UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

IN RE GENWORTH FINANCIAL, INC. SECURITIES LITIGATION	Case No. 14-CV-02392 (AKH)

MEMORANDUM OF LAW IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS THE SECOND AMENDED CLASS ACTION COMPLAINT

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Defendants Genworth Financial, Inc. ("Genworth"), Michael D. Fraizer, and Martin P. Klein respectfully submit this memorandum of law in support of their motion to dismiss Plaintiffs' second amended complaint ("SAC") filed on April 17, 2015 (ECF No. 42) under Fed. R. Civ. P. 9(b) and 12(b)(6) and the Private Securities Litigation Reform Act ("PSLRA").

PRELIMINARY STATEMENT

At the start of the class period in November 2011, Genworth announced a "planned initial public offering of Genworth Australia" "targeted for the second quarter of 2012" (April–June). From the outset, Genworth told investors that while it "expect[s] this transaction is achievable, there can be *no assurance* that this transaction can be executed within the targeted timeframe or on the desired terms," and "[a]dverse market or other conditions might delay or impede the planned IPO." On April 17, 2012, the final day of the purported class period, Genworth announced that the possibility it had warned shareholders about had eventuated, and, based on Genworth Australia's recent performance, postponed the IPO to "early 2013," again subject to certain conditions. Genworth disclosed that, during the first three months of 2012, lenders had submitted more claims, for significantly higher claim amounts, than Genworth Australia had previously anticipated, particularly in the Queensland region. Shortly thereafter, in connection with its first quarter 2012 ("Q1 2012") earnings announcement on May 1, Genworth reported an increase in Genworth Australia reserves of $82 million to account for the increased number and size of claims experienced during the first three months of 2012.

This is Plaintiffs' third attempt to allege that the above sequence of events was a fraudulent scheme by Genworth management to deceive investors, perpetrated for reasons Plaintiffs have yet to articulate, but allegedly involving dozens of misleading statements and persistently falsified financials over the course of the five-month class period (November 3, 2011 to April 17, 2012). Plaintiffs filed their first complaint in April 2014 and an amended complaint

in October 2014. On March 25, 2015, the Court dismissed the amended complaint, ruling that "it fail[ed] to plead a coherent claim for relief," as is required to "satisfy[] the command of the PSLRA, 15 U.S.C. § 78u-4, and Rules 8(a)(2) and 9(b) of the Federal Rules of Civil Procedure." The Court granted Plaintiffs leave to amend with instructions to endeavor to comply with these pleading rules and to plead with "more thought and analysis, and less volubility." Plaintiffs' 157-paragraph second amended complaint hardly qualifies as concise. More importantly, the complaint still fails to set forth a coherent—much less thoughtful or analytical—theory of securities fraud.

First, Plaintiffs accuse Defendants of falsifying a swath of financial results that Genworth Australia reported quarterly during the class period (including loss reserves) and lying about Defendants' plans to execute the IPO, among other challenged statements. Plaintiffs say that Defendants—and literally scores of other Genworth employees—knew all of these statements were false because during the class period Genworth supposedly experienced but did not disclose (i) materially increasing delinquencies on mortgage loans the company insured and (ii) materially increasing mortgage insurance policy claims. But Plaintiffs fail to plead *any* facts supporting the existence of allegedly undisclosed delinquency and claim trends. Instead, Plaintiffs rely on the alleged assertions of two unnamed "confidential witnesses" (dubbed "CW1" and "CW2")—neither of whom offers any plausible or particularized factual allegations supporting Plaintiffs' claims—and a gross mischaracterization of Defendants' post-class period remarks concerning the Q1 2012 reserves strengthening. In short, Plaintiffs fail to specify how or when Genworth's delinquency rates and claims experience were anything other than what Genworth publicly reported, or when and why Genworth's loss reserves were inadequate, much less fraudulent. For these reasons and others explained below, Plaintiffs fail to identify any false

or misleading statement by Defendants. *See* Point I below.

Second, Plaintiffs fail to articulate a logical theory of scienter. This is a critical analytical and legal failure. Nowhere does the complaint explain *why* Defendants would promote the IPO as "very, very important" to Genworth and publicly target its execution for Q2 2012, when they knew—as the complaint alleges—that this schedule was not achievable. Nor does the complaint explain *why* Defendants would conceal increased delinquencies and losses in Q3 and Q4 2011, only to disclose this information one quarter later when Defendants announced results for Q1 2012 and postponed the IPO. The far more compelling inference from Plaintiffs' allegations is non-fraudulent: Genworth believed the IPO was on track until the company experienced unexpected losses in Q1 2012 causing the postponement of the IPO and a strengthening of reserves. That Plaintiffs' allegations more logically describe innocent rather than fraudulent behavior requires dismissal under the comparative analysis required by the Supreme Court's decision in *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308 (2007). Aside from this ground, Plaintiffs' complaint fails to plead a single motive Defendants had to commit fraud or plead that Defendants acted with conscious misbehavior or recklessness, as Second Circuit law requires. Plaintiffs accordingly have not pleaded scienter. *See* Point II below.

Third, independent of the other grounds supporting this motion, Defendants' statements that the planned IPO was "targeted for the second quarter of 2012" are protected by the PSLRA's safe harbor for forward-looking statements. Genworth plainly identified its statements about the "targeted" or "planned" IPO as forward-looking and accompanied them with meaningful cautionary language identifying factors that could cause actual results to change. Moreover, even without this cautionary language, Plaintiffs fail to plead that these statements were made with actual knowledge of their falsity, as required by the PSLRA. *See* Point III below.

Fourth, the individual claims against Mr. Fraizer (Genworth's former CEO), and Mr. Klein (Genworth's CFO) should be dismissed because the complaint is devoid of any particularized allegations demonstrating that either of these individual defendants made a false statement or acted with scienter. *See* Point IV below.

Finally, Plaintiffs' control-person claim under Section 20(a) of the Exchange Act should also be dismissed, as the complaint pleads no underlying securities fraud. *See* Point V below.

STATEMENT OF FACTS

The alleged class period begins on November 3, 2011, when Genworth announced a plan to pursue an IPO of 40% of Genworth Australia, and ends on April 17, 2012, when Genworth announced that it expected to report elevated losses in Australia for the first three months of 2012 and that it was postponing the IPO until early 2013 due to "recent business performance in Australia." SAC ¶¶ 1, 21, 109.[1] The facts below are taken from the complaint and documents the complaint references.[2]

A. Genworth Australia's Mortgage Insurance Business and Loss Reserves

Genworth is the leading provider of mortgage insurance products in many countries outside of the United States, including Australia. SAC ¶ 42. Genworth Australia insures mortgage lenders against borrower default primarily through "single premium" contracts, in

[1] All emphasis added to quotations of Genworth's disclosures in the complaint has been removed.

[2] The Declaration of Greg A. Danilow, filed with this brief, attaches 12 exhibits ("Ex. A" through "Ex. L"). The Court may consider Exhibits A-C and E-L on the basis that they are "documents integral to and relied upon in the complaint, even if not attached or incorporated by reference." *Bd. of Trs. of City of Ft. Lauderdale Gen. Emps.' Ret. Sys. v. Mechel OAO*, 811 F. Supp. 2d 853, 865 (S.D.N.Y. 2011), *aff'd sub nom. Frederick v. Mechel OAO*, 475 F. App'x 353 (2d Cir. 2012). Although not specifically referenced in the complaint, the Court may consider Exhibit D (Genworth's 2010 Form 10-K) because it is a document filed with the SEC (*id.*) and also because this brief cites the risk disclosures from Exhibit D, which are explicitly incorporated by reference in earnings calls and Forms 10-Q cited in the complaint. *See, e.g.*, Ex. A (11/4/2011 Tr.) at 2; Ex. B (Q3 2011 Form 10-Q) at 146. In addition, courts routinely consider such risk disclosures when addressing the sufficiency of cautionary language under the PSLRA safe harbor. *See, e.g.*, *Finn v. Barney*, 471 F. App'x 30, 32 (2d Cir. 2012) (district court did not abuse its discretion in taking judicial notice of "prospectuses that … disclosed the risk of [securities] auction failures"); *Jones v. Perez*, 550 F. App'x 24, 29 (2d Cir. 2013) (considering risks disclosed in defendants' SEC filings). None of these documents are offered for their truth, but rather for the fact of their disclosure, as permitted by the Second Circuit.

which lenders obtain coverage through a one-time, up-front payment. SAC ¶ 44.

Genworth establishes loss reserves for the Australian mortgage insurance policies it issues, as required by GAAP, and discloses these reserves quarterly. Genworth generally "consider[s] a loan to be delinquent and establish[es] reserves if the borrower has failed to make a scheduled mortgage payment." Ex. C (FY 2011 Form 10-K) at 162 (*cited in* SAC ¶ 12).[3] The loss reserve established reflects "management's best estimate of ultimate paid claims for reported delinquencies" on the underlying mortgage loans. SAC ¶ 116. Genworth disclosed in its Fiscal Year ("FY") 2011 Form 10-K dated February 27, 2012, that "[m]anagement reviews quarterly the loss reserves for adequacy, and if indicated, updates the assumptions used … based on actual experience." SAC ¶¶ 13, 55.

Genworth's risk disclosures explain to investors that reserving for predicted future losses is, by definition, "inherently uncertain" and "require[s] significant judgment." Ex. D (FY 2010 Form 10-K) at 105; Ex. C (FY 2011 Form 10-K) at 116. This is because delinquencies occur "for a variety of reasons" and borrowers may cure delinquencies (resulting in no claim costs) "by making all of the delinquent loan payments or by selling the property in full satisfaction of all amounts due under the mortgage." Ex. D (FY 2010 Form 10-K) at 141; *see also* Ex. C (FY 2011 Form 10-K) at 162. Genworth's disclosures explain that loss reserves "reflect estimates and actuarial assumptions with regard to [Genworth's] future experience" and that "[m]any factors can affect future experience, including economic and social conditions." Ex. D (FY 2010 Form 10-K) at 58; Ex. C (FY 2011 Form 10-K) at 62. Thus, Genworth disclosed, it "cannot determine with precision the ultimate amounts [it] will pay for actual claims or the timing of those payments" (Ex. D (FY 2010 Form 10-K) at 58; Ex. C (FY 2011 Form 10-K) at 62), and "[t]he

actual amount of the claim payments may vary significantly from the loss reserve estimates" (Ex. D (FY 2010 Form 10-K) at 106; Ex. C (FY 2011 Form 10-K) at 116).

