

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

IN RE ZOOM SECURITIES LITIGATION

Case No. [20-cv-02353-JD](#)

ORDER RE MOTION TO DISMISS

Re: Dkt. No. 78

This is a securities fraud class action against Zoom Video Communications, Inc., and its CEO, Eric Yuan, and CFO, Kelly Steckelberg. Court-appointed lead plaintiff Adam Butt filed a consolidated complaint on behalf of “all who purchased or acquired Zoom securities from April 18, 2019 through April 6, 2020.” Dkt. No. 63 (Compl.) ¶ 2. Butt alleges that defendants violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78j(b) and 78t(a), and SEC Rule 10b-5, 17 C.F.R. § 240.10b-5, “by making false and misleading statements and omissions concerning the Company’s operations; the security capabilities, including the ability to use AES 256-bit end-to-end encryption, available in its main product offering, Zoom Meetings; and its collection and use of its users’ personal data.” Compl. ¶ 3. The consolidated complaint challenges fifteen statements and omissions identified in plaintiff’s summary chart attached to the complaint. *Id.*, Ex. A.

Defendants ask to dismiss the complaint under the Private Securities Litigation Reform Act of 1995 (PSLRA), 15 U.S.C. § 78u-4, and Federal Rule of Civil Procedure 12(b)(6), for

failure to state a claim. Dkt. No. 78. The parties’ familiarity with the record is assumed, and the

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motion is granted and denied in part. Plaintiff's Section 10(b)/Rule 10b-5 claim against Yuan and Zoom for Statement No. 1 was adequately alleged and will go forward. All of the other statements and claims are dismissed with leave to amend.

DISCUSSION

I. LEGAL STANDARDS

Under Section 10(b) of the Securities Exchange Act of 1934, it is unlawful for any person "[t]o use or employ, in connection with the purchase or sale of any security registered on a national securities exchange . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 78j(b). One of those rules prescribed by the U.S. Securities and Exchange Commission is Rule 10b-5, which makes unlawful for any person to, *inter alia*, "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 the light of the circumstances under which they were made, not misleading." 17 C.F.R. § 240.10b-5(b).

"To plead a claim under [S]ection 10(b) and Rule 10b-5, [plaintiff] must allege: (1) a material misrepresentation or omission; (2) scienter; (3) a connection between the misrepresentation or omission and the purchase or sale of a security; (4) reliance; (5) economic loss; and (6) loss causation." *Or. Pub. Emps. Ret. Fund v. Apollo Grp. Inc.*, 774 F.3d 598, 603 (9th Cir. 2014) (citing *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 157 (2008)). A complaint alleging claims under Section 10(b) and Rule 10b-5 must also "satisfy the dual pleading requirements of Federal Rule of Civil Procedure 9(b) and the PSLRA." *Zucco Partners, LLC v. Digimarc Corp.*, 552 F.3d 981, 990 (9th Cir. 2009).

Under FRCP 9(b), the circumstances constituting the alleged fraud must be stated with particularity. "Rule 9(b) applies to all elements of a securities fraud action." *Or. Pub. Emps. Ret. Fund*, 774 F.3d at 605. The PSLRA further imposes specific pleading requirements on securities fraud plaintiffs for falsity and scienter. *Zucco Partners*, 552 F.3d at 990-91. For falsity, the complaint must "specify each statement alleged to have been misleading, the reason or reasons

on information and belief, . . . state with particularity all facts on which that belief is formed.” 15 U.S.C. § 78u-4(b)(1). For scienter, the complaint must “state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind.” *Id.* § 78u-4(b)(2)(A). “To adequately demonstrate that the ‘defendant acted with the required state of mind,’ a complaint must ‘allege that the defendants made false or misleading statements either intentionally or with deliberate recklessness.’” *Zucco Partners*, 552 F.3d at 991 (quotations and citation omitted).

Section 20(a) of the Act makes certain “controlling persons” also liable for violations of Section 10(b) and its underlying regulations. Specifically, the statute provides that “[e]very person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable . . . , unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.” 15 U.S.C. § 78t(a).

II. CLAIMS AGAINST DEFENDANT STECKELBERG

Defendant Kelly Steckelberg is barely mentioned at all in the complaint. This means that plaintiff has not adequately alleged scienter for the Section 10(b) claim against Steckelberg. The PSLRA requires that “the complaint shall, with respect to each act or omission alleged to violate this chapter, 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). Scienter must be alleged on a statement-by-statement, defendant-by-defendant basis.

