No. 17-50840

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

EMPLOYEES' RETIREMENT SYSTEM OF THE STATE OF HAWAII,
*Plaintiff-Appellant*,

vs.

WHOLE FOODS MARKET, INCORPORATED; JOHN P. MACKEY; GLENDA JANE FLANAGAN; WALTER E. ROBB; A. C. GALLO; DAVID LANNON; KENNETH J. MEYER,
*Defendants-Appellees*.

Appeal from the United States District Court
for the Western District of Texas, Austin Division
No. 1:15-cv-00681-LY
The Honorable Lee Yeakel

# PLAINTIFF-APPELLANT'S REPLY BRIEF

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## I. INTRODUCTION

Plaintiff's Complaint plainly and particularly alleges the "who, what, when, where, and how" of defendants' fraud. *ABC Arbitrage Plaintiffs Group v. Tchuruk*, 291 F.3d 336, 350 (5th Cir. 2002). Defendants' specifically identified financial statements[1] were materially false and misleading because they violated the specifically identified accounting rules[2] which prohibit recognizing revenues that are not earned. (ROA.1000-01¶¶126-127) Those allegations, as well as others detailed below, amply plead falsity. *Cent. Laborers' Pension Fund v. Integrated Elec. Servs. Inc.*, 497 F.3d 546, 552 (5th Cir. 2007).

Additionally, defendants have now effectively conceded scienter by acknowledging that Whole Foods' chief lawyer was fully aware of Whole Foods' overcharging throughout the Class Period—and by failing to even address plaintiff's citation to black letter law that a lawyer's knowledge is imputed to her or his client. *Parich v. State Farm Mut. Auto Ins. Co.*, 919 F.2d 906 (5th Cir. 1990). No less than five separate investigations during the Class Period—in two of Whole Foods' largest geographic markets, California and New York—focused on the precise overcharging

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[1] ROA.959¶54; ROA.963¶59; ROA.966-67¶63; ROA.970¶67; ROA.975¶75; ROA.978-79¶81; ROA.982¶88; ROA.985¶94; ROA.999-1000 n.21; ROA.999-1001¶¶124-127.

[2] ASC 605-10-25-1; ASC 605-10-S99-1; ROA.999-1001¶¶124-127.

conduct alleged in the Complaint. (ROA.962¶56(g); ROA.972-74¶¶69-71; ROA.977¶77; ROA.981¶83; ROA.987-88¶96; ROA.996¶112) Whole Foods' lawyer, "Global Litigation Counsel" John Hempfling, represented the company in each one. (ROA.993-94¶108 and nn.17-19; ROA.694¶7) In light of defendants' concession, scienter is addressed first in reply.

Defendants simply cannot defend the district court's dismissal on falsity, scienter, loss causation, or control person liability grounds. Instead, defendants pepper their brief with factual disputes that have no place in a pleading analysis when all fact allegations must be assumed true. *Lormand v. US Unwired, Inc.*, 565 F.3d 228, 232 (5th Cir. 2009). They entirely omit decisions by the Supreme Court and this Court that are central to scienter in this case: *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27 (2011); *Spitzberg v. Houston American Energy Corp.*, 758 F.3d 676 (5th Cir. 2014); *Parich*, 919 F.2d 906. When the correct pleading standard and relevant law are applied, it is clear that reversal is required.

## II. ARGUMENT

### A. Defendants Effectively Concede Scienter

Defendants ask this Court to find that plaintiff has not pled "an inference of scienter *at least as likely as* any plausible opposing inference" (*Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 328 (2007) (emphasis in original))—"even in light of the Global Litigation Counsel's knowledge of both the California and New York City investigations." (Defendants' Brief ("DB") 1)

Thus, defendants acknowledge that Global Litigation Counsel, Hempfling, is specifically alleged to have been the point person in both the California and New York regulatory actions that spanned the Class Period. (ROA.694¶7; ROA.993-94¶108 and nn.17-19; ROA.988-90¶98) He knew about the overcharging in detail, as well as Whole Foods' commitment to implement changes to correct the problem. (*Id.*)

Defendants' assertion that scienter is not well-pled entirely ignores settled law establishing that Hempfling's knowledge is imputed to his client, Whole Foods, as argued in Appellant's Opening Brief ("AOB"). *Parich*, 919 F.2d at 916.