Along with reserve estimates, Genworth provided investors with exhaustive disclosures concerning the composition, performance, and risk profile of Genworth Australia's mortgage insurance business. Each quarter, including Q3 and Q4 2011, Genworth disclosed quarterly loss ratios (the ratio of incurred losses to earned premiums) (48% (Q3), 46% (Q4)), delinquency rates (0.59% (Q3), 0.55% (Q4)), the total amount of actual paid claims (AU$25 million (Q3), AU$31 million (Q4)), and the average paid claim amount for each quarter (AU$62,400 (Q3), AU$64,000 (Q4)). *See* Ex. E (Q3 2011 Quarterly Fin. Supp.) at 35, 37, 40-41 (*cited in* SAC ¶ 77 & n.5); Ex. F (Q4 2011 Quarterly Fin. Supp.) at 35, 38, 40, 43-44 (*cited in* SAC ¶ 77 & n.5). Genworth also further detailed—for each major geographical region within Australia (including Queensland) and each insurance policy vintage (the year the insurance policy was issued)—delinquencies and the percentage of Genworth Australia's overall risk in-force (*i.e.*, the risk associated with the business's "in-force" (issued) policies) that each region and vintage represented. *Id.*

B. The Impact of the Queensland Flooding

In January 2011, the Queensland region of Australia experienced widely reported severe flooding, which impacted the Australian economy and Genworth Australia's results, including earnings, delinquency rates, loss ratios, and claim amounts. *See* SAC ¶¶ 6-7.

On September 26, 2011, several weeks before the start of the class period, Genworth published a presentation about Genworth Australia's mortgage insurance business and the

[3] "'Delinquency' is defined in [Genworth's] master policies as the borrower's failure to pay when due an amount equal to the scheduled monthly mortgage payment under the terms of the mortgage." Ex. D (FY 2010 Form 10-K) at 141.

ongoing impact of the Queensland flooding. SAC ¶¶ 6-7.[4]

The complaint alleges that, in this presentation, Genworth disclosed that the Queensland region was the "primary driver of [an] increase" in loan delinquency rates, due to factors including the "Queensland flooding," "retail spending [being] down," and "small businesses [being] pressured." SAC ¶ 7. Genworth noted that these factors particularly impacted mortgage insurance policies that Genworth issued in 2007 and 2008 to small-business and self-employed borrowers. SAC ¶ 6. The presentation also addressed the measures taken to mitigate the Queensland risk and projected a "second half [2011] loss ratio in high 40's/low 50's." SAC ¶ 7. Under "Risk Management—Loss Mitigation," Genworth disclosed that the company would "accelerate action on late stage delinquencies." SAC ¶ 7.

Plaintiffs omit from their description of the September 2011 presentation in the complaint Genworth's disclosure—in the same document—that the Queensland book had been "Clearly Impacted" by the January 2011 flooding in Queensland. Ex. G (9/26/2011 Presentation) at 28 (*cited in* SAC ¶¶ 6-7). Genworth also identified the "2007/2008 [loan origination] Books" in the "Queensland Region" as "Pressured," and explained that these books were experiencing delinquencies "above expected levels" and in particular that "small business/self-employed [borrowers] [were] impacted by retail spending decline." SAC ¶ 6.

Although Plaintiffs repeatedly assert that Defendants failed to disclose "deteriorating economic conditions in Queensland" (SAC ¶¶ 92, 97, 107, 132), in fact, Genworth informed investors about the ongoing impact of the Queensland flooding before the beginning of the class

[4] Plaintiffs refer to the September 2011 presentation thirteen times in the second amended complaint (SAC ¶¶ 6-9, 22) but nonetheless also allege that the contents of the presentation "were not discussed by the market" (SAC ¶ 6). Plaintiffs expressly allege, however, that the presentation "reminded investors that Australia had a 'strong financial track record'" and "gave investors assurance that the Australian market was sound, and that known risks related to Queensland and the 2007/2008 books were being effectively managed and mitigated." SAC ¶ 7. Plaintiffs also allege that a Morgan Stanley analyst report discussed the September 2011 presentation. SAC ¶ 22.

period, on the first day of the class period, and each quarter during the class period.

Following the pre-class period disclosure on September 26, 2011, in its Q3 2011 earnings release on November 3, 2011 (*cited in* SAC ¶ 45), Genworth again discussed Genworth Australia's performance and the impact of the Queensland flooding on results. Genworth disclosed that "Australia operating earnings decreased four percent from the prior year due to increased delinquencies." Ex. H (11/3/2011 News Release) at 9. And, consistent with the "high 40s/low 50s" loss ratio projection Genworth made in September 2011, Genworth disclosed a Q3 2011 loss ratio for Genworth Australia of 48% and explained that this "reflect[ed] ongoing economic impacts from flooding in Queensland earlier in 2011 and continued pressure on certain consumers and small business owners from the combined impacts of higher interest rates, increased living costs, currency valuation and lower consumer spending." *Id.* Discussing these disclosures during Genworth's November 4, 2011 earnings call, Genworth's then-CEO, Mr. Fraizer, expressed his view that "Australia is transitioning as expected, absorbing the loss pressures coming from the early 2011 Queensland flood events." SAC ¶ 91. Genworth's CFO, Mr. Klein, opined that, as of Q3 2011, the Australian unemployment rate was "stable" and that the Australian housing market was "sound overall, although certain regions are feeling pressure." SAC ¶ 91.

Plaintiffs claim that Defendants "fail[ed] to disclose that the Australian MI unit was experiencing deteriorating economic conditions in Queensland" (SAC ¶ 92), but in Genworth's Q3 2011 Form 10-Q filed on November 7, 2011 (*cited in* SAC ¶ 89), Genworth disclosed that "the economy has slowed particularly in Queensland, given the economic impact of the flooding in January 2011, pressures from higher interest rates, higher costs of living, higher exchange rates and cautious consumer spending … [and] increased levels of new delinquencies were

reported by financial institutions in this market, *which adversely impacted the results of our operations*." Ex. B (Q3 2011 Form 10-Q) at 74 (emphasis added). Genworth disclosed that delinquencies and reserves had increased because of "the cumulative impact of the factors noted" for previous quarters, and prognosticated that "*these pressures [would] continue through the remainder of 2011*" and "begin to moderate in 2012." *Id.* at 75 (emphasis added).

For Q4 2011, Genworth disclosed in its February 2, 2012 earnings release (*cited in* SAC ¶ 94) that, while delinquencies were lower than in Q3, including in Queensland (SAC ¶ 50), Genworth Australia's operating earnings were down year-over-year "reflecting reserve additions for prior delinquencies where lenders accelerated actions to move these loans through to claim." Ex. I (2/2/2012 News Release) at 9. Directly contradicting Plaintiffs' allegation that Genworth concealed delinquency backlogs caused by lender delays during the class period, Genworth reported in its FY 2011 Form 10-K, filed with the SEC on February 27, 2012, that Genworth Australia had increased reserves in Q4 2011 because lenders were "accelerat[ing] actions to transition delinquencies to claim." Ex. C (FY 2011 Form 10-K) at 159. Also in its FY 2011 Form 10-K, Genworth summarized the delinquencies Genworth Australia experienced for the year:

> In the first quarter of 2011, losses began to increase driven by higher rates, lower retail spending and higher reserves for claims anticipated from the natural disasters during that quarter, particularly the flooding in Queensland. During the second and third quarters of 2011, there was an increase in the number of outstanding delinquencies and reserves as the cumulative impact of the factors noted previously exerted pressure on elements of the portfolio. During the fourth quarter of 2011, total delinquencies decreased but remained above 2010 levels and the rate of new delinquencies slowed.

SAC ¶ 12.

Following the conclusion of Q4 2011, Genworth and its management expressed their opinion that the Australian housing market and Genworth Australia's performance had stabilized, following the increasing delinquency levels in 2011 that they had previously disclosed

and discussed. On Genworth's Q4 2011 earnings call on February 3, 2012, Mr. Klein opined that the Australian housing market was "performing as expected." SAC ¶ 96. On a second investor call on the same day, Mr. Klein also expressed his expectation that housing prices would remain "stable" in Australia. SAC ¶ 104. On March 29, 2012, Mr. Klein expressed the expectation that the Australian market would "remain solid with mortgage originations and MI market size … to remain fairly flat." SAC ¶ 106.

C. Genworth Announces Its Plan to Pursue a Minority IPO of Genworth Australia

On November 3, 2011, Genworth announced its "plan" to pursue a minority IPO of up to 40% of Genworth Australia "in the second quarter of 2012, *subject to market conditions and regulatory review and approval*." SAC ¶ 45 (emphasis added). Genworth explained: "This move is part of a broader strategy to rebalance the business portfolio, support future growth opportunities … and together with other actions, free material capital for redeployment." SAC ¶ 45. Genworth disclosed from the start of the class period that, while it "expect[s] this transaction is achievable, there can be *no assurance* that this transaction can be executed within the targeted timeframe or on the desired terms," and "[a]dverse market or other conditions might delay or impede the planned IPO." Ex. B (Q3 2011 Form 10-Q) at 148 (emphasis added). Plaintiffs do not allege that Defendants' November statements about the planned IPO were false.

Genworth continued to caution investors about the risks attendant to the IPO plan throughout the remainder of the class period, not only in its public filings (*see* Ex. C (FY 2011 Form 10-K) at 85; Ex. I (2/2/2012 News Release) at 20) but also during calls with investors. For example, in a February 3, 2012 investor call, Mr. Klein, Genworth's CFO, stated that the plans for the IPO "remain on track" and that "our expected timing would be sometime in the second quarter." SAC ¶ 104. But Mr. Klein also stated that Genworth was not planning to do the IPO

"out of necessity," but rather "from a position of strength." Ex. J (2/3/2012 Tr.) at 18 (*cited in* SAC ¶ 104). Thus, he stated, "we are managing holding company cash at the moment as if the Australia IPO is not going to occur." *Id.* Mr. Klein continued, "But again the priority is going to be risk buffers and seeing where we are, what the economies look like at that point in time," *i.e.*, the planned Q2 execution date. *Id.*

At a conference on March 29, 2012, Mr. Klein reiterated that "the [IPO] transaction will of course depend on … market conditions including valuation considerations" and that "we're pursuing a[n] [IPO] transaction from a position of strength and will do what's most beneficial for shareholders and bondholders based on the conditions at the time." Ex. K (3/29/2012 Tr.) at 4-5 (*cited in* SAC ¶ 106). Mr. Klein further disclosed during the same conference that, while Genworth was "working very actively" to execute the IPO in Q2 2012, "there's a number of factors that impact timing" of the IPO, and Genworth was "watching those very closely," including "the impact … in the Australian housing market and things of that nature." SAC ¶ 106. Neither of Plaintiffs' "confidential witnesses" (CWs) asserts that either Mr. Klein or Mr. Fraizer or any other member of the senior management team did not believe that the IPO was targeted for Q2 2012 execution, that Genworth was not working hard to execute the IPO, or that Defendants, at any time before the end of the class period, changed the target date of the IPO or stopped working hard to execute it.

