cites statements by CWs that Individual Defendants regularly monitored such data. (*See, e.g.,* AC ¶ 112.) Plaintiffs vaguely describe the real-time data as "incorporat[ing] inputs from all operating entities," and make general assertions that this data revealed "daily sales activities, sales forecasts, and the projected value of accounts." (AC ¶ 7.) This falls short of the high pleading requirements for scienter, which requires a much more detailed and specific account of the contents of such data. *See, e.g., In re Silicon Graphics Inc. Sec. Litig.,* 183 F.3d 970, 985 (9th Cir.1999) (insufficient pleading of scienter

where complaint cites officers' knowledge of reports without describing details of reports' contents, such as "specifics regarding ASIC chip shortages, volume shortages, negative financial projections, and so on"). The Amended Complaint also alleges that Individual Defendants were aware of the slowdown in business because of their involvement in QSI's daily operations and access to all material information regarding QSI's core operations. (AC ¶ 145.) Such allegations are wholly conclusory and are insufficient to support an inference of scienter. *See, e.g., In re Lockheed Martin Corp. Sec. Litig.,* 272 F.Supp.2d 944, 956 (C.D.Cal.2003) (insufficient fraud allegations based on officers' role in the company, including "review[ing] the financial condition of the Company" and "receiv[ing] regular updates regarding the [company's] status").

Finally, Plaintiffs cite two additional facts to further bolster their scienter allegations. First, Plaintiffs point to the fact that Defendant Plochocki sold 87% of his QSI stock during the Class Period. Second, Plaintiffs cite two letters from the SEC commenting on QSI's projections in proxy materials. Although "suspicious" insider stock sales may be circumstantial evidence of scienter, such sale must be "dramatically out of line with prior trading practices at times calculated to maximize the personal benefit from undisclosed inside information." *Ronconi v. Larkin,* 253 F.3d 423, 435 (9th Cir.2001). Here, Defendant Plochocki's sale fails to show scienter because it was not a dramatic deviation from his prior trading practices. In fact, the Amended Complaint admits that Defendant Plochocki had a prior history of making a massive stock sale in September 2008. (AC ¶ 135.) Likewise,

the SEC letters also fail to show Defendants' actual knowledge of falsity, as they only requested QSI to revise its proxy materials to discuss QSI's FY2013 projections and the underlying assumptions in the same place. (Rykken Decl. 1, Exhs. 17–19.) These allegations do not give rise to a strong inference of actual knowledge of falsity.

V. CONCLUSION

For the foregoing reasons, Defendants' motion to dismiss is GRANTED. Due to the applicability of the safe harbor provision, the Amended Complaint suffers from fatal defects and is DISMISSED WITH PREJUDICE.

ORDER DENYING PLAINTIFFS' MOTION FOR RECONSIDERATION

I. INTRODUCTION & BACKGROUND

Lead Plaintiffs Arkansas Teacher Retirement System and the City of Miami Fire Fighters' and Police Officers' Retirement Trust brought this securities class action on behalf of all persons or entities who, during May 26, 2011 through July 25, 2012 (the "Class Period"), purchased or otherwise acquired the common stock of Defendant Quality Systems, Inc. ("QSI"), (collectively, "Plaintiffs"). In the Amended Complaint, Plaintiffs allege that QSI and its high-ranking directors and officers, Sheldon Razin, Steven Plochocki, and Paul Holt (collectively, "Defendants") made false and misleading statements regarding revenue forecasts, sales pipeline figures, and greenfield sales projections. (Dkt. No. 26, Amended Compl. ["AC"].)

On June 20, 2014, Defendants brought a motion to dismiss, arguing, *inter alia,* that the alleged

statements were forward-looking and protected by the safe harbor provision of the Private Securities Litigation Reform Act of 1995 ("PSLRA"), 15 U.S.C. § 78u–4(b). (Dkt. No. 29 ["Defs.' MTD"].) Specifically, Defendants argued that Plaintiffs had failed to show that Defendants made the alleged forward-looking statements with knowledge of their falsity and that the statements were accompanied by meaningful cautionary language. (*Id.*) In support of the latter proposition, Defendants requested judicial notice of numerous exhibits pursuant to the incorporation by reference doctrine and Federal Rule of Evidence 201. (Dkt. Nos. 29–2, 35–1.)