### 1. Defendants Admit that Whole Foods' Chief Lawyer Knew About the Overpricing Issue for Years and Committed the Company to Making Changes—Knowledge that Is Directly Imputed to the Lawyer's Client, Whole Foods

The Complaint alleges Whole Foods' knowledge, particularly through its chief lawyer, Hempfling, during the July 31, 2013 through July 29, 2015 Class Period. Hempfling signed the California Stipulation on June 18, 2014—after what the State of California described as "lengthy negotiations." (ROA.973¶70) In the California Final Judgment and Permanent Injunction, the Superior Court of the State of California, County of Los Angeles, stated that Whole Foods was represented by "John H. Hempfling, Esq." (ROA.1022-23) Similarly, in New York, the consent order entered between Whole Foods and the New York regulators states that Whole Foods "is represented in this matter by John H. Hempfling II, Esq." (ROA.694¶7) As *The New York Times* reported on June 24, 2015, according to Hempfling, "the company had been working to address [New York City's] concerns since December [2014]." (ROA.988-90¶98)

Thus, Hempfling's knowledge is quite particularly alleged. Overlooking all of these particularized factual allegations, defendants assert in a footnote that plaintiff alleges only a "conclusory assumption" that Whole Foods' counsel was a "senior member of leadership" and attempts to impute Hempfling's knowledge based only on

his "title and alleged position in the leadership ranks." (DB 28 n.6) But, the actual fact allegations—his signature on the California Stipulation, Whole Foods' designation of him as the point person for the California legal action, and Whole Foods' declaration of him as its representative in the New York matters (ROA.993-94¶108 and nn.17-19; ROA.694¶7)—go well beyond a conclusory allegation.

Defendants also completely ignore this Court's jurisprudence confirming that Hempfling's knowledge is directly attributable to Whole Foods as the company's chief lawyer. *Parich*, 919 F.2d at 916. Yet, as this Court plainly holds, "[i]t is well established that notice to [a party's] attorney is imputed to [that party]." *In re Deepwater Horizon*, 819 F.3d 190, 199 & n.7 (5th Cir. 2016) (finding that a client "had actual notice through his counsel, which satisfies due process" and, accordingly, finding it unnecessary to address additional arguments regarding "constructive notice"). The Supreme Court has explained the basis for that imputation: "[The party] voluntarily chose this attorney as his representative in the action, and he cannot now avoid the consequences of the acts or omissions of this freely selected agent. Any other notion would be wholly inconsistent with our system of representative litigation, in which each party is deemed bound by the acts of his lawyer-agent and is considered to have 'notice of all facts, notice of which can be charged upon the

attorney.'" *Link v. Wabash R. Co.*, 370 U.S. 626, 633-34 (1962) (quoting *Smith v. Ayer*, 101 U.S. 320, 326 (1879)).

The district court acknowledged the concept of imputing "in-house counsel's knowledge" in analyzing scienter—but, only considered whether to "impute knowledge of the California and New York investigations on *all the Individual Defendants*." (ROA.1391, emphasis added) The district court never mentioned the more direct imputation of Hempfling's knowledge to the company. (*Id.*) That imputation of knowledge from lawyer to client is "well-established" (*Deepwater Horizon*, 819 F.3d at 199) and amply pleads scienter here.