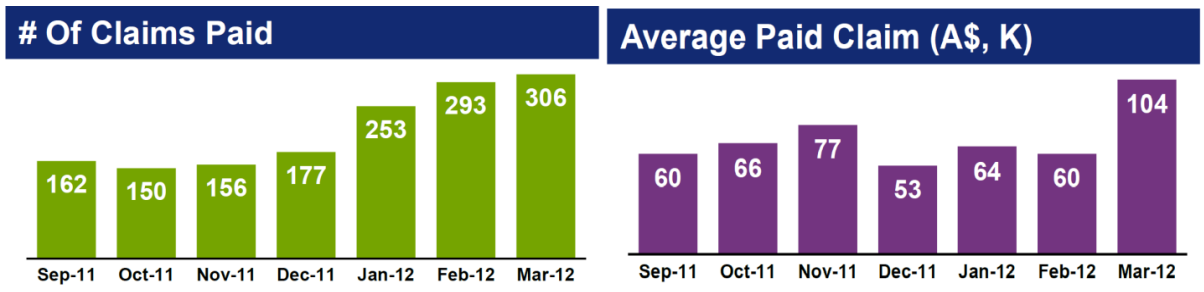
On April 17, 2012, Genworth announced that, due primarily to "recent business performance in Australia," it was delaying the previously targeted Q2 2012 execution of the IPO, stating that, "Genworth is now seeking to complete the IPO in early 2013, subject to market conditions, valuation considerations including business performance, and regulatory approvals." SAC ¶ 109. Elaborating on "business performance in Australia," Genworth disclosed:

> For the 2012 first quarter, the company expects to report elevated loss experience in Australia as lenders accelerated the processing of later-stage delinquencies from prior years through to foreclosure and claim at a higher rate and severity than expected, particularly in coastal areas of Queensland that experienced natural catastrophes and regional economic slowdowns and among certain groups of small business owners and self-employed borrowers. First quarter experience is anticipated to result in a modest first quarter loss in the Australian [mortgage insurance] business.

SAC ¶ 109. This announcement marks the close of the class period.

D. Post-Class Period: Genworth Discloses Q1 2012 Results and Reserve Strengthening

On May 2, 2012, Genworth held an earnings call discussing Genworth Australia's Q1 2012 results. SAC ¶ 85. As discussed below, Genworth explained that sharp increases in the number of claims in Q1 2012 (January–March 2012) and in claim amounts in March 2012—*i.e.*, more claims and for greater amounts—drove these disappointing results. The following charts, presented to investors on the Q1 2012 earnings call, illustrate these trends:



Ex. L (5/2/2012 Presentation) at 9 (*cited in* SAC ¶ 88).

The number of claims paid and the average paid claim amount are separate factors that can separately, and in combination, impact reserves. An increase in the number of claims does not, in and of itself, automatically result in greater losses. For example, from November to December 2011, the number of claims Genworth paid increased by 13.5% (156 to 177). The average paid claim, however, decreased by 31.2% (AU$77,000 to AU$53,000). Thus, despite the increase in the number of claims paid from November to December 2011, the total amount paid

decreased by AU$2.6 million from November (AU$12.0 million) to December (AU$9.4 million).

As Genworth reported during the Q1 2012 earnings call on May 2, there was a significant increase in claim numbers in January (the start of Q1 2012)—42.9% higher than the number of claims in December—with claim numbers remaining at elevated levels through February and March. With respect to paid claim amounts, Genworth disclosed an average paid claim for March 2012 (AU$104,000) that was 67% greater than the average paid claim amount disclosed for Q3 2011 and 61% greater than the amount disclosed for Q4 2011. *Compare* Ex. L (5/2/2012 Presentation) at 9, *with* Ex. E (Q3 2011 Quarterly Fin. Supp.) at 41; Ex. F (Q4 2011 Quarterly Fin. Supp.) at 44. Indeed, as Mr. Upton explained on the earnings call, claim severity (the claim amount) "was more concentrated in March, with a significant increase in the average claim paid as many of these claims also had higher loan balances." SAC ¶ 116. In the subsequent Q&A portion of the call, in response to an analyst's asking whether the need for reserve strengthening for Genworth Australia "should have been caught earlier or was … truly something that arose in March," Mr. Upton explained: "it was—the March loss emergence and the average claims size[] that really gave rise to our deep dive on the delinquency inventory and the extensive review that we undertook to strengthen loss reserves of $82 million." SAC ¶ 117.

Mr. Upton also discussed that, "[i]n the second half of 2011, we did see increasing delinquency levels and we did observe lender processing delays" and went on to note that Genworth had begun "to work more closely with those lenders to improve the collection and default management techniques" and that this process "did accelerate some of the older delinquencies coming through and as those came through in the first quarter, the claim paid counts did increase in January and February." SAC ¶ 117. This was not new information. As

Plaintiffs acknowledge, Genworth disclosed in its September 2011 presentation that, as part of a risk management effort, it would work to "accelerate action on late stage delinquencies." SAC ¶ 7. Genworth later explained in a February 2, 2012 news release announcing Q4 2011 results and then again in its FY 2011 Form 10-K filed on February 27, 2012 that the company had increased reserves for "prior delinquencies *where lenders accelerated actions to move these loans through to claim*." Ex. I (2/2/2012 News Release) at 9 (emphasis added); *see also* Ex. C (FY 2011 Form 10-K) at 159 (disclosing "increased reserves … *as lenders accelerated actions to transition delinquencies to claim*") (emphasis added). Thus, Mr. Upton's statement that "[i]n the second half of 2011, we did see increasing delinquency levels"—which Plaintiffs mischaracterize as an "admi[ssion]" or "forced" acknowledgement that earlier statements were false (SAC ¶¶ 85, 87; *see also* SAC ¶ 16)—is nothing of that sort. Rather, it is a reiteration of prior disclosures updated to reflect subsequent events that occurred in Q1 2012, not before.

ARGUMENT

"To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (citation omitted). "'[L]abels and conclusions'" and "'naked assertion[s]' devoid of 'further factual enhancement'" do not suffice. *Id.* (citation omitted). To state a claim for securities fraud under Section 10(b) of the Exchange Act, a plaintiff must adequately plead (i) a material misrepresentation; (ii) scienter; (iii) a connection with the purchase or sale of a security; (iv) reliance; (v) economic loss; and (vi) loss causation. *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 341-42 (2005). Under Rule 9(b) and the PSLRA, a complaint asserting a Section 10(b) claim must "stat[e] with particularity the circumstances constituting fraud." *ECA & Local 134 IBEW Joint Pension Trust v. JP Morgan Chase Co.*, 553 F.3d 187, 196 (2d Cir. 2009). In addition, the PSLRA safe harbor for forward-looking statements protects statements about "plans

and objectives of management for future operations" (15 U.S.C. § 78u-5(i)(1)) that are "identified and accompanied by meaningful cautionary language *or* [are] immaterial *or* the plaintiff fails to prove that [the statement] was made with actual knowledge that it was false or misleading" (*Slayton v. Am. Express Co.*, 604 F.3d 758, 766 (2d Cir. 2010)). Plaintiffs' complaint does not even plausibly state a Section 10(b) claim, much less satisfy the heightened pleading requirements of Rule 9(b) and the PSLRA.

I. PLAINTIFFS FAIL TO PLEAD AN ACTIONABLE FALSE STATEMENT OR OMISSION

Plaintiffs claim that Defendants made some two-dozen false and misleading statements during the November 4, 2011 to April 17, 2012 class period. SAC ¶¶ 89-108. The challenged statements generally cover three subjects: (i) Genworth Australia's financial performance and results (*see* Point I.A below), (ii) Genworth Australia's loss reserves (*see* Point I.B below), and (iii) Genworth's plan for the IPO (*see* Point I.C below). Plaintiffs allege that all of these statements were false because, in Plaintiffs' words, "[a]t the same time that Fraizer and Klein were reassuring investors that no economic conditions warranted a delay in the IPO, and as the Company continued to report stable loss ratios, internal data revealed a significant increase in claims and delinquencies in Australia during the Class Period." SAC ¶ 59; *see also* SAC ¶¶ 89, 92, 93, 95, 97, 98, 100, 105, 107, 108 (all similarly alleging that Defendants' statements were "false and misleading" because of concealed increases in delinquencies and claims).

Below we address the alleged misstatements, grouped by the three categories identified above, and explain why Plaintiffs have failed to plead, with the particularity that Rule 9(b) and the PSLRA require, that any of Defendants' statements were false.

A. Plaintiffs Fail to Plead that Defendants' Statements Concerning Genworth Australia's Financial Performance and Results Were False

In granting leave to replead, the Court instructed Plaintiffs to endeavor in their second

amended complaint to "'specify each statement alleged to have been misleading,' and 'the reason or reasons why,' but plainly and clearly, and not in an effusive ambiguity as the Amended Complaint does." Dkt. No. 41 at 3 (quoting 15 U.S.C. §78u-4(b)(l)). The second amended complaint fails to satisfy the Court's instruction and the pleading requirements of the PSLRA, Rule 9(b), and the Second Circuit.

Plaintiffs allege that throughout the class period, Genworth regularly reported false financial information for Genworth Australia, including earnings per share, net income, delinquent loans, delinquency rates, loss ratios, net losses, and reserves. SAC ¶ 89. Plaintiffs similarly challenge as false Mr. Fraizer's qualitative assessment of Genworth Australia's performance in November 2011: "Australia is transitioning as expected, absorbing the loss pressures coming from the early 2011 Queensland flood events." SAC ¶ 91. Plaintiffs' sole basis for claiming that these statements were false is their allegation that Genworth Australia was experiencing undisclosed material increases in delinquencies and claims during the class period. *See* SAC ¶¶ 89, 92. The complaint, however, is devoid any particularized, well-pleaded allegations supporting either assertion.

1. Plaintiffs' Unparticularized Assertion that There Were Undisclosed "Increasing Delinquencies" During the Class Period Fails to Demonstrate Falsity

Every quarter, Genworth disclosed, among many other performance metrics, the delinquency rates not only for Genworth Australia's overall portfolio, but also for each major geographical region within Australia, including Queensland, and for each insurance policy vintage, including the 2007 and 2008 vintages. *See* Facts Section A, above. These are the allegedly problematic region and policy vintages. *See* SAC ¶¶ 16, 77, 81, 82, 85, 88, 93, 97, 105.

Notwithstanding these disclosures, Plaintiffs repeatedly insist that Genworth failed to disclose unspecified "increasing delinquencies" for Genworth Australia during the class period.