The Court granted the motion to dismiss with prejudice on October 20, 2014 based on the finding that the vast majority of the alleged statements were forward-looking and accompanied by meaningful cautionary language ("Order"). (Dkt. No. 39 [Order] at 1101–03.)[1] Additionally, the Court found that Plaintiffs had failed to allege that Defendants made the statements with knowledge of their falsity. (Order at 1102–04.) Currently before the Court is Plaintiffs' motion for reconsideration of the Order, or, in the alternative, a motion to amend. (Dkt. No. 40 ["Pls.' Mot."] at 3.) For the reasons provided below, the Court DENIES Plaintiffs' motion.

II. LEGAL STANDARD

Plaintiffs move for reconsideration pursuant to Federal Rule of Civil Procedure 59 or, in the

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[1] With respect to the few non-forward-looking statements alleged, the Court concluded that the statements either amounted to non-actionable puffery or that Plaintiffs had failed to allege that any of the "historical results were incorrect." (Order at 1102.)

alternative, request leave to amend under Rule 15. Where, as here, final judgment has been entered, "a motion to amend the complaint can only be entertained if the judgment is first reopened under a motion brought under Rule 59 or 60." *Lindauer v. Rogers,* 91 F.3d 1355, 1357 (9th Cir.1996). The Court thus denies Plaintiffs' motion in the alternative and will only consider the Rule 59 motion for reconsideration.

The standard for obtaining reconsideration of a previously entered order is rigorous. The Ninth Circuit has held that reconsideration is appropriate "if the district court (1) is presented with newly discovered evidence, (2) committed clear error or the initial decision was manifestly unjust, or (3) if there is an intervening change in controlling law." *Sch. Dist. No. 1J, Multnomah Cnty., Or. v. ACandS, Inc.,* 5 F.3d 1255, 1263 (9th Cir.1993). In this district, Local Rule 7–18 provides that "a motion for reconsideration may be made only on the grounds of (a) a material difference in fact or law from that presented to the Court before such decision that in the exercise of reasonable diligence could not have been known to the party moving for reconsideration at the time of such decision, or (b) the emergence of new material facts or a change of law occurring after the time of such decision, or (c) a manifest showing of a failure to consider material facts presented to the Court before such decision." Local Rule 7–18. "No motion for reconsideration shall in any manner repeat any oral or written argument made in support of or in opposition to the original motion." *Id.; see also Kona Enters., Inc. v. Estate of Bishop,* 229 F.3d 877, 890 (9th Cir.2000).

III. ANALYSIS

Plaintiffs request reconsideration on the ground that the Court committed clear error when it dismissed the Complaint *with prejudice.* Plaintiffs do not dispute the dismissal—only that the Court should have granted leave to amend. (Pls.' Mot. at 2.) To that end, Plaintiffs proffer a number of purportedly new facts that they would allege if given the opportunity to bring a second amended complaint. Plaintiffs further contend that the Court erred by taking judicial notice of five PowerPoint slides that were shown at healthcare conferences during which Defendants made allegedly misleading statements.

A. Dismissal with Prejudice

Plaintiffs seek reconsideration of the Court's decision to dismiss the Amended Complaint with prejudice, citing the liberal policy in favor of granting leave to amend and the Ninth Circuit decision in *Eminence Capital, LLC v. Aspeon, Inc.,* 316 F.3d 1048 (9th Cir.2003). Plaintiffs' arguments are unavailing.

Although the district court should grant the plaintiff leave to amend if the complaint can possibly be cured by additional factual allegations, *Doe v. United States,* 58 F.3d 494, 497 (9th Cir.1995), the district court need not grant leave to amend if amendment of the complaint would be futile, *Kendall v. Visa U.S.A., Inc.,* 518 F.3d 1042, 1051–52 (9th Cir.2008). In granting the motion to dismiss, the Court found that all forward-looking statements fell within the safe harbor for two, independent reasons. (*See* Order at 1102 ["[T]he alleged statements are forward-looking and, as discussed

below, qualify for safe harbor under *either* ground." (emphasis added)].) The first reason was that the statements were accompanied by meaningful cautionary language; the second reason was that Plaintiffs had failed to show that the statements were made with knowledge of their falsity. (Order at 1102–04.) Having made such findings, the Court concluded that the Amended Complaint "suffer[ed] from fatal defects" and denied leave to amend. *See Kendall,* 518 F.3d at 1051–52.