Indeed, Hempfling's knowledge is also specifically imputed to Whole Foods on basic agency principles as Whole Foods designated him as the point person for the California legal action and declared him as the company's representative in the New York matters. (ROA.993-94¶108 and nn.17-19; ROA.694¶7) He was a "senior official[]" "acting within the scope of [his] apparent authority." *Adams v. Kinder-Morgan, Inc.*, 340 F.3d 1083, 1106 (10th Cir. 2003) (senior executive officer's knowledge of falsity sufficient to allege scienter of the company in §10(b) and Rule 10b-5 action); *accord City of Monroe Emps. Ret. Sys. v. Bridgestone Corp.*, 399 F.3d 651, 688 (6th Cir. 2005) ("knowledge of a corporate officer or agent acting within the

scope of his authority is attributable to the corporation" in a securities fraud action).[3] "A corporation cannot act or have a mental state by itself, and thus, under the common law, the acts and mental states of its agents and employees will be imputed to the corporation where such natural persons acted on behalf of the corporation." *United States ex rel. Vavra v. Kellogg Brown & Root, Inc.*, 848 F.3d 366, 372 (5th Cir. 2017).

Hempfling's knowledge is Whole Foods' knowledge—both on attorney-client and agency principles. That knowledge is plainly sufficient to plead a strong inference of scienter. *Lormand*, 565 F.3d at 254 n.17. Defendants' opposing argument—that defendants who are alleged to have made knowingly false statements to investors can never be liable for securities fraud unless a plaintiff is also able to plead the nefarious thought process that motivated them to be knowingly false—is absurd.

It is also contrary to law. As this Court has emphasized, the "required state of mind [for scienter] is an intent to deceive, manipulate, or defraud *or* severe recklessness." *Id.* at 251 (alteration in original; emphasis added). Specifically, contrary to the district court's ruling (ROA.1391), the "absence of a motive allegation, though relevant, is not dispositive" under the PSLRA. *Matrixx*, 563 U.S. at 48. Thus, while the district court dismissed the Complaint by holding that it alleged "only

[3] Internal quotations and citations are omitted throughout, unless noted.

purported knowledge, not intent to deceive" (ROA.1391), this Court holds that it is a "mistake[]" to "focus[] on the presence or absence of a pecuniary motive for Defendants-Appellees to commit securities fraud." *Spitzberg*, 758 F.3d at 685.

Despite all of the above and the district court's conclusion that plaintiff had indeed alleged "in-house counsel's knowledge" (ROA.1391), defendants contradict themselves by persisting that the Complaint "has not alleged direct knowledge with particularity." (*Compare* DB 1 *with* DB 31) Worse, in a footnote, defendants urge that the district court was correct in holding that something more than "merely knowledge" is needed to plead a knowing state of mind. (DB 31 n.10) In doing so, defendants fail to mention *Matrixx* or *Spitzberg* and instead offer their "basic psychological point" that they believe motive should matter. (*Id.*)

Whole Foods' scienter is well pled. Hempfling's knowledge of ongoing regulatory and legal actions regarding the overcharging—as well as his knowledge of the requirement that Whole Foods adopt specific practices and hire specific employees to correct the problem—are alleged with particularity. (ROA.973¶70) Indeed, the district court recognized as much (ROA.1391)—and defendants have effectively conceded Whole Foods' knowledge through Hempfling. (DB 1) Thus, "'a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged.'" *Spitzberg*, 758 F.3d at

684 (quoting *Tellabs*, 551 U.S. at 324). The district court's dismissal should be reversed.

### 2. Given that Whole Foods' Chief Lawyer Committed the Company to Detailed and Systemic Changes on Pricing, It Would Be Absurd to Think that the Co-CEOs and Other Officers Did Not Know About the Overcharging and Its Consequences

Scienter is also well pled as to the individual defendants. The investigations in California and New York spanned years, preceding the beginning of the Class Period in July 2013, and continuing well past the end of it, until at least 2016. (ROA.962¶56(g); ROA.981¶84) By June 18, 2014 (the middle of the Class Period), Whole Foods had already been investigated by several California cities (ROA.962¶56(g)) and sued by the cities of Los Angeles, Santa Monica, and San Diego on behalf of the State of California. (ROA.972-73¶69)