SAC ¶¶ 89, 95, 97, 100. But Plaintiffs fail to supply any particularized facts. Plaintiffs do not once allege specifically when and by how much Genworth Australia's "true" delinquency rates were higher than disclosed, nor do Plaintiffs once allege that, even if this were the case, what specific information Defendants had demonstrating that they fraudulently reported lower rates.[5]

Instead, Plaintiffs rest on their mischaracterization of a statement made by Genworth's global mortgage insurance CFO, Jerome Upton, during the May 2012 first-quarter-end investor call, that, "[i]n the second half of 2011, we did see increasing delinquency levels and we did observe lender processing delays." SAC ¶¶ 16, 87, 117. Plaintiffs describe this statement as a "Post-Class Period Admission" (SAC at p. 30; SAC ¶ 87)—in other words, a disclosure of information not previously provided to investors. *See* SAC ¶¶ 81, 82, 85, 95, 100 (referencing delinquency trends in the "second half of 2011"). The complaint pleads no basis for this assertion. Plaintiffs identify no class period statement by Defendants that delinquencies were *not* increasing in the second half of 2011. On the contrary, Defendants repeatedly discussed increasing delinquencies and the resulting impact on earnings:

- In a September 2011 presentation, Genworth stated that policies were experiencing delinquencies "above expected levels." SAC ¶ 6.
- In the news release announcing Genworth's Q3 2011 results, Genworth disclosed decreased Australia operating earnings "due to increased delinquencies." Ex. H (11/3/2011 News Release) at 9.
- In its Q3 2011 Form 10-Q, Genworth disclosed that "increased levels of new delinquencies were reported by financial institutions in [the Australian] market," explaining that these increasing delinquencies resulted from "the cumulative impact of the factors noted" for previous quarters, and prognosticated that "these pressures [would] continue through the remainder of 2011." Ex. B (Q3 2011 Form 10-Q) at 74-75.
- In the same Q3 2011 Form 10-Q, Genworth also reported an increase in delinquency rates of approximately 20% for the Queensland region during the

[5] The alleged assertion from Plaintiffs' second CW ("CW2") that, "throughout 2011, there were internal reports showing an increase in delinquencies in Australia" (SAC ¶ 68) fails for the same reasons.

second half of 2011. *Compare* Ex. G (9/26/2011 Presentation) at 27 (reflecting Q1 and Q2 2011 delinquency rates of 0.64% and 0.74% respectively), *with* Ex. F (Q4 2011 Quarterly Fin. Supp.) at 43 (reflecting Q3 and Q4 2011 delinquency rates of 0.84% and 0.81% respectively).

- In Q4 2011, although Genworth reported that the overall Australia delinquency rate for Q4 2011 decreased from Q3 2011 (from 0.59% to 0.55%), Genworth reported a year-over-year increase from the same quarter in the prior year (increasing from 0.48% in Q4 2010 to 0.55% in Q4 2011). Ex. F (Q4 2011 Quarterly Fin. Supp.) at 43. Similarly, although the Queensland delinquency rate in Q4 2011 had decreased from Q3 2011 (decreasing from 0.84% to 0.81%, respectively), the delinquency rate represented a significant increase from the Queensland delinquency rate reported in Q4 2010 (increasing from 0.56% to 0.81%). *Id.*

Plaintiffs plead *no facts* indicating any mismatch between these disclosures and Mr. Upton's comment that delinquency levels increased "[i]n the second half of 2011." Judge Buchwald dismissed a securities fraud claim for a similar failure in *City of Taylor General Employees Retirement System v. Magna International Inc.*, 967 F. Supp. 2d 771 (S.D.N.Y. 2013), reasoning that "the Court cannot decipher—and plaintiff has not adequately explained—how the purported 'details' Magna disclosed on August 5, 2011 were meaningfully different from the information the Company provided earlier in the putative class period." *Id.* at 793.

Plaintiffs also point to Mr. Upton's follow-on remark that "[i]n the second half of 2011, … we did observe lender processing delays" and that Genworth had begun "to work more closely with those lenders to improve the collection and default management techniques," which "did accelerate some of the older delinquencies coming through and as those came through in the first quarter, the claim paid counts did increase in January and February." SAC ¶ 117. As Plaintiffs acknowledge, however, Genworth disclosed in its September 2011 presentation that, as part of a risk management effort, it would work with lenders to "accelerate action on late stage delinquencies." SAC ¶ 7. Genworth later explained in a February 2, 2012, news release announcing Q4 2011 results that the company had increased reserves for "prior delinquencies

where lenders accelerated actions to move these loans through to claim." Ex. I (2/2/2012 News Release) at 9 (emphasis added). Genworth similarly explained in its FY 2011 Form 10-K filed on February 27, 2012, that the company had "increased reserves … *as lenders accelerated actions to transition delinquencies to claim*." Ex. C (FY 2011 Form 10-K) at 159 (emphasis added).

The complaint does not allege any specific material information about lenders' processing of claims (whether delays or acceleration efforts) that Defendants knew but failed to disclose, nor does the complaint explain how Mr. Upton's post-class period comments rendered any class period statement false when made. At bottom, Plaintiffs appear to assert that Genworth should have earlier and better predicted that lenders, as they worked through processing delays, would accelerate more and costlier delinquencies through to claim, which would increase the paid claim amounts and require higher reserves increases. But that is not the stuff of securities fraud. *See* Point I.B below.[6]

2. Plaintiffs' Assertions About Undisclosed "Increasing Claims" Do Not Demonstrate Falsity

Plaintiffs similarly fail to support their allegation that Defendants concealed "increasing claims" at Genworth Australia during the class period. As discussed above, Genworth disclosed "Total Paid Claims" and "Average Paid Claim" each quarter. *See* Ex. E (Q3 2011 Quarterly Fin. Supp.) at 41; Ex. F (Q4 2011 Quarterly Fin. Supp.) at 44. These disclosures showed total claim payments increasing by only $6 million between Q3 2011 ($25 million) and Q4 2011 ($31 million) (*id.*), before jumping by *$38 million* to $69 million in Q1 2012 (*see* Ex. L (5/2/2012 Presentation) at 9). These disclosures also showed the average claim payment increasing by only

[6] The only class period statement that Plaintiffs specifically allege was fraudulent based on Mr. Upton's post-class period comments about processing delays is Genworth's statement in its FY 2011 Form 10-K that "We have established processes, as well as contractual rights, to ensure we receive timely information from loan servicers to aid us in the establishment of our estimates." SAC ¶¶ 102, 103. Plaintiffs' argument is illogical. Even assuming *arguendo* that these delays were not previously disclosed, the fact that a process allegedly was ineffective does not establish that Genworth did not have "processes, as well as contractual rights," in place.

AU$2,200 between Q3 2011 (AU$62,400) and Q4 2011 (AU$64,600) (Ex. F (Q4 2011 Quarterly Fin. Supp.) at 44), before jumping by *AU$12,400* to *AU$77,000* in Q1 2012 (*see* Ex. L (5/2/2012 Presentation) at 9). These disclosed results are consistent with Mr. Upton's comment after the class period, in May 2012, that "it was—the March loss emergence and the average claims size[] that really gave rise to our deep dive on the delinquency inventory and the extensive review that we undertook to strengthen loss reserves of $82 million." SAC ¶ 117.

Notwithstanding these disclosures, Plaintiffs repeatedly assert that Defendants' statements were fraudulent because Defendants failed to disclose that Genworth Australia experienced an "increase in claims of $100-125 million" during the class period that "exceeded allotted reserves." *See* SAC ¶¶ 92, 95, 97, 100, 105, 107, 108. This is Plaintiffs' only articulation of the alleged "increasing claims." Plaintiffs' sole pleaded basis for this allegation is the assertions of CW1, who the complaint describes as a Genworth IT employee who left the company in April 2014 and whose job purportedly entailed assisting the local IT teams in Genworth's global mortgage insurance locations with operational needs, including "remotely downloading patches and supporting email systems." SAC ¶ 60. CW1 allegedly asserts the following about a December 2011 "Leadership and Management" meeting:

- "Schneider and Upton led quarterly domestic MI meetings called Leadership and Management ('L&M') meetings … [that] occurred during the beginning or middle … of the last month in each quarter before the Company publicly announced quarterly results" and that "40-50 MI employees" attended. SAC ¶ 62.
- While the IPO was "very important to Genworth and … the intent to having it occur in the first half of 2012 was a topic at each of these quarterly meetings, … this changed by the quarterly meeting that was held in either early or mid-December 2011." SAC ¶¶ 63-64.
- "[A]t this [December] meeting, either Schneider or Upton fielded the question as to whether the IPO was still planned for in the early part of 2012. The response was that the Australian MI unit had had a poor quarter due to increased claims, leading to miscalculating of reserves, and that claims were exceeding the allotted reserves." SAC ¶ 64.

- "[A] Powerpoint presentation in this meeting showing the increase in claims in Australia equaling around *$100-125 million*, and that this never had happened before to the Australian unit." SAC ¶ 65.

The Second Circuit imposes strict pleading requirements for CW allegations, reflecting skepticism of pleadings that rely on unnamed sources to meet their heavy pleading burden under the PSLRA and Rule 9(b). In *Novak v. Kasaks*, 216 F.3d 300 (2d Cir. 2000), the Second Circuit held that, "where plaintiffs rely on confidential personal sources," those CWs must "provide an adequate basis for believing that the defendants' statements were false." *Id.* at 314. Plaintiffs must describe CWs "with sufficient particularity to support the *probability* that a person in the position occupied by the source would possess the information alleged." *Mechel OAO*, 811 F. Supp. 2d at 880 (emphasis added) (citation omitted) (rejecting CW allegations where plaintiffs failed to plead facts "needed to substantiate the confidential witness's knowledge").

There is good reason for imposing these pleading safeguards. As Judge Posner observed writing for the Seventh Circuit in *City of Livonia Employees Retirement System v. Boeing Co.*, 711 F.3d 754 (7th Cir. 2013):

> [U]nnamed confidential sources of damaging information require a heavy discount. The sources may be ill-informed, may be acting from spite rather than knowledge, may be misrepresented, may even be nonexistent—a gimmick for obtaining discovery costly to the defendants and maybe forcing settlement or inducing more favorable settlement terms.

Id. at 759.

CW1's assertions should be rejected for a multitude of reasons.

Perhaps most critically, none of CW1's assertions about the December L&M meeting are corroborated by Plaintiffs' second confidential witness, CW2. The implications of that are significant. Plaintiffs allege that CW2 was the Chief Operating Officer ("COO") of Genworth Australia and was "in-charge of the day-to-day operations of the Australian MI unit … through early 2012" (SAC ¶ 67), *i.e.*, when the December 2011 L&M meeting allegedly occurred.