Relying heavily on *Eminence,* Plaintiffs contend that granting leave to amend was required, particularly given this "technical and demanding corner of the law" and the need to provide securities litigation plaintiffs with "court guidance" in drafting a sufficient complaint. *See Eminence,* 316 F.3d at 1052–53. However, *Eminence* does not stand for such a blanket rule and clearly states that dismissal with prejudice may be appropriate if "it is clear on de novo review that the complaint could not be saved by amendment." *Id.* at 1052 (citing *Chang v. Chen,* 80 F.3d 1293, 1296 (9th Cir.1996)). Indeed, the liberal amendment policy in the PSLRA context is warranted due to the "unprecedented degree of specificity and detail" required to plead scienter. *Id.* But the present case is not one where Plaintiffs could have fixed their errors after having received the Court's guidance. The rhetorical questions posed by the Ninth Circuit are instructive: "How much detail is *enough* detail? When is an inference of deliberate recklessness *sufficiently* strong?" *Id.* (emphasis in original). Such questions have no applicability here because the basis for the Court's dismissal with prejudice was *not* about Plaintiffs' failure to plead with requisite "specificity and

detail." Rather, it was about a definitive legal bar via the safe harbor to Plaintiffs' claims—the affirmative finding that each of the forward-looking statements was accompanied by meaningful cautionary language. Such an error cannot be remedied.

B. Plaintiffs' Proposed Amendments

Next, Plaintiffs point to a number of new facts that they could bring supporting materiality, falsity, and scienter. Plaintiffs also propose amendments, stylized as "new allegations," that would demonstrate the insufficiency of the cautionary language. Plaintiffs fail to make the requisite showing for reconsideration under Local Rule 7–18. Plaintiffs do not state that the proposed facts (which arise during the Class Period) were not discoverable with the exercise of reasonable diligence or that such facts emerged after the Order was issued. Furthermore, Plaintiffs proposed amendments regarding the inadequacy of the cautionary language merely recycle the same arguments that were already presented in their opposition to the motion to dismiss. *See Kona Enters.,* 229 F.3d at 890 ("A Rule 59(e) motion may *not* be used to raise arguments or present evidence for the first time that could reasonably have been raised earlier in the litigation." (emphasis in original)). For instance, Plaintiffs contend that the cautionary language was insufficient because the stated risk factors—specifically, saturation and the ARRA—did not "relate directly" to the risks that actually materialized and that Defendants repeated the same risk disclosures without providing updates. (Pls.' Mot. at 6–11.) Both these arguments were presented

in Plaintiffs' opposition, (Dkt. No. 32 ["Pls.' Opp'n"] at 21–22), and have already been rejected by the Court, (*see* Order at 1102–03).

In any event, the "new" facts purportedly demonstrating scienter are insufficient to revive Plaintiffs' complaint because of the preclusive effect of the cautionary language. As explained above, the applicability of the cautionary language prong of the safe harbor applied to all forward-looking statements as an independent ground for immunity. Thus, even if Plaintiffs were to allege new facts to "demonstrate that defendants' statements were made with actual knowledge of their falsity," (Pls.' Mot. at 14), this would not disturb the holding that the forward-looking statements were accompanied by meaningful cautionary language. For example, Plaintiffs contend they would allege that Defendant Plochocki stated that QSI's "strong pipeline continues to get stronger and build momentum" and is "continuing to build up every quarter . . . ." (Pls.' Mot. at 12.) Not only is this the same type of "anticipatory statements about the future strength of pipeline sales" that was deemed forward-looking, (*see* Order at 1101–02), but the statement was made at the same May 26, 2011 earnings call conference that this Court found was accompanied by cautionary language, (*see* Order at 1102; Dkt. 29–1, Decl. of Katherine A. Rykken ISO Defs.' MTD ["Rykken Decl."] Exh. 4, [safe harbor provision in Form 8–K for May 26, 2011 earnings call]). The same is true for Plaintiffs' "new" statement by Defendant Plochocki that "all four units remain on target," made at the July 28, 2011 earnings call. (Pls.' Mot.

