

Ninth Circuit rejects securities fraud claim involving ambiguous tech lingo

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On November 19, 2024, a Ninth Circuit panel affirmed the dismissal of a securities fraud action alleging that Cloudera and its officers made false and misleading statements regarding the technical capabilities of Cloudera's products. The panel found that because the plaintiff failed to plead facts establishing what "cloud-native" and "cloud architecture" meant—and that the terms have no plain meaning—the plaintiff could not plead that statements about those topics were false or misleading.

In June 2019, after reporting earnings, Cloudera, Inc.—a data management and analytics software company—saw its stock price drop by 40%. Shortly after, an investor filed a putative securities fraud class action asserting claims under, among other provisions, Sections 10(b) of the Securities Exchange Act of 1934 and Securities and Exchange Commission Rule 10b-5.

The plaintiff argued that Cloudera and the individual defendants made materially false and misleading statements that exaggerated the company's technological capabilities. In particular, the plaintiff alleged that the defendants tricked investors by claiming that the company had "original cloud native architecture and cloud-native platform." In reality, the complaint alleged, Cloudera's software was *not* cloud-native and that customers and potential customers "widely panned" the software because it lacked "key attributes of cloud products." (Op. at 5.)

Judge Maxine M. Chesney on the United States District Court for the Northern District of California dismissed the complaint for failure to state a claim. She held that the plaintiff failed to provide a contemporaneous definition for what it meant to have "'cloud-native' products or 'cloud-native' architecture." Judge Chesney allowed the plaintiff to replead, but warned that failure to address the issue would result in dismissal with prejudice.

The plaintiff's second amended complaint challenged dozens of Cloudera's statements. Judge Chesney found that a number were either not false, protected forward-looking statements, or constituted mere puffery. But two dozen related to statements about the cloud-native attributes of Cloudera's software. As to those, the plaintiff attempted to plead what "cloud-native" and "cloud architecture" meant to investors: "that such offerings or capabilities had specific material attributes such as the use of containers, ease-of-use, seamless scalability, security and elasticity." Judge Chesney again dismissed, finding that the proffered definition was not grounded in the record.

The plaintiff appealed. Writing for the [unanimous panel](#), Circuit Judge Eric D. Miller explained that "[i]t is impossible to evaluate the truth or falsity of [Cloudera's] statements without understanding what phrases like 'cloud-native,' 'native public cloud services,' and 'hybrid cloud' meant at the time the statements were made." (Op. at 11.)

The panel found that the second amended complaint's proposed definition might be sufficient to survive dismissal of some cases, but that it did not meet the heightened pleading requirements necessary to survive dismissal of a securities fraud action.

The panel held that when a plaintiff asserts that words in a statement hold a special or nuanced meaning, the plaintiff must plead facts sufficient to demonstrate the basis of that meaning. The sole source the plaintiff cited to support the second amended complaint's definitions came from a blog post that post-dated the statements in question. Including for that reason, the panel found that the plaintiff had not established the contemporaneous meaning of the terms.

The panel's decision provides a useful reminder of how the Private Securities Litigation Reform Act requires that a plaintiff plead particularized facts in seeking to allege that a defendant made a false or misleading statement. Specifically, if the challenged statement contains terms with nuanced or technical meanings, courts in the Ninth Circuit will not merely accept the plaintiff's proffered definition for such terms, but will scrutinize the factual record to determine whether the plaintiff has pleaded sufficient facts to confirm their meaning.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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