Plaintiffs allege that CW2 was personally "responsible for including the operational information for the Australian unit" in monthly reports to Genworth upper management (including Mr. Fraizer) that analyzed and discussed "financial information," "delinquencies," "reports claims [sic]," "where the Risk Team foresaw the trends or issues in the[] market," and "loss mitigation," as well as "identified 'trigger points' as part of the portfolio's risk analysis" (SAC ¶ 70)—*i.e.*, consistent with his role, CW2 received reports and participated in meetings discussing the details of Genworth Australia's mortgage insurance portfolio in extensive detail. In other words, even if CW2 did not attend the alleged December 2011 L&M meeting—and the complaint is silent on the point—it is simply not credible to suggest that the information conveyed at that meeting was not personally known to CW2 at least as of the time of alleged meeting, if not earlier. If Plaintiffs' allegations are assumed true, it automatically follows that CW2 saw whatever information would have supported CW1's assertions that "the Australian MI unit had had a poor quarter due to increased claims, leading to miscalculating of reserves, and that claims were exceeding the allotted reserves" (SAC ¶ 64) and that Genworth Australia had experienced an unprecedented "increase in claims in Australia equaling around *$100-125 million*" (SAC ¶ 65).

Strikingly, however, CW2 supports no part of CW1's recollection about the information supposedly conveyed at a December 2011 meeting and makes no claim that he heard or was aware of this blockbuster information about a fraud at any point. CW2 says nothing about a PowerPoint presentation, says nothing about a $100-125 million increase in claims (or undisclosed claim increases of any amount), and says nothing about insufficient loss reserves. CW2 does not even corroborate an L&M meeting having occurred in December (SAC ¶ 64), let alone one disclosing financials to "40-50 MI employees" "before the Company publicly announced quarterly results" for the quarter discussed at the meeting (SAC ¶ 62). Presumably

Plaintiffs' counsel or their investigators *asked* CW2 about these issues—the allure of a C-suite executive possibly confirming Plaintiffs' theory of fraud would have been too compelling to pass up. But CW2—who as COO is alleged to have intimate knowledge of Genworth Australia's operations and results—is tellingly silent on the critical factual allegations underlying Plaintiffs' claims.

By contrast, CW1, a former Genworth IT technician, has lots to say about these issues. And even setting aside the lack of corroboration from Genworth Australia's former COO, substantial bases exist for rejecting CW1's assertions.

To begin with, CW1 was an IT employee who supposedly reported to a vice president of "Technical Services," who reported to a chief information officer, who reported to senior management, who ultimately reported to Mr. Fraizer. SAC ¶ 60. In other words, the IT support person was a low-level non-executive two levels below the chief information officer. CW1 worked in Genworth's Raleigh, North Carolina location, and his responsibilities allegedly included designing and building Genworth's servers for the Company's global mortgage insurance locations and providing guidance to each location's local IT team, including Australia's, with operational needs such as "remotely downloading patches and supporting email systems." SAC ¶ 60.

CW1 asserts no connection to or involvement with Genworth Australia except for providing these remote IT services—remote services he provided to each of Genworth's many locations. But "remotely downloading patches and supporting email systems" from Genworth's Raleigh office did not provide CW1 with any exposure to Genworth Australia's business operations or results. Thus, addressing similarly situated CWs in *Steinberg v. Ericsson LM Telephone Co.*, 2008 WL 5170640 (S.D.N.Y. Dec. 10, 2008), the late Judge Patterson found it

"not plausible" that two CWs who worked in the defendants' North American office "would have direct knowledge about HSPA rollouts in the pipeline for the regions [outside of the United States], rather, it is likely that they would know only about HSPA contracts in the United States." *Id.* at *6.

Nor did CW1's employment provide him with any of the requisite expertise to understand or interpret Genworth Australia's operations and results. His job description has nothing to do with mortgage insurance, loss reserves, IPO planning, or any other area such as finance or accounting that would suggest that CW1 could or should understand the complexities of setting mortgage insurance reserves or the role that delinquencies and claims play in setting those reserves. *See Stein v. Tangoe, Inc.*, 2014 U.S. Dist. LEXIS 137966, at *46-47 (D. Conn. Sept. 30, 2014) ("[T]he Plaintiff has not provided any details showing that [the witness], who appears to be a technical engineer reporting to Tangoe's Chief Operating Officer ('COO'), has any financial expertise or was even involved in the preparation of the financial statements…. Therefore, at this stage, the Plaintiff is required to explain why or how [the witness] would have had the financial background or was privy to the finance department's methodology before his statements can be used to withstand a motion to dismiss. It has not done so.") (citing *Novak*, 216 F.3d at 314).[7] Thus, nothing in the complaint supports an inference, much less a "probability," that CW1 would have "possess[ed] the information alleged" about Genworth Australia's mortgage insurance business or reserving, or the ability to describe that information accurately to Plaintiffs' counsel. *See Mechel OAO*, 811 F. Supp. 2d at 880.

[7] CW1's limited understanding of the mortgage insurance business is evident in his assertion that Genworth, in "calculating risk and reserves," "would have factored" in the fact that the loans affected by the Queensland flooding "were predominantly secondary/vacation homes and not primary residences…. because they were properties that homeowners were more likely to walk away from if trouble occurred." SAC ¶ 65. This is not true: as Plaintiffs acknowledge, Australia "'ha[s] legal recourse laws that reduce the risk of borrowers walking away from their mortgages, while in the U.S. reports of borrowers leaving their keys and abandoning their homes have been rampant.'" SAC ¶ 5 (quoting an analyst report).

Moreover, CW1's assertions ask the Court to believe a nonsensical, fraudulent conspiracy running from Genworth's senior management right down to "director-like employees" (whatever that means) in the company's IT department. SAC ¶ 62. Specifically, CW1 asserts that Genworth management hosted a meeting of "40-50 MI employees" from various departments (SAC ¶ 62) and essentially told these people that the company had experienced an increase in claims of $100-125 million, an amount far exceeding what Genworth was reporting to investors and the Securities and Exchange Commission (SAC ¶ 65). These "40-50 MI employees" supposedly kept quiet, to absolutely no alleged benefit to themselves or the company, until CW1 confided Genworth's secret scheme to Plaintiffs' investigators nearly three years later, at some point before Plaintiffs filed their first amended complaint. Dkt. No. 26. Further confounding this conspiracy theory, CW1 asserts a specific "increase in claims in Australia equaling around $100-125 million," a single number plucked from one page of a PowerPoint allegedly presented during a meeting that took place in late 2011, which CW1 *alone* supposedly recalls with specificity three years later. SAC ¶ 65. This figure undermines CW1's assertions, as explained below. But more fundamentally, this case should not be permitted to proceed based on the facially improbable (if not absurd) notion that Genworth's senior management openly and notoriously presented, in a meeting of 40-50 employees (including IT support), not only material non-public information concerning an important multi-million dollar strategic transaction, but material non-public information that revealed an ongoing fraudulent scheme to misstate the company's financials and mislead the market about whether the IPO would proceed as planned. And this is particularly true when CW2, a member of the senior management team responsible for all day-to-day operations and with direct knowledge of Genworth Australia's financials and performance, is a confidential witness that offers no

corroboration for CW1's story.

Plaintiffs appear to allege one of two things, both illogical: either (i) Genworth experienced the $100-125 million increase in claim costs in 2011 and concealed these losses until Q1 2012 or (ii) the elevated losses reported for Q1 2012 were separate from the $100-125 million and never disclosed to this day. If the former, Plaintiffs allege no conceivable basis for why Genworth would simply (and fraudulently) push off an inevitable disclosure for one quarter. The supposed delay is not alleged to have benefitted anyone or served any purpose. The delay did not save the IPO, which was postponed before Genworth reported its Q1 2012 results. If the latter, Genworth is alleged to remain in violation of the federal securities laws, sitting on $100-125 million in concealed losses, which would make Plaintiffs' decision to end the class period in April 2012 rather peculiar. Indeed, the latter interpretation is fundamentally inconsistent with Plaintiffs' allegation that the "Truth" about the alleged fraud was "Revealed" on April 17, 2012. SAC at p. 42. Neither of these two possible interpretations makes any sense.

Thus, to summarize Plaintiffs' "increase in claims" allegation, (i) over an unspecified period in the second half of 2011, Genworth Australia experienced an undisclosed increase in claims, (ii) Genworth management disclosed this secret increase to 40-50 Genworth employees of varying seniority levels and job responsibilities, without any conceivable reason for involving these people in a conspiracy to commit fraud, (iii) everyone went along with the conspiracy and concealed this information either for a quarter or until the present day (the complaint is not clear), in either case having no conceivable reason for doing so, and (iv) these allegations come from a former Genworth computer technician, three years after the fact, and are not corroborated by Genworth Australia's COO, who also would have possessed the information alleged.

Given the fundamental implausibility of CW1's assertions, and the internal

inconsistencies with the assertions of CW2, CW1's story of fraud should not be credited. Indeed, even giving CW1 the benefit of the doubt that the meeting he recalls, in fact, occurred, the far more likely explanation is that CW1 is describing a meeting in 2012 where he heard about Genworth Australia's materially increased Q1 2012 losses and the impact on the IPO and is misremembering when that meeting occurred and what the $100-125 million represented. Indeed, *Q1 2012's* losses truly "never had happened before to the Australian unit" (SAC ¶ 65), as Plaintiffs allege elsewhere in the complaint. *See* SAC ¶ 24 (describing Q1 2012 results as "the first-ever reported loss by the Australian MI unit"). CW1's lack of relevant expertise and the amount of time that has elapsed since the alleged events further support the likelihood of a faulty recollection.[8]

In short, Plaintiffs' claims fail because (i) Genworth disclosed delinquency rates and claim amounts each quarter, and (ii) Plaintiffs do not plead adequate facts (much less the requisite particularized facts) supporting that Genworth Australia's delinquencies or claims were "increasing" by more than what Genworth disclosed. Cover to cover, the complaint does not allege when specifically or by what amount each of Genworth's reported financial metrics were false. Plaintiffs' challenge to Genworth Australia's reported financials thus fails to satisfy the pleading requirements of Rule 9(b) and the PSLRA that a complaint "stat[e] with particularity the circumstances constituting fraud." *ECA*, 553 F.3d at 196. Plaintiffs cannot simply assert conclusorily that delinquency and claim trends "rendered the Company's Class Period financials … false and misleading" (SAC ¶ 89) and that these same trends rendered Mr. Fraizer's qualitative assessment of Genworth Australia false (SAC ¶ 92). Plaintiffs "must demonstrate

[8] In the event that the Court denies Defendants' motion based on any CW allegations, Defendants respectfully request that the denial be without prejudice and with leave to refile after having the opportunity to depose Plaintiffs' CWs to "determin[e] whether the confidential witnesses acknowledge[] the statements attributed to them in the complaint." *Campo v. Sears Holdings Corp.*, 371 F. App'x 212, 216 n.4 (2d Cir. 2010).

with specificity why and how that is so." *Rombach v. Chang*, 355 F.3d 164, 174 (2d Cir. 2004).