at 12; *see* Rykken Decl. Exh. 6 [safe harbor provision in Form 8–K for July 28, 2011 earnings call].)[2]

Plaintiffs' already-presented arguments regarding the sufficiency of the cautionary language are equally unavailing. According to Plaintiffs' own cited case, the Seventh Circuit directly refutes Plaintiffs' contention that the risk factors must "warn of risks that . . . actually materialized." (Pls.' Mot. at 7, 11); *see Asher v. Baxter Int'l Inc.,* 377 F.3d 727, 730 (7th Cir.2004) (holding that securities law does not "demand prescience" and "[a]s long as the [defendant] reveals the principal risks, the fact that some other event caused problems cannot be dispositive"). Rather, the cautionary statement need only "identify[ ] important factors that could cause actual results to differ materially from those in the forward-looking statements." 15 U.S.C. § 78u–5(c)(1)(A). Likewise, the cautionary language is not rendered insufficient merely because Defendants utilized similar language in their cautionary disclosures throughout the Class Period.

C. Judicial Notice of PowerPoint Slides

Finally, Plaintiffs seek reconsideration of the Court's decision to take judicial notice of the five PowerPoint slides submitted by Defendants. "On any motion to dismiss based [on the safe harbor], the court shall consider any statement cited in the complaint and any cautionary statement

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[2] Plaintiffs also claim that they will present new, quantitative statements regarding QSI's pipeline, but fail to specify what these statements would be and merely cite to statements from the dismissed Amended Complaint that the Court found to be puffery. (Pls.' Mot. at 12–13; Order at 1101–02.)

accompanying the forward-looking statement, which are not subject to material dispute, cited by the defendant." 15 U.S.C. § 78u–5(e). The Supreme Court affirmed that "courts must consider the complaint in its entirety, as well as other sources courts ordinarily examine when ruling on Rule 12(b)(6) motions to dismiss, in particular, documents incorporated into the complaint by reference, and matters of which a court may take judicial notice." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.,* 551 U.S. 308, 322–23, 127 S.Ct. 2499, 168 L.Ed.2d 179 (2007). Under the "incorporation by reference" doctrine, "a court may consider evidence on which the complaint necessarily relies if: (1) the complaint refers to the document; (2) the document is central to the plaintiffs' claim; and (3) no party questions the authenticity of the copy attached to the 12(b)(6) motion." *Daniels–Hall v. Nat'l Educ. Ass'n,* 629 F.3d 992, 998 (9th Cir.2010).

Citing *Daniels–Hall,* the Court took judicial notice of the PowerPoint slides. (Order at 1099 n. 5.) The Amended Complaint alleged that Defendants' misleading statements at the healthcare conferences were actionable and made without accompanying cautionary language. (AC ¶¶ 60, 73, 79, 82–84, 92, 173; Pls.' Opp'n at 21.) Disputing this characterization, Defendants sought judicial notice of the PowerPoint slides presented at the conferences and cited the cautionary language contained therein. *See* 15 U.S.C. § 78u–5(e). Importantly, the Court found that Plaintiffs had waived any objection to the request for judicial notice of the PowerPoint slides. (*See* Order at 1099 n. 5.) Plaintiffs now contend, however, that they had insufficient opportunity to object because the slides

were raised in Defendants' reply brief. This argument is simply not true. Although submitted alongside the reply brief, the request for judicial notice of the slides was filed as a separate memorandum, (*see* Dkt. No. 35–1), and Plaintiffs were free to submit an objection to the request. Moreover, the request for judicial notice of the slides was submitted on September 11, 2014—nearly six weeks before the October 20 hearing. Plaintiffs had ample opportunity to object but failed to do so.