To settle the California lawsuit, Hempfling stipulated to final judgment and a "permanent injunction" for "five years," prohibiting Whole Foods from "[k]nowingly marking a short weight or taking a false tare on any container." (ROA.973¶70; ROA.1022-35) The Stipulation also committed Whole Foods to creating specific systems for "pricing accuracy," "random in-store price-checking audits," and prompt investigation of any "[p]ricing [d]iscrepancy." (*Id.*) Thus, pursuant to the Stipulation,

Whole Foods needed to hire personnel and outside auditors—and adopt specific policies for five years. (ROA.973¶70)

It is plainly reasonable to infer that Whole Foods' senior management was involved in: (1) agreeing to settle a lawsuit with the State of California; (2) stipulating to a permanent injunction on Whole Foods' overpricing; (3) creating systems for "[e]ach defendants' store in California" to comply with the "pricing accuracy" and "in-store price-checking audits"; and (4) facilitating prompt investigation of any "[p]ricing [d]iscrepancy." (*Id.*) Indeed, defendants' proffered competing inference—that management knew nothing about the California settlement and Stipulation—is wholly implausible and would be gross recklessness in its own right.

Defendants and co-CEOs Robb and Mackey expressly admitted knowing about the New York investigations into the same issues. (ROA.990¶99; ROA.992¶104) According to Robb, "[a]s soon as the New York City Department of Consumer Affairs came to us, we worked to understand and address the issues."[4] (ROA.992¶104) Even further, he told investors "[w]e have taken immediate steps to address these issues, including improving our training regarding in-store packing, weighing, and labeling

[4] As Hempfling told *The New York Times*, Whole Foods knew of the New York overcharging by at least December 2014. (ROA.988-90¶98)

processes; and expanding our third-party auditing process *Company-wide*." (*Id.*, emphasis added)

Despite this statement that defendants not only knew about the pricing problem, but had "taken immediate steps" to put systems in place to address the problem—on a "Company-wide" basis—defendants ask this Court to find that the inference they did not know about the pricing issue is *stronger* than the inference that they did. Defendants' position defies credulity. Even if the opposing inferences were close, which they are not, "'a tie favors the plaintiff.'" *Lormand*, 565 F.3d at 254 (citing *Tellabs*, 551 U.S. at 323-24).

Indeed, the inference of scienter for the individual defendants is especially strong here because, at the very time they were being investigated by California and New York regulators for overpricing and being compelled to make "Company-wide" changes in pricing accuracy, defendants nonetheless persistently told investors that it was transparency and value pricing that separated Whole Foods from others in the grocery industry. (ROA.967¶64; ROA.974-75¶74) Allegations that defendants spoke falsely on the very issue for which Whole Foods was being investigated raise a strong inference of scienter because defendants "must have been aware of the danger of misleading the investing public." *Plotkin v. IP Axess Inc.*, 407 F.3d 690, 697 (5th Cir. 2005).

Defendants also continued to certify the company's financial statements as accurate and reliable. (*E.g.*, ROA.959-60¶55) An inference of scienter is "proper 'if the person signing the certification had reason to know, or should have suspected, due to the presence of glaring accounting irregularities or other "red flags," that the financial statements contained material misstatements or omissions.'" *Central Laborers*, 497 F.3d at 554-55 (quoting *Garfield v. NDC Health Corp.*, 466 F.3d 1255, 1266 (11th Cir. 2006)). The need to implement "Company-wide" changes at Whole Foods (ROA.992¶104) is more than a "red flag."