For example, Plaintiffs allege that Genworth Australia had "grossly understated loss ratios," list the reported ratios, and point to "increasing" "claims" as the reason these ratios were false. SAC ¶ 89. But Plaintiffs do not allege what specifically the ratios should have been, much less why it was fraud not to report some unspecified different number. These critical deficiencies similarly plague Plaintiffs' challenge to the accuracy of Genworth Australia's "net loss[] and loss adjustment expense[]," "net income," and every other financial metric alleged to be misleading. SAC ¶ 89. Simply pointing to a number and calling it "grossly understated" does not suffice. *See C.D.T.S. v. UBS AG*, 2013 WL 6576031, at *4 (S.D.N.Y. Dec. 13, 2013) ("plaintiffs must do more than assert in a conclusory fashion that statements were or must have been false—they must allege facts supportive of how and why this is the case"; dismissing where "not a single one of the reports, filings, or subsequent statements" plaintiffs pointed to was "directly tied to any particular alleged misstatements""); *Pollio v. MF Global, Ltd.*, 608 F. Supp. 2d 564, 570 (S.D.N.Y. 2009) (rejecting "conclusory" allegations that statements "were misleading because they failed to disclose that MF Global's business was 'weaker than represented' and that the Company had insufficient capital" because such allegations "fall[] woefully short of satisfying the PSLRA's requirement that plaintiff identify the reasons why each allegedly actionable statement is misleading.").[9]

B. Plaintiffs Fail to Plead that Defendants' Reported Loss Reserves Were False

Plaintiffs also challenge as false Genworth's reported loss reserves for Genworth Australia's mortgage insurance policies. Specifically, Plaintiffs allege that Defendants "did not provide an adequate estimate for the Company's loss reserves during the Class Period" because

Defendants "failed to consider" certain "negative factors impacting the Australian MI unit's loss reserves," namely, (i) "a significant increase of $100-125 million in claims during the Class Period," which "exceed[ed] the allotted reserves," and (ii) "increasing delinquencies in the second half of 2011," both arising from the effect of a weak Australian economy on Genworth's insuring of mortgage loans to small-business and self-employed borrowers in 2007 and 2008. SAC ¶¶ 81, 82. No pleaded facts support this claim or set forth when and by how much Genworth's reserve increases were insufficient, much less explain how Genworth's reserve estimates were not only wrong, but fraudulent.

To begin with, as the Second Circuit held in *Fait v. Regions Financial Corp.*, 655 F.3d 105 (2d Cir. 2011), loss reserves are "not a matter of objective fact," but rather "reflect management's opinion or judgment about what, if any, portion of amounts due on the loans ultimately might not be collectible." *Id.* at 113. "Such a determination is inherently subjective, and like goodwill, estimates will vary depending on a variety of predictable and unpredictable circumstances." *Id*.

Under the Supreme Court's recent decision in *Omnicare Inc. v. Laborers District Council Construction Industry Pension Fund*, 135 S. Ct. 1318 (2015), an opinion may be actionable if (i) the speaker does not genuinely believe it (*id.* at 1326) or (ii) the speaker omits material facts about the basis of the opinion (*id.* at 1332). Plaintiffs meet neither of these tests.

With respect to Defendants' subjective belief about Genworth Australia's reserves, the complaint is devoid even of conclusory allegations that Defendants did not genuinely believe that the reported reserves represented a best estimate of the cost of claims. The closest Plaintiffs come to alleging what Defendants actually knew and believed are the allegations from CW1

[9] Because Plaintiffs fail to plead that Genworth Australia's financials were falsely reported, Plaintiffs' allegation that Messrs. Fraizer and Klein fraudulently certified the accuracy of Genworth's financial reporting under the Sarbanes-

regarding a December meeting, which the Court should reject for the reasons explained in Point I.A.2 above. And, as discussed in Point IV below, there is nothing in the complaint linking Messrs. Fraizer and Klein to the information allegedly held by CW1. Plaintiffs' remaining allegations "'provide[] absolutely no reasonable basis for concluding that defendants did not think [the] reserves were [previously] adequate.'" *NECA-IBEW Pension Trust Fund v. Bank of Am. Corp.*, 2012 WL 3191860, at *10-12 (S.D.N.Y. Feb. 9, 2012) (Pitman, Mag. J.) (quoting *In re CIT Grp., Inc. Sec. Litig.*, 349 F. Supp. 2d 685, 690-91 (S.D.N.Y. 2004)).

Plaintiffs do not plead that Defendants omitted material facts concerning the basis for their opinions about loss reserves adequacy, under the second prong of *Omnicare*. Rather, Plaintiffs merely recycle their arguments that Genworth Australia experienced increasing claims and delinquencies during the class period (SAC ¶ 81), and conclude that, "[g]iven Defendants' awareness of these negative factors, Defendants should have recorded a significant portion (if not the entirety) of the $82 million reserve charge announced at the end of the Class Period in 3Q 11 and 4Q 11" (SAC ¶ 82). As explained in Point I.A above, Plaintiffs' allegations concerning increased claims and delinquencies are conclusory and meritless. To plead the inadequacy of reserves, Plaintiffs must "allege at what point in time a[] … charge should have been taken and which specific losses known to the [c]ompany should have triggered a[] … charge." *City of Sterling Heights Police & Fire Ret. Sys. v. Vodafone Grp. PLC*, 655 F. Supp. 2d 262, 269-70 (S.D.N.Y. 2009).

The complaint contains none of the required particularity. Instead, Plaintiffs simply substitute their own opinion for Defendants' and assert that claim and delinquency trends "should have" led Genworth to reserve more, earlier. SAC ¶¶ 82, 84. This is not enough. The

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Oxley Act of 2002 (SAC ¶ 90) should also be rejected.

Second Circuit rejected assertions of this nature in *City of Omaha, Nebraska Civilian Employees' Retirement System v. CBS Corp.*, 679 F.3d 64 (2d Cir. 2012), explaining that, while "Plaintiffs' allegations regarding the downward trajectory of CBS's overall market capitalization, declining advertising revenues for some CBS reporting units, … and CBS's own anticipation of an economic slowdown may suggest that CBS expressed overly optimistic views regarding its overall business outlook…. these allegations, even viewed in combination, do not plausibly demonstrate" that defendants committed securities fraud by misreporting the company's financials. *Id.* at 68. Similarly, in *In re Wachovia Equity Securities Litigation*, 753 F. Supp. 2d 326 (S.D.N.Y. 2011), Judge Sullivan rejected "generalized allegations" that "Wachovia was well aware of, or recklessly indifferent to, the fact that their loan reserves were significantly understated in light of the deteriorating real estate market" and that "Defendants could not have reasonably concluded that loan loss reserves were set at adequate levels," because those allegations "fail[ed] to specify what caused the Defendants to know that the loan loss reserves were insufficient." *Id.* at 361-62. Along these lines, many other decisions in the Second Circuit and this District have rejected such challenges to reserves adequacy:

- *In re Fannie Mae 2008 Sec. Litig.*, 525 F. App'x 16, 18-19 (2d Cir. 2013) (dismissing allegations that Fannie Mae should have "set aside these loss reserves earlier" as "a classic example of pleading fraud by hindsight," finding that although "greater clairvoyance" might have led Fannie Mae to act sooner, "failure to make such perceptions does not constitute fraud") (citation omitted);

- *Okla. Firefighters Pension & Ret. Sys. v. Student Loan Corp.*, 951 F. Supp. 2d 479, 497-98 (S.D.N.Y. 2013) (finding that "a complaint must allege more than the mere existence of contradictory information to support a securities fraud claim" (citing *CBS*, 679 F.3d at 68) and dismissing "conclusory allegations … that defendants could not possibly have believed their own estimates [of reserves], since plaintiffs interpret those estimates to have proven inadequate");

- *NECA-IBEW*, 2012 WL 3191860, at *10-12 ("[T]he mere fact that BAC's predicted loss reserves turned out to be insufficient some time after they were made does not render those figures false at the time that they were publicly filed

with the SEC."), *cited in Student Loan Corp.*, 951 F. Supp. 2d at 498 and *In re Fannie Mae 2008 Sec. Litig.*, 525 F. App'x at 19;

- *CIT*, 349 F. Supp. 2d at 689-91 (dismissing complaint because "plaintiffs' claim that loan loss reserves were inadequate is nothing more than an assertion that CIT was incorrect or unskillful in determining exactly what amount of reserves would be adequate").

Plaintiffs' allegations that Genworth Australia's reserves were fraudulently understated should similarly be rejected.[10]

C. Plaintiffs Fail to Plead that Defendants' Statements Concerning the Planned Australia IPO Were False

Plaintiffs allege that the following statements concerning Defendants' plans for a minority IPO of Genworth Australia were fraudulent:

- Mr. Fraizer's statements on the February 3, 2012 Q4 2011 earnings call that "we continue to move forward with our planned minority interest IPO of up to 40% of Australia Mortgage Insurance," "[w]e still anticipate second-quarter 2012 execution," "[w]e have not encountered any regulatory or market conditions that would change that timing," and "the minority IPO of Australia that is moving down the track right in accordance with our plans." SAC ¶ 97.

- Mr. Klein's statements on a call later that same day that "our [IPO] plans remain on track" and that "our expected timing would be some time in the second quarter [of 2012]." SAC ¶ 104.

- Mr. Klein's statements at a March 29, 2012 investor conference that "[w]hat we wanted to do all along is do this transaction [the IPO] from a position of strength," that "[w]e're working very actively to put ourselves in a position to execute this in the second quarter, as we've said," and that "we're working really hard to put ourselves in a position to do the transaction in the second quarter." SAC ¶ 106.

Plaintiffs allege that these statements "were false and misleading because Fraizer failed to disclose that deteriorating economic conditions in Queensland had led to a significant increase in claims and delinquencies during the Class Period, including on low documentation loans issued

[10] Plaintiffs also allege that Mr. Klein's "statements regarding Genworth's risk management procedures, specifically stress testing 'in terms of home price depreciation… and unemployment,' and that the Company 'look[s] at the impact on delinquencies and on cure rates' were false and misleading" because Genworth Australia was experiencing increasing claims and delinquencies. SAC ¶ 107. Even accepting these alleged trends as true, they do nothing to establish that Genworth did not perform stress testing.

to small business and self-employed borrowers in 2007 and 2008, that exceeded allotted reserves—information that would, if disclosed, delay the IPO." SAC ¶ 97; *see also* SAC ¶¶ 105, 106. This allegation fails for the reasons stated in Point I.A above.[11]

Indeed, tellingly, CW2 (the COO) corroborates that, in fact, Genworth Australia employees were doing "a lot of analysis" "for the investment banks that were preparing for the IPO," and "analyzed many of the internal metrics including monthly default figures and everything that went into calculating the [Australia] unit's overall income" in connection with that effort. SAC ¶ 73. CW2 nowhere asserts that Defendants changed their plans for the IPO. *See* SAC ¶¶ 67-73. Nor does he assert based on this information and analysis that Genworth senior management knew the IPO could not or would not happen, suspected that the IPO might not happen, or that the targeted Q2 2012 execution date was in jeopardy.