Indeed, the Court specifically questioned the attorneys at the hearing about the authenticity of the slides to remove any doubt about their admissibility. (*See* Dkt. No. 44, Tr. of Oct. 20, 2014 Hearing on MTD ["Tr."] 2:24–4:1, 16–20.) Defendants' counsel represented that the slides with the safe harbor warnings were projected at the conference and additionally represented that the slides were posted to a website. (Tr. 4:20–21.) In response, Plaintiffs' counsel only disputed the latter point, noting that "whether these slides were in fact widely distributed, posted to the website" was a factually intensive dispute but further reassured the Court "I don't think we need to get into that dispute." (Tr. 10:13–17.) Later in the hearing, Plaintiffs' counsel again reiterated, "We don't oppose the court take judicial notice within the limits of proper judicial notice that these [slides] exist, but we do not accept them for the truth of the matters asserted or for the additional representations that these warnings were widely disseminated." (Tr. 18:15–21.) Plaintiffs' counsel later added, "[W]e did object, by the way, to appendix B as cumulative and exceeding the page limit." (Tr. 19:16–18.)

Nothing in the record amounts to a challenge of the "authenticity of the copy [of the slides] attached to the 12(b)(6) motion." *See Daniels–Hall,* 629 F.3d at 998. The Order did not rely on Appendix B or on the representation that the slides were widely publicized through a website. Nor did the Order accept the slides for the truth of the matters asserted—that actual results of QSI's performance may be affected by the factors listed. *See City of Roseville Employees' Ret. Sys. v. Sterling Fin. Corp.,* 963 F.Supp.2d 1092, 1108 (E.D.Wash.2013) (distinguishing judicial notice for the truthfulness of the out-of-court representations of the documents from judicial notice of the fact that such documents exist and thus, that the representations were made). Rather, the Court relied on the slides only for the proposition that the slides, as submitted by Defendants, were presented at the same healthcare conferences where Defendants purportedly made misleading statements. (Order at 1102.) Given Plaintiffs' failure to object and this Court's duty to inquire into "whether *all* of the facts alleged, taken collectively, give rise to a strong inference of scienter, [and] not whether any individual allegation, scrutinized in isolation, meets that standard," *Tellabs, Inc.,* 551 U.S. at 322–23, 127 S.Ct. 2499, it was appropriate to take judicial notice of the slides.

IV. CONCLUSION

For the foregoing reasons, Plaintiffs' motion for reconsideration is DENIED.

FILED
SEP 29 2017
MOLLY C. DWYER,
CLERK
U.S. COURT OF
APPEALS

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re: QUALITY SYSTEMS, INC., SECURITIES LITIGATION, --- CITY OF MIAMI FIRE FIGHTERS' AND POLICE OFFICERS' RETIREMENT TRUST; ARKANSAS TEACHER RETIREMENT SYSTEM, Plaintiffs-Appellants, v. QUALITY SYSTEMS, INC.; STEVEN T. PLOCHOCKI; PAUL A. HOLT; SHELDON RAZIN, Defendants-Appellees.	No. 15-55173 D.C. No. 8:13-cv-01818-CJC-JPR Central District of California, Santa Ana ORDER

Before: REINHARDT, W. FLETCHER, and PAEZ, Circuit Judges.

Judge Reinhardt, Judge W. Fletcher, and Judge Paez unanimously voted to deny Defendants-Appellees' petition for rehearing en banc (Dkt. 47), filed September 5, 2017.

The full court has been advised of the petition for rehearing en banc and no judge of the court has requested a vote on whether to rehear the matter en banc. Fed. R. App. P. 35.

The petition for rehearing en banc, filed September 5, 2017, is **DENIED**.

[Attorneys names omitted]

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

* * *

DECLARATION OF KATHERINE A. RYKKEN IN SUPPORT OF DEFENDANTS' SECOND REQUEST FOR JUDICIAL NOTICE[*]

* * *

EXHIBIT 39

* * *

SAFE HARBOR PROVISIONS FOR FORWARD-LOOKING STATEMENTS:

This news release may contain forward-looking statements within the meaning of the federal securities laws. Statements regarding future events, developments, the Company's future performance, as well as management's expectations, beliefs, intentions, plans, estimates or projections relating to the future (including, without limitation, statements concerning revenue and net income), are forward-looking statements within the meaning of these laws and involve a number of risks and uncertainties. Management believes that these forward looking statements are reasonable and are based on reasonable assumptions and forecasts, however, undue reliance should not be placed on such statements that speak only as of the date hereof. Moreover, these forward-looking statements are