Even further, the fact that defendants persisted in the same overcharging over years and despite intervention from multiple regulators in two of Whole Foods' largest markets also supports a strong inference of scienter. Where "defendants persisted in the incorrect accounting after receiving the report[s]" that they were incorrect, this Court held scienter was amply pled. *Barrie v. Intervoice-Brite, Inc.*, 397 F.3d 249, 264 (5th Cir. 2005). Here, that was exactly the case. As the City Attorney for Los Angeles explained, there was a "high volume of errors that occurred over and over and weren't fixed. And the company knew about them and didn't fix them." (ROA.993-94¶108)

"[T]aken collectively," those allegations amply plead scienter as to Whole Foods' co-CEOs Mackey and Robb, Whole Foods' CFO and Executive Vice President

Flanagan, Whole Foods' President and COO Gallo and two Executive Vice Presidents of Operations, Lannon and Meyer. *Lormand*, 565 F.3d at 251. This was the team that reportedly "functioned as a sort of CEO committee" and made "decisions on strategy, finances, and other company matters" "collectively." (ROA.957¶49) The combined allegations absolutely "give rise to a strong plausible inference of scienter." *Lormand*, 565 F.3d at 251.

### B. Defendants Cannot Dispute the Particularity of Plaintiff's Detailed Allegations of Falsity

Falsity is straight-forward in this case. And the false statements, as well as the reasons why false, are particularized.

First, Whole Foods' financial statements throughout the Class Period were false. Pursuant to GAAP, a company may only recognize revenues once they are earned—once "the entity has substantially accomplished what it must do to be entitled to the benefits represented by the revenues." (ROA.1001¶127; ASC 605-10-25-1) Despite that requirement, Whole Foods overstated revenue, net income, and earnings throughout the Class Period by at least $127.7 million in New York and California alone by inaccurately labeling the weight of pre-packaged goods. (ROA.1003-05¶¶130-132) As co-CEOs Robb and Mackey eventually admitted: "Straight up, we made some mistakes." (ROA.990¶99)

Second, at the same time that defendants were wantonly charging customers for more food than customers were actually receiving, being investigated for that overcharging, and agreeing to make systemic changes, defendants nonetheless consistently told investors that Whole Foods was distinguished by its value pricing, transparency, and trust between the company and its customers. (ROA.943-44¶12; ROA.967¶64) "[I]n the context of all facts alleged by the complaint and [drawing] all plausible inferences favorable to the plaintiff," those statements were also materially false. *Lormand*, 565 F.3d at 265.

Third, throughout the Class Period, defendants Mackey, Robb, and Flanagan signed Sarbanes-Oxley documents, certifying that Whole Foods' internal controls were sufficient "to provide reasonable assurance regarding the [financial reports'] reliability." (ROA.959-61¶¶55, 56(e); ROA.984¶92(f)) But, as defendants have acknowledged (ROA.990¶99), the financial statements were not reliable; they included substantial "mistakes"—revenues that were not earned. Thus, either the internal controls worked and defendants deliberately concealed that information—or the internal controls did not work and the certifications were false. (ROA.961¶56(d)) Either way, falsity is amply pled. *Spitzberg*, 758 F.3d at 683.

### 1. The Particularized Falsity Allegations More than Satisfy the PSLRA's Requirements Regarding Whole Foods' Overstated Revenues

The particularized details about the precise amount of defendants' overstatement of revenues is far above and beyond the pleading requirements of the PSLRA. The PSLRA requires that plaintiff identify the particular statements alleged to be false. 15 U.S.C. §78u-4(b)(1). Plaintiff has.[5] The PSLRA also requires that plaintiff allege "with particularity why each one of defendants' representations or omissions was 'misleading' under 15 U.S.C. §78u-4(b)(1)." *Spitzberg*, 758 F.3d at 683. Again, plaintiff has.[6] Those allegations satisfy the PSLRA's pleading requirements for falsity.

The additional details—based on defendants' own admissions in the sworn Moll affidavits (ROA.1037-57)—as to the precise amount of the overcharging are well beyond even the demanding pleading requirements of the PSLRA. Those affidavits, filed by Whole Foods in the United States District Court for the Southern District of New York, detailed financial data available to Whole Foods and estimated

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[5] ROA.959¶54; ROA.963¶59; ROA.966-67¶63; ROA.970¶67; ROA.975¶75; ROA.978-79¶81; ROA.982¶88; ROA.985¶94; ROA.999-1000 n.21; ROA.999-1001¶¶124-127; ROA.943-44¶12; ROA.967¶64; ROA.959-61¶¶55, 56(e); ROA.984¶92(f).