As for CW1 (the computer technician), he admits that "the Australian IPO was important to Genworth" and that "having it occur in the first half of 2012 was a topic at each of the[] quarterly [L&M] meetings." SAC ¶ 63. CW1 asserts that "this changed" (without specifically explaining what, exactly, had changed) by the alleged December 2011 L&M meeting. SAC ¶ 64. CW1 purports to recall management fielding a direct and, for purposes of Plaintiffs' complaint, extremely pertinent question about the timing of the IPO: "either Schneider or Upton fielded the question as to whether the IPO was still planned for in the early part of 2012." SAC ¶ 64. But the response from management that CW1 recalls is a vague non sequitur: "[T]he Australian MI unit

[11] Plaintiffs also challenge as false Defendants' statements that the Australian housing market was "stable" or "solid." SAC ¶¶ 91, 96, 104, 106. Plaintiffs allege that these statements were false because of increasing delinquency rates and claims at Genworth Australia. SAC ¶¶ 92, 97, 105, 108. These allegations have no merit. Whatever the state of the Australian housing market was, it was obviously public information, and so Defendants' qualitative characterizations of that market could not have misled investors. *See In re GeoPharma, Inc. Sec. Litig.*, 399 F. Supp. 2d 432, 452-53 (S.D.N.Y. 2005) ("Cases in this Circuit assume that the contradictory information in question must be non-public."); *see also Jones*, 550 F. App'x at 26 (a plaintiff alleging securities fraud cannot merely contend that "defendants arguably took a more optimistic view of [the company's] prospects" than others "viewing the same publicly available information" might have taken).

… had a poor quarter due to increased claims, leading to miscalculating of reserves, and that claims were exceeding the allotted reserves." SAC ¶ 64. Setting aside the myriad concerns with CW1's assertions about the December meeting (*see* Point I.A.2 above), the alleged management response does not support the conclusion that management had changed its plans for the IPO but needlessly concealed that delay for a random four-month period.

Plaintiffs also do not allege that Defendants were not actually "working very actively" or "working really hard" to execute the IPO in Q2 2012, and in fact, their CW2 COO allegedly corroborates that work and analysis was being conducted internally in that regard. SAC ¶ 106; SAC ¶ 73. Plaintiffs' challenge to these statements thus fails. *See In re Sanofi-Aventis Sec. Litig.*, 774 F. Supp. 2d 549, 566 (S.D.N.Y. 2011) (dismissing claim because "Plaintiffs never allege[d] any facts that would demonstrate that, at the time the statement was made, Defendants were either not planning for a launch in the second half of 2006 or not planning to continue such efforts in the future" or "any facts that would demonstrate that a reasonable investor could have understood this statement to convey a guarantee about the timing or success of the … launch") (citing *Rombach*, 355 F.3d at 174); *City of Roseville Emps.' Ret. Sys. v. Nokia Corp.*, 2011 WL 7158548, at *9 (S.D.N.Y. Sept. 6, 2011) (dismissing challenges to defendants' statements concerning planned product release schedule where "factual allegations [were] insufficient to conclude that, at the time various statements were made about release dates, Nokia had no reasonable basis to believe that it could meet those deadlines even in light of the alleged software problems, or that Nokia had no intention of meeting the announced release dates").

Plaintiffs also challenge Defendants' opinions that the IPO could be achieved by Q2 2012 and that the IPO was "on track" for Q2 2012 execution. SAC ¶ 104. These are clearly statements of opinion. *See Faulkner v. Verizon Commc'ns, Inc.*, 156 F. Supp. 2d 384, 389, 395, 397-400

(S.D.N.Y. 2001) (statements that merger was "on schedule" and "on track" "were not actionable because they were mere predictions or statements of opinion"); *Elliott Assocs., L.P. v. Covance, Inc.*, 2000 WL 1752848, at *9 (S.D.N.Y. Nov. 28, 2000) ("Given the usual level of uncertainty as to whether any proposed merger will actually be completed, these statements [regarding the expected completion of the merger] could not possibly be understood as anything but opinions."). But Plaintiffs offer no explanation, other than their unsupported conclusions about increasing delinquencies and claims, as to *why* the IPO was not objectively achievable by Q2 2012, or when Defendants should have known this.

Finally, Plaintiffs' claim that "Defendants systematically misled the market into believing … that there were no market conditions that would delay the IPO" (SAC ¶ 19) such that "investors had no reason to suspect that the Australian MI unit—and the planned Australian IPO—was subject to any sudden destabilization" (SAC ¶ 13) can be summarily rejected. As discussed below, Genworth expressly warned investors that "[a]dverse market or other conditions might delay or impede the planned IPO of our mortgage insurance business in Australia" and "there can be no assurance that this transaction can be executed within the targeted timeframe or on the desired terms." Ex. B (Q3 2011 Form 10-Q) at 148 (emphasis added). *See also* Ex. C (FY 2011 Form 10-K) at 85 (repeating these same warnings); Point III, *supra*.

Plaintiffs' contention that Defendants made false statements about the IPO accordingly should be rejected.

II. PLAINTIFFS FAIL TO PLEAD SCIENTER

Plaintiffs also fail to plead scienter—a mental state embracing an "intent to deceive, manipulate, or defraud." *ECA*, 553 F.3d at 198 (citation and internal quotation marks omitted). To survive dismissal, a complaint must "state with particularity facts giving rise to a strong

inference" of scienter for each defendant. 15 U.S.C. §§ 78u–4(b)(2) & (b)(3)(A). A plaintiff can plead the requisite strong inference of scienter by alleging with particularity facts showing either (i) "that defendants had the motive and opportunity to commit fraud" or (ii) "strong circumstantial evidence of conscious misbehavior or recklessness." *ECA*, 553 F.3d at 198; *see also Kalnit v. Eichler*, 264 F.3d 131, 138 (2d Cir. 2001) (same). To qualify as "strong," the inference of scienter must be "more than merely plausible or reasonable—it must be cogent and at least as compelling as any opposing inference of nonfraudulent intent." *Tellabs*, 551 U.S. at 314. "An inference of fraudulent intent may be plausible, yet less cogent than other, nonculpable explanations for the defendant's conduct." *Id.* at 314. "Therefore, the court 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?'" *ECA*, 553 F.3d at 198 (quoting *Tellabs*, 551 U.S. at 326).

The third time is not the charm for Plaintiffs, whose second amended complaint still fails to articulate *any* theory of scienter, much less a compelling or even logical one under *Tellabs*. Nowhere do Plaintiffs explain *why* Defendants would promote the IPO as a boon to Genworth's capital plan despite allegedly knowing that the transaction was not achievable within the targeted timeframe (and that Genworth's stock price might drop when the company postponed the IPO). Nor do Plaintiffs explain *why* Defendants would lie about the adequacy of the company's loss reserves, despite allegedly knowing that economic circumstances in Australia would require a significant strengthening of reserves. Plaintiffs do not explain *why*, every quarter, Defendants would disclose delinquency rates not only for Genworth Australia as a whole, but also for the Queensland region and for each policy year, and take meaningful reserve charges consistent with the results disclosed, but conceal the purported need to strengthen reserves even more. Indeed, to

accept Plaintiffs' fraud claim, one must believe that, after Defendants saw increasing delinquencies and claims in Genworth Australia, for two quarters they not only systematically falsified that unit's relevant performance metrics, but casually informed 40-50 employees that they were doing so, all instead of simply adjusting reserves as soon as these supposed trends emerged, as Genworth ultimately did anyway in Q1 2012.

Plaintiffs' failure to bridge these logical chasms (even with multiple pleading attempts) warrants dismissal under *Tellabs*, as courts repeatedly have rejected illogical or nonsensical securities fraud claims.[12]

The far more compelling inference is that, as Genworth publicly disclosed, the company was fully committed to executing an IPO in Q2 2012, believed it was important, and believed it was on track during the class period, as the Genworth Australia loss ratios disclosed in Q3 and Q4 2011 were in line with publicly disclosed expectations. *Compare* SAC ¶ 7 (citing a September 2011 Genworth presentation projecting loss ratios for Australia in the second half of 2011 in the "High 40's/Low 50's"), *with* Ex. E (Q3 2011 Quarterly Fin. Supp.) at 37; Ex. F (Q4 2011 Quarterly Fin. Supp.) at 40 (showing disclosed Q3 and Q4 2011 loss ratios of 48% and 46%, respectively). Then, in March 2012, Genworth experienced unexpected losses that caused the postponement of the IPO and a strengthening of reserves. This theory, unlike Plaintiffs', is cogent and consistent with Defendants' public disclosures.

Apart from the illogic of Plaintiffs' theory of fraud, Plaintiffs fail to plead (i) "that

[12] *See Local No. 38 IBEW Pension Fund v. Am. Express Co.*, 724 F. Supp. 2d 447, 462-63 (S.D.N.Y. 2010) (finding no "strong inference of scienter" where "common sense caution[ed] against" such an inference), *aff'd*, 430 F. App'x 63 (2d Cir. 2011); *In re PXRE Grp., Ltd., Sec. Litig.*, 600 F. Supp. 2d 510, 533 (S.D.N.Y. 2009) (rejecting theory of fraud in part because of the "seeming futility of Defendants' alleged scheme"), *aff'd sub nom. Condra v. PXRE Grp. Ltd.*, 357 F. App'x 393 (2d Cir. 2009); *Fadem v. Ford Motor Co.*, 352 F. Supp. 2d 501, 525 (S.D.N.Y. 2005) (rejecting scienter theory that "defie[d] economic reason," was "a recipe for economic disaster" and was "inconsistent with hopes for or expectations of increased bonuses") (citation omitted), *aff'd*, 157 F. App'x 398 (2d Cir. 2005).

defendants had the motive and opportunity to commit fraud" or (ii) "strong circumstantial evidence of conscious misbehavior or recklessness." *ECA*, 553 F.3d at 198.

A. Plaintiffs Fail to Plead Any Discernible Motive for the Alleged Fraud

In order to raise a strong inference of scienter based on "motive and opportunity" to defraud, Plaintiffs must allege that Defendants "benefitted in a concrete and personal way from the purported fraud." *Novak*, 216 F.3d at 311. Plaintiffs do not allege a single motive Defendants had to commit fraud. Plaintiffs do not allege (nor could they) that Defendants personally benefited in any way from the alleged fraud, whether through sales of Genworth stock or other means. *See In re Sec. Capital Assurance, Ltd. Sec. Litig.*, 729 F. Supp. 2d 569, 594 (S.D.N.Y. 2010) ("That Defendants … did not sell their stock prior to a price drop 'suggest[s] the absence of any nefarious motives."') (citation omitted).