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[* Exhibit 39 consists of the written presentation materials from the Goldman Sachs Global Healthcare Conference held on June 9, 2011.]

subject to a number of risks and uncertainties, some of which are outlined below. As a result, actual results may vary materially from those anticipated by the forward-looking statements. Among the important factors that could cause actual results to differ materially from those indicated by such forward-looking statements are: the volume and timing of systems sales and installations; length of sales cycles and the installation process; the possibility that products will not achieve or sustain market acceptance; seasonal patterns of sales and customer buying behavior; impact of incentive payments under The American Recovery and Reinvestment Act on sales and the ability of the Company to meet continued certification requirements; the development by competitors of new or superior technologies; the timing, cost and success or failure of new product and service introductions, development and product upgrade releases; undetected errors or bugs in software; product liability; changing economic, political or regulatory influences in the health-care industry; changes in product-pricing policies; availability of third-party products and components; competitive pressures including product offerings, pricing and promotional activities; the Company's ability or inability to attract and retain qualified personnel; possible regulation of the Company's software by the U.S. Food and Drug Administration; uncertainties concerning threatened, pending and new litigation against the Company including related professional services fees; uncertainties concerning the amount and timing of professional fees incurred by the Company generally; changes of accounting estimates and assumptions used to prepare the prior periods'

financial statements; general economic conditions; and the risk factors detailed from time to time in the Company's periodic reports and registration statements filed with the Securities and Exchange Commission.

15 U.S.C. § 78u–5

§ 78u-5. Application of safe harbor for forward-looking statements

(a) Applicability

This section shall apply only to a forward-looking statement made by—

(1) an issuer that, at the time that the statement is made, is subject to the reporting requirements of section 78m(a) of this title or section 78*o*(d) of this title;

(2) a person acting on behalf of such issuer;

(3) an outside reviewer retained by such issuer making a statement on behalf of such issuer; or

(4) an underwriter, with respect to information provided by such issuer or information derived from information provided by such issuer.

(b) Exclusions

Except to the extent otherwise specifically provided by rule, regulation, or order of the Commission, this section shall not apply to a forward-looking statement—

(1) that is made with respect to the business or operations of the issuer, if the issuer—

(A) during the 3-year period preceding the date on which the statement was first made—

(i) was convicted of any felony or misdemeanor described in clauses (i) through (iv) of section 78*o*(b)(4)(B) of this title; or

(ii) has been made the subject of a judicial or administrative decree or order arising out of a governmental action that—

(I) prohibits future violations of the antifraud provisions of the securities laws;

(II) requires that the issuer cease and desist from violating the antifraud provisions of the securities laws; or

(III) determines that the issuer violated the antifraud provisions of the securities laws;

(B) makes the forward-looking statement in connection with an offering of securities by a blank check company;

(C) issues penny stock;

(D) makes the forward-looking statement in connection with a rollup transaction; or

(E) makes the forward-looking statement in connection with a going private transaction; or

(2) that is—

(A) included in a financial statement prepared in accordance with generally accepted accounting principles;

(B) contained in a registration statement of, or otherwise issued by, an investment company;

(C) made in connection with a tender offer;

(D) made in connection with an initial public offering;

(E) made in connection with an offering by, or relating to the operations of, a partnership, limited liability company, or a direct participation investment program; or

(F) made in a disclosure of beneficial ownership in a report required to be filed with the Commission pursuant to section 78m(d) of this title.

(c) Safe harbor

(1) In general

Except as provided in subsection (b), in any private action arising under this chapter that is based on an untrue statement of a material fact or omission of a material fact necessary to make the statement not misleading, a person referred to in subsection (a) shall not be liable with respect to any forward-looking statement, whether written or oral, if and to the extent that—

(A) the forward-looking statement is—

(i) identified as a forward-looking statement, and is accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement; or

(ii) immaterial; or

(B) the plaintiff fails to prove that the forward-looking statement—

(i) if made by a natural person, was made with actual knowledge by that person that the statement was false or misleading; or

(ii) if made by a business entity;[1] was—

(I) made by or with the approval of an executive officer of that entity; and

(II) made or approved by such officer with actual knowledge by that officer that the statement was false or misleading.