The complaint makes just one factual allegation against Steckelberg. Plaintiff says that “Defendant Steckelberg has served as the Company’s CFO since November 2017. Since becoming Zoom’s CFO, Steckelberg had the power to authorize or approve publicly disseminated information about the Company, regularly spoke on Zoom’s quarterly earnings calls with Wall Street analysts and investors, made live presentations at analyst-sponsored investor conferences and signed or authorized filings for Zoom with the SEC.” Compl. ¶ 23. This is little more than a generic job description that comes nowhere close to pleading scienter with the level of

claim against Steckelberg by not individually naming her even once in the “scienter” column. Dkt. No. 63-1. Plaintiff’s opposition brief contains no discussion at all of Steckelberg’s individual scienter. Dkt. No. 80 at 9-13.

Consequently, the Section 10(b) claim against Steckelberg is dismissed. The same goes for the Section 20(a) claim, which also lacks any allegations establishing Steckelberg’s control person liability. The Court declines to reach defendants’ other arguments for dismissal of the claims against Steckelberg.

III. SECTION 10(b) CLAIM AGAINST YUAN AND ZOOM FOR STATEMENT NO. 1

For plaintiff’s 10(b) claim against defendants Yuan and Zoom, dismissal is denied for Statement No. 1 in plaintiff’s summary chart. Dkt. No. 63-1 at 1-3. Plaintiff challenges this statement, which appeared in Zoom’s April 18, 2019 Registration Statement and Prospectus: *“Security and disaster recovery. We offer robust security capabilities, including end-to-end encryption, secure login, administrative controls and role-based access controls.”* *Id.* at 1 (emphasis in original). Defendants do not contest that Yuan “made” this statement by signing the Registration Statement, Dkt. No. 82 at 3 n.2, and they challenge only the elements of falsity, scienter, and loss causation. Dkt. No. 78.

A. Falsity

Plaintiff has satisfied the falsity element for Statement No. 1 by alleging that defendants represented that Zoom offered “end-to-end encryption” when in fact it did not. Plaintiff alleges that “[w]hereas end-to-end encryption means that not even the company that runs the messaging service can access the cryptographic keys necessary to decrypt the end users’ communication, here Zoom secretly maintained access to the cryptographic keys that could allow Zoom to decrypt and decipher the communications between the end users.” Compl. ¶ 9(a). Among other things, plaintiff points to an article published on March 31, 2020, on *The Intercept* website titled, “ZOOM MEETINGS AREN’T END-TO-END ENCRYPTED, DESPITE MISLEADING MARKETING: The video conferencing service can access conversations on its platform.” *Id.* ¶ 56.

Defendants say that plaintiff’s falsity allegations are lacking because the term “end-to-end

which are alleged in the complaint, demonstrate otherwise. Plaintiff alleges that on April 1, 2020, “Yuan published ‘A Message to Our Users’ on Zoom’s blog,” stating, “we recognize that we have fallen short of the community’s -- and our own -- privacy and security expectations.”

Compl. ¶ 62. This blog post by Yuan further “referred and linked to a post of the same date by Oded Gal, Zoom’s Chief Product Officer, titled, ‘The Facts Around Zoom and Encryption for Meetings/Webinars.’” *Id.* ¶ 63. That linked post included these statements: “we want to start by apologizing for the confusion we have caused by incorrectly suggesting that Zoom meetings were capable of using end-to-end encryption. . . . While we never intended to deceive any of our customers, we recognize that there is a discrepancy between the commonly accepted definition of end-to-end encryption and how we were using it.” *Id.*

These statements make this case very different from *Wochos v. Tesla, Inc.*, 985 F.3d 1180, 1194 (9th Cir. 2021), in which the circuit found that plaintiffs had failed to “plead sufficient facts to establish that the actual term used had the distinctive, and false, meaning that plaintiffs claim.” There, plaintiffs “pleaded no facts to support their premise that ‘production car’ would be understood as referring exclusively to the *fully automated* production of identical vehicles.” *Id.* (emphasis in original). That is not the situation here. Plaintiff has identified defendants’ express acknowledgement that they had “incorrectly suggest[ed] that Zoom meetings were capable of using end-to-end encryption,” and they had used the term “end-to-end encryption” differently from “the commonly accepted definition.” Compl. ¶ 63. Plaintiff has adequately alleged that defendants’ Statement No. 1 gave an “impression of a state of affairs that differs in a material way from the one that actually exist[ed].” *Berson v. Applied Signal Tech., Inc.*, 527 F.3d 982, 985 (9th Cir. 2008) (quotations and citation omitted).

B. Scienter

Scienter is also satisfied by plaintiff’s allegations that Yuan -- who made the statement on April 18, 2019, that Zoom offers “end-to-end encryption” -- issued a public statement on April 1, 2020, linking to a post that acknowledged and apologized for Zoom’s “incorrect” use of the term. Defendants’ suggestion that the later statement does not qualify as “a statement similar to ‘I knew

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