Securities Regulation Daily Wrap Up, FRAUD AND MANIPULATION—S.D. Cal.: Second amended complaint fails to address actionable claims, (Dec. 4, 2017)

Securities Regulation Daily Wrap Up

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By R. Jason Howard, J.D.

A California District Court has determined that the second amended complaint in a shareholder class action against BofI Holdings, Inc., a California-based bank, failed to assert sufficient allegations to establish a relevant corrective disclosure of the falsity of the defendants' actionable misrepresentations but granted leave to file a third amended complaint (*In re BofI Holdings, Inc. Securities Litigation*, December 1, 2017, Curiel, G.).

BofI Holdings. Within the second amended complaint (SAC), the court found that the plaintiff's allegations stated plausible securities fraud claims only with respect to BofI and its CEO's statements about: (1) BofI's loan underwriting standards; and (2) internal controls and compliance infrastructure.

The defendants then filed their motion for judgment on the pleadings under the theory that the second amended complaint did not contain sufficient allegations of loss causation. The defendants argued that the corrective disclosures relied upon by the plaintiff, a "whistleblower action and the related New York Times coverage, as well as a litany of articles about BofI published on the website Seeking Alpha—did not disclose the falsity of the actionable misrepresentations and were merely duplicative of publicly available information."

Question for the court. The court explained that the basic question the court must answer is: "[A]fter the disclosures identified by Plaintiff were made, did the market become aware of Defendants' misrepresentations to the extent that BofI's stock price declined? If yes, Plaintiff has pled with particularity how Defendants' misrepresentations caused Plaintiff harm; if no, Plaintiff's allegations do not meet the pleading requirements."

Corrective disclosures. The court reviewed the *Erhart* complaint and the various articles referred to in the SAC, but it concluded that even after considering all the documents together, the SAC failed to identify a relevant corrective disclosure.

The *Erhart* complaint was determined to be irrelevant to the CEO's allegedly false statements so it could not serve as even a partial disclosure, and the SAC did not identify a sufficient corrective disclosure of the falsity of the CEO's statements about BofI's loan underwriting standards or its compliance infrastructure.

Findings. The court found that the articles represented in the SAC were insufficient for two reasons. The first was that they relied exclusively on previously disclosed public information, and the second, more important reason according to the court, was that the articles were not relevant to the misrepresentations the court had found to be actionable in the context of BofI's internal controls and compliance infrastructure.

Continuing, the court explained that while the articles identified many serious violations of federal law and securities regulations, none of the articles contradicted the CEO's statements or suggested that they were false.

The court concluded, stating that because the articles did not disclose the falsity of the actionable misrepresentations identified by the SAC, the SAC failed to allege loss causation with particularity as to the CEO's statements about BofI's internal controls and compliance infrastructure.

The court granted the defendants' motion for judgment on the pleadings but also granted the plaintiff leave to amend the SAC. The third amended complaint is due within 21 days of the date of the order.

The case is No. 3:15-cv-02324-GPC-KSC.

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