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[1] So in original. The semicolon probably should be a comma.

(2) Oral forward-looking statements

In the case of an oral forward-looking statement made by an issuer that is subject to the reporting requirements of section 78m(a) of this title or section 78*o*(d) of this title, or by a person acting on behalf of such issuer, the requirement set forth in paragraph (1)(A) shall be deemed to be satisfied—

(A) if the oral forward-looking statement is accompanied by a cautionary statement—

(i) that the particular oral statement is a forward-looking statement; and

(ii) that the actual results might differ materially from those projected in the forward-looking statement; and

(B) if—

(i) the oral forward-looking statement is accompanied by an oral statement that additional information concerning factors that could cause actual results to materially differ from those in the forward-looking statement is contained in a readily available written document, or portion thereof;

(ii) the accompanying oral statement referred to in clause (i) identifies the document, or portion thereof, that contains the additional information about those factors relating to the forward-looking statement; and

(iii) the information contained in that written document is a cautionary statement that satisfies the standard established in paragraph (1)(A).

(3) Availability

Any document filed with the Commission or generally disseminated shall be deemed to be readily available for purposes of paragraph (2).

(4) Effect on other safe harbors

The exemption provided for in paragraph (1) shall be in addition to any exemption that the Commission may establish by rule or regulation under subsection (g) of this section.

(d) Duty to update

Nothing in this section shall impose upon any person a duty to update a forward-looking statement.

(e) Dispositive motion

On any motion to dismiss based upon subsection (c)(1), the court shall consider any statement cited in the complaint and any cautionary statement accompanying the forward-looking statement, which are not subject to material dispute, cited by the defendant.

(f) Stay pending decision on motion

In any private action arising under this chapter, the court shall stay discovery (other than discovery that is specifically directed to the applicability of the exemption provided for in this section) during the pendency of any motion by a defendant for summary judgment that is based on the grounds that—

(1) the statement or omission upon which the complaint is based is a forward-looking statement within the meaning of this section; and

(2) the exemption provided for in this section precludes a claim for relief.

(g) Exemption authority

In addition to the exemptions provided for in this section, the Commission may, by rule or regulation, provide exemptions from or under any provision of this chapter, including with respect to liability that is based on a statement or that is based on projections or other forward-looking information, if and to the extent that any such exemption is consistent with the public interest and the protection of investors, as determined by the Commission.

(h) Effect on other authority of Commission

Nothing in this section limits, either expressly or by implication, the authority of the Commission to exercise similar authority or to adopt similar rules and regulations with respect to forward-looking statements under any other statute under which the Commission exercises rulemaking authority.

(i) Definitions

For purposes of this section, the following definitions shall apply:

(1) Forward-looking statement

The term "forward-looking statement" means—

(A) a statement containing a projection of revenues, income (including income loss), earnings (including earnings loss) per share, capital expenditures, dividends, capital structure, or other financial items;

(B) a statement of the plans and objectives of management for future operations, including plans or objectives relating to the products or services of the issuer;

(C) a statement of future economic performance, including any such statement contained in a discussion and analysis of

financial condition by the management or in the results of operations included pursuant to the rules and regulations of the Commission;

(D) any statement of the assumptions underlying or relating to any statement described in subparagraph (A), (B), or (C);

(E) any report issued by an outside reviewer retained by an issuer, to the extent that the report assesses a forward-looking statement made by the issuer; or

(F) a statement containing a projection or estimate of such other items as may be specified by rule or regulation of the Commission.

(2) Investment company

The term "investment company" has the same meaning as in section 80a-3(a) of this title.

(3) Going private transaction

The term "going private transaction" has the meaning given that term under the rules or regulations of the Commission issued pursuant to section 78m(e) of this title.

(4) Person acting on behalf of an issuer

The term "person acting on behalf of an issuer" means any officer, director, or employee of such issuer.

(5) Other terms

The terms "blank check company", "roll-up transaction", "partnership", "limited liability company", "executive officer of an entity" and "direct participation investment program", have the meanings given those terms by rule or regulation of the Commission.