[6] ASC 605-10-25-1; ASC 605-10-S99-1; ROA.999-1001¶¶124-127.

the financial impact of the overpricing, including the description of pre-packaged foods affected, the net unit sales of those products, and the net dollars generated by those sales. (ROA.1001-02¶128) Based on that data, Whole Foods quantified a minimum amount of overcharges in excess of $9 million for the State of New York alone from June 2012 to June 2015. (*Id.*) Whole Foods acknowledged that its calculations were based on a "very conservative analysis." (*Id.*) Using the facts attested to in the Moll affidavits, plaintiff estimated that Whole Foods overstated revenues by $127.7 million from June 2012 to June 2015 in New York and California alone. (ROA.1002-04¶¶129-130) Those details—accepted as true at this stage (*Lormand*, 565 F.3d at 265)—are far above and beyond what the PSLRA requires. *Spitzberg*, 758 F.3d at 683.

Moreover, defendants' cavalier assertion that Whole Foods was permitted to recognize the unearned revenue because it was received as "payment at the cash register" (DB 19) completely overlooks the applicable accounting rules. GAAP provides that revenues are only "earned" when there is a "final understanding between the parties as to the specific nature and terms of the agreed-upon transaction." (ROA.1000-01¶126, quoting ASC 605-10-S99-1) But, Whole Foods charged customers for more food than was actually in the package—a misrepresentation of the "nature and terms" of the transaction. GAAP further provides that revenues are only

"earned" once "the entity has substantially accomplished what it must do to be entitled to the benefits represented by the revenues." (ROA.1001¶127; ASC 605-10-25-1) But, Whole Foods put less food in the packages than they represented and collected the extra money anyway. The revenues were not "earned" according to GAAP and, thus, not properly recognized even if Whole Foods was able to dupe customers into making "payment at the cash register." (DB 19)

As here, where defendants "respond that their accounting methods were not improper and that they made no false statements regarding earnings," this Court recognizes that "defendants' argument is fact-based and is therefore insufficient to support a motion to dismiss." *Barrie*, 397 F.3d at 257. Where "accounting questions … are disputed, dismissal was not appropriate." *Id.* Here, falsity is particularly alleged.

### 2. Defendants Themselves Explained the Materiality of Their "Transparency" and "Competitiveness" Statements

Defendants publicly acknowledged the importance of the public's "trust" in Whole Foods—and the materiality of customers' perception of Whole Foods' "transparency" and "accuracy"—in public statements in June 2014. (ROA.973-74¶71) Co-CEO Robb specifically described those "value efforts" as "a key element in driving sales growth." (ROA.974-75¶74)

In that crucial "context," defendants' statements were materially false. *Lormand*, 565 F.3d at 265. Again, the statements have been alleged with particularity (ROA.943-44¶12; ROA.967¶64)—as well as the reasons why they were false. (ROA.999-1001¶¶124-127) Defendants themselves established the materiality. Dismissal was in error.

### 3. Defendants' Fact Disputes Must Await a Later Stage of the Proceedings

Defendants' fact arguments must await summary judgment or trial. This Court is clear that on review of a Rule 12(b)(6) dismissal, it "accept[s] all factual allegations in the complaint as true" and "draw[s] all reasonable inferences in the plaintiff's favor." *Lormand*, 565 F.3d at 232; *accord Pub. Emps.' Ret. Sys. of Miss. v. Amedisys, Inc.*, 769 F.3d 313, 320 (5th Cir. 2014).

Thus, defendants' fact challenges to the Moll affidavits (DB 20-22) must await a later stage. Indeed, their attempt to backpedal from Whole Foods' sworn statements, submitted in federal court, may be tough going even then. But, those assertions have absolutely no place in a pleading stage analysis of falsity where allegations are accepted "as true." *Lormand*, 565 F.3d at 232. Falsity is subject to the PSLRA's particularity requirements—which are more than amply met here, as detailed above. But, the competing inferences analysis that applies to scienter does not apply to falsity (*id*. at 239); particularized allegations are accepted "as true." *Id.* at 232.

For precisely the same reason, defendants' attempt to challenge whether the overcharging problem was "systemic" must await trial. (DB 10) Again, defendants' assertion contradicts Complaint allegations that New York regulators publicly identified "a systematic problem" in which "89 percent of the packages tested did not meet the federal standard"—"the worst case of mislabeling" the inspectors had seen. (ROA.948¶24; ROA.987¶96) Moreover, regardless of what the regulators called it—or were persuaded to ultimately state in a "Consent Order"—the Complaint alleges particularized facts of rampant overcharging throughout California and New York. (ROA.972-73¶69; ROA.948¶24; ROA.987-88¶96) That is systemic. Indeed, when co-CEO Robb eventually acknowledged the issue, he admitted that "Company-wide" changes were necessary. (ROA.992¶104) In any event, defendants' fact-bound challenges have no place at this stage. *Lormand*, 565 F.3d at 232.

### C. Defendants Confuse Loss Causation with an Admission of Liability

Plaintiff's burden for pleading loss causation is simply to "provide the defendant with 'fair notice of what the plaintiff's claim is and the grounds upon which it rests.'" *Lormand*, 565 F.3d at 256 (quoting *Dura Pharms., Inc. v. Broudo*, 544 U.S. 336, 346 (2005)). The Rule 8 pleading standard requires only a "short and plain statement." *Id.*

Here, the Complaint alleged false financial and related statements throughout the Class Period, based on Whole Foods' overcharging for prepackaged goods. (ROA.1008¶141) The Complaint alleges that the New York regulators disclosed the "widespread problem" of "[s]ystemic overcharging" on June 24, 2015 (ROA.1008¶143)—and that defendants acknowledged the financial impact of that disclosure ("national news," "clearly [] affected the comps," "had significant impact on our sales") on July 29, 2015. (ROA.992-93¶¶104-105; ROA.1008¶144)

Those disclosures caused loss. Investors reacted sharply and swiftly, dropping Whole Foods' stock price by $4.74 per share in one day. (ROA.1008¶145) Contrary to defendants' assertion that plaintiff must plead disclosure of a "fraudulent practice" (DB 1), this Court recognizes that loss causation is well-pled by allegations that the market responded to revelation of the financial "impact" of a previously disclosed problem. *Amedisys*, 769 F.3d at 324. Analysts' contemporaneous reports confirmed the connection. (ROA.993¶107) Those allegations more than amply satisfy the Rule 8 pleading requirement.

Still, defendants struggle to support the district court's erroneous ruling that loss causation was not adequately pled. None of their assertions withstands scrutiny.

Defendants urge this Court to make factual findings—contrary to Complaint allegations on an issue that is subject to Rule 8 pleading—that "the weights and

measures issues" were already part of the "total mix" of information in the market. (DB 35) But, the Complaint alleges that the revelation of "impact" information was new—and alleges analyst reaction to that "news." (ROA.1008¶144; ROA.992-93¶¶104-105, 107) Moreover, this Court holds that it is "not authorized or required to determine whether the plaintiff's plausible inference of loss causation [under 15 U.S.C. §78u-4(b)(4)] is equally or more plausible than other competing inferences, as [it] must in assessing allegations of scienter under the PSLRA." *Spitzberg*, 758 F.3d at 683 (first alteration in original).

Further, as Judge Easterbrook pointedly explained in response to a similar assertion by other defendants that "the full truth had reached the market," "[i]f this is so, however, it is hard to understand the sharp drop in the price of its stock." *Asher v. Baxter Int'l Inc.*, 377 F.3d 727, 735 (7th Cir. 2004). In any event, a "'truth-on-the-market' defense" is not available at the pleading stage. *Id.*

Defendants also urge this Court to find import in Whole Foods' decisions not to issue a "disclosure of restated earnings" or an "admission of wrongdoing." (DB 13) Of course, neither a restatement nor defendants' admission is a requisite to pleading loss causation—or fraud. As the First Circuit explained in rejecting a defendant's claim that failure to issue a restatement should insulate it from fraud liability, "[t]o hold otherwise would shift to accountants the responsibility that belongs to the courts.

It would also allow officers and directors of corporations to exercise an unwarranted degree of control over whether they are sued, because they must agree to a restatement of the financial statements." *Aldridge v. A.T. Cross Corp.*, 284 F.3d 72, 83 (1st Cir. 2002).

In short, plaintiff's allegations more than amply provide the required "fair notice" to defendants. *Lormand*, 565 F.3d at 256. As this Court recognized in reversing another district court's dismissal of well-pled loss causation allegations, "[w]here the Complaint sets forth specific allegations of a series of partial corrective disclosures, joined with the subsequent fall in [the company's] stock value, and in the absence of any other contravening negative event, the plaintiffs have complied with *Dura*'s analysis of loss causation." *Amedisys*, 769 F.3d at 326. Plaintiff here has more than met that standard.

### D. The "CEO Committee" that Consulted Each Other on All Major Decisions Certainly Had Control Person Liability

The control person liability allegations are also well-pled. (ROA.957-58¶¶49-51) The Complaint alleges each individual defendant's role in the company and each one's ability to control Whole Foods' financial and other statements. (*Id.*) The Complaint also alleges that defendants Mackey, Robb, and Flanagan certified the accuracy of Whole Foods' financial statements throughout the Class Period. (ROA.959-60¶55; ROA.970¶67; ROA.978-79¶81; ROA.985¶94) Indeed, the

Complaint further alleges that the named defendants "functioned as a sort of CEO committee, collectively making decisions on strategy, finances, and other company matters." (ROA.957¶49)

The district court's dismissal was based on its dismissal of the underlying §10(b) claim, not any lack of allegation that the chief officers and managers of the company did control Whole Foods. (ROA.1394) Thus, defendants' discussion of whether the individuals "were weighing products" or "had notice of the supposed 'practices'" (DB 39) makes no sense in the context of control person liability. Each individual is alleged to have had "actual power or influence" over Whole Foods. *Abbott v. Equity Grp., Inc.*, 2 F.3d 613, 620 (5th Cir. 1993). That is all this Court requires.

## III. CONCLUSION

For the reasons set forth above, the district court's dismissal of securities claims under §§10(b) and 20(a) of the Exchange Act should be reversed.

DATED: February 7, 2018

Respectfully submitted,

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## RULE 32(g) CERTIFICATE

The undersigned counsel certified that PLAINTIFF-APPELLANT'S REPLY BRIEF uses a proportionally spaced Times New Roman typeface, 14-point, and that the text of the brief comprises 4,634 words according to the word count provided by Microsoft Word 2010 word processing software.

*s/Susan K. Alexander*
SUSAN K. ALEXANDER

DECLARATION OF SERVICE

I, the undersigned, declare:

1. That declarant is and was, at all times herein mentioned, a citizen of the United States and employed in the City and County of San Francisco, over the age of 18 years, and not a party to or interested party in the within action; that declarant's business address is Post Montgomery Center, One Montgomery Street, Suite 1800, San Francisco, California 94104.

2. I hereby certify that on February 7, 2018, I electronically filed the foregoing document: **PLAINTIFF-APPELLANT'S REPLY BRIEF** with the Clerk of the Court for the United States Court of Appeals for the Fifth Circuit by using the appellate CM/ECF system.

3. I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

I declare under penalty of perjury that the foregoing is true and correct. Executed on February 7, 2018, at San Francisco, California.

*s/Tamara J. Love*

TAMARA J. LOVE