B. Plaintiffs Fail to Plead Conscious Misbehavior or Recklessness

Because Plaintiffs "fail[] to demonstrate that defendants had a motive to defraud … [they] must produce a *stronger* inference" of conscious misbehavior or recklessness. *Kalnit*, 264 F.3d at 143 (emphasis added); *see also ECA*, 553 F.3d at 199 ("the strength of the circumstantial allegations must be correspondingly greater if there is no motive") (citation and internal quotation marks omitted). To plead conscious misbehavior, Plaintiffs must allege that Defendants engaged in "deliberate illegal behavior." *Novak*, 216 F.3d at 308. The bar for recklessness is equally high: it requires a state of mind "approximating actual intent" and not "merely a heightened form of negligence." *S. Cherry St. LLC v. Hennessee Grp. LLC*, 573 F.3d 98, 109 (2d Cir. 2009) (quoting *Novak*, 216 F.3d at 312). Specifically, Plaintiffs must allege particularized facts showing that Defendants' conduct was "an extreme departure from the standards of ordinary care … to the extent that the danger was either known to the defendant or so obvious that the defendant must have been aware of it." *ECA*, 553 F.3d at 198 (quoting

Novak, 216 F.3d at 308).

So far as can be inferred from their complaint,[13] Plaintiffs attempt to plead scienter by alleging that Defendants possessed non-public information that contradicted their public statements. Plaintiffs base these allegations on the supposed assertions of two CWs. Well-settled Second Circuit precedent requires that where, as here, plaintiffs contend defendants "knew facts or had access to information suggesting that their public statements were not accurate," for each and every challenged statement plaintiffs must specifically identify, and plead particularized facts regarding, the source and content of contradictory information available to the speaker when each statement was made. *Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital Inc.*, 531 F.3d 190, 196 (2d Cir. 2008) (quoting *Novak*, 216 F.3d at 309, 311). The conclusory allegations of Plaintiffs' two CWs fall well short of these pleading requirements.

For the reasons discussed above (in Point I.A.2), CW1's allegations should not be credited because CW1, a low-level information technology employee, was not in a position to have comprehended the financial information he claims to have gleaned from the L&M meeting he purports to describe (replete with discrepancies and ambiguities that render it fundamentally unreliable). CW1's remaining allegations add nothing to Plaintiffs' scienter theory. Even if CW1's allegation that Messrs. Fraizer and Schneider traveled frequently to Australia (SAC ¶ 61) is credited, Plaintiffs fail to allege what information, much less contradictory information, was learned on these trips. *See City of Brockton Ret. Sys. v. Avon Prods., Inc.*, 2014 WL 4832321, at *20 (S.D.N.Y. Sept. 29, 2014) (rejecting allegations that the individual defendant was aware of bribery because he "traveled to China several times for meetings with Avon executives" because plaintiffs did "not allege[] facts demonstrating that these meetings would have made [individual

defendant] aware [of contradictory information]").

CW2's allegations are even more deficient. SAC ¶ 67. Unlike CW1, CW2's supposed assertions are devoid of alleged facts (even confounding ones, like those alleged by CW1) that even arguably contradict Defendants' public statements. CW2 allegedly asserts:

- "[T]hroughout 2011, there were internal reports showing an increase in delinquencies in Australia." SAC ¶ 68.
- "[T]he monthly reporting package given to Corporate was reviewed by Upton and Genworth's Chief MI Risk Officer…. [T]he package included Australian financials, loss mitigation, risk evaluation of the trending market, and identified 'trigger points' as part of the portfolio's risk analysis." The package consisted of "two reports bundled into one: (1) a consolidated financial report of all the international business, with the individual financials for each international unit including Australia, that 'encapsulated' high level financial information including income, estimates going forward and an operational take; and (2) the risk report, assembled by the 'Risk Team,' that reported both delinquencies and where the Risk Team foresaw the trends or issues in their market." SAC ¶ 70.
- There was "a monthly international call, in which [CW2] participated, that Fraizer would 'get on' to at a minimum on a quarterly basis…. [T]he monthly call would take place on the second Thursday night of the month (Friday morning in Australia). The calls were led by Upton…. Klein also participated in these calls, providing an update on the Company's finances based on information from meeting with the finance team prior to the monthly call." SAC ¶ 72.
- "[W]hen [CW2] participated in the calls with Upton and [Genworth's chief risk officer], default rates in Australia were definitely discussed. On the calls that Fraizer participated in, [there were] … discussions regarding 'what's driving the conditions in the marketplace' and the forecasts." SAC ¶ 72.

See also SAC ¶¶ 68-72 (additional descriptions about reporting processes).

Plaintiffs' lengthy recitation of CW2's assertions amounts to one unremarkable conclusion that could be drawn—without the insight of a "confidential witness"—about any publicly reporting company in America: Genworth had a process for upward-reporting financial

[13] Plaintiff's first amended complaint contained a section labeled "Additional Scienter Allegations." *See* Dkt. No. 26, ¶¶ 105-18. Plaintiffs' second amended complaint does not specify which of its 157 paragraphs of allegations supposedly demonstrate scienter.

information.[14] The *only* content that is allegedly contained in these reports—"throughout 2011, there were internal reports showing an increase in delinquencies in Australia" (SAC ¶ 68)—is entirely consistent with Genworth's public disclosures cited in the complaint. *See* SAC ¶¶ 12, 51, 99 ("During the fourth quarter of 2011, total delinquencies decreased but remained above 2010 levels …."). Similarly, CW2's allegation that "there was 'certainly evidence' that the economic conditions in Australia were deteriorating prior to the IPO" (SAC ¶ 72) seemingly references publicly available information about the Australian economy, wholly untethered to Genworth. Further, Plaintiffs fail to allege what that "evidence" was, how the "evidence" relates to Genworth Australia's performance in any way, or why the unspecified "evidence" contradicted Defendants' statements or differed in any way from Genworth's public disclosures. These conclusory allegations should be rejected. *See Jones*, 550 F. App'x at 28 (allegation that "defendants had access to reports showing that consumer inkjet sales were missing internal forecasts … absent any pleading indicating a divergence from publicly disclosed information … fails the specificity requirements of the PSLRA and Rule 9(b)").

In short, none of Plaintiffs' allegations about Genworth's reporting system "establish[es] what specific contradictory information the Individual Defendants received or when they received it." *Local No. 38*, 724 F. Supp. 2d at 461 (collecting cases); *see also Glaser v. The9, Ltd.*, 772 F. Supp. 2d 573, 591 (S.D.N.Y. 2011) ("[A]s with all allegations going to scienter, confidential source allegations must show that individual defendants actually possessed the knowledge highlighting the falsity of public statements; conclusory statements that defendants 'were aware' of certain information, and mere allegations that defendants 'would have' or

[14] CW1's vague chain of reporting allegations (*see* SAC ¶ 66) similarly add nothing. The unremarkable fact that Genworth had a process for the upward reporting of financial information does nothing to "establish what specific contradictory information the Individual Defendants received or when they received it." *See Local No. 38*, 724 F. Supp. 2d at 461 (dismissing complaint for this pleading failure).

'should have' had such knowledge is insufficient.") (collecting cases).

Finally, as discussed above, what CW2 does not assert is perhaps most telling. CW2, based on his position as COO of Genworth Australia and the very reporting processes he describes, actually sat in a position in which he not only would have been fully aware of Genworth Australia's performance results, but would have possessed the expertise to describe this information cogently to Plaintiffs' investigators (two counts on which CW1, who provides Plaintiffs' most crucial allegations, fails). But CW2 does not identify a single fact that even generally—let alone specifically and with particularity—contradicts Genworth's public disclosures.

III. THE PSLRA'S SAFE HARBOR PROTECTS GENWORTH'S FORWARD-LOOKING STATEMENTS CONCERNING THE IPO

The PSLRA defines forward-looking statements "as those which speak predictively about the future" (*Gissin v. Endres*, 739 F. Supp. 2d 488, 505 (S.D.N.Y. 2010)), including statements about "plans and objectives of management for future operations." 15 U.S.C. § 78u-5(i)(1). In the SAC, Plaintiffs challenge the following five statements about the IPO that Defendants made during two investor calls in February 2012 (in connection with announcing 4Q 2011 results):

- "We still anticipate second-quarter 2012 execution." SAC ¶ 96.
- "[T]he minority IPO of Australia … is moving down the track right in accordance with our plans …." SAC ¶ 96.
- "[O]ur plans [to complete the IPO] remain on track." SAC ¶ 104.
- "[O]ur expected timing [for the IPO] would be some time in the second quarter [of 2012] …." SAC ¶ 104.
- "[W]e're working really hard to put ourselves in a position to do the transaction in the second quarter." SAC ¶ 106.

Each of these statements is inherently "forward-looking, as it clearly identifies future intentions and includes language signaling a forward-looking statement." *See In re Molycorp, Inc. Sec.*

Litigation, 2015 WL 1097355, at *14 (S.D.N.Y. Mar. 12, 2015) (statement that "[w]e also believe that we're on the path for market acceptance of XSORBX into drinking water purification markets" is "forward-looking"); *Gissin*, 739 F. Supp. 2d at 505-06, 507 n.106 (finding that the statement, "'[b]ased on our *current* expectation of cash flows from operations … we feel we will be in a position to fund those capital investments for the year,'" "'say[s] only that, whatever that situation is, it makes the future projection attainable,'" which is an "'assertion [that] is necessarily implicit in every future projection'"). Indeed, the challenged forward-looking statements about the IPO reflect a current belief about a "plan[] and objective[] of management for future operations," and thus are squarely within the ambit of PSLRA safe harbor protection. 15 U.S.C. § 78u-5(i)(1).[15]

As such, the IPO-related statements cannot form the basis for a securities fraud claim if they are either "identified and accompanied by meaningful cautionary language *or* [are] immaterial *or* the plaintiff fails to prove that [the statement] was made with actual knowledge that it was false or misleading." *Slayton v. Am. Express Co.*, 604 F.3d 758, 766 (2d Cir. 2010) (emphasis in original); *see also In re Sanofi Sec. Litig.*, 2015 WL 365702, at *14 (S.D.N.Y. Jan. 28, 2015) ("Because the statute is written in the disjunctive, statements are protected by the safe harbor if they satisfy any one of these three categories" and dismissing under the "independent" cautionary language prong). Genworth's statements about the IPO are protected under the "meaningful cautionary language" prong and, independently, the "no actual knowledge" prong.

[15] Plaintiffs may argue that Defendants' statements about their IPO plans are not protected by the safe harbor because they are "mixed" present and forward-looking statements. For this argument Plaintiffs may rely on a recent decision by the Eastern District of Virginia, *In re Genworth Financial Inc. Securities Litigation*, 2015 WL 2061989 (E.D. Va. May 1, 2015), which declined to apply the safe harbor to the Genworth defendants' statements about the company's long-term care insurance reserves, holding that "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." *Id.* at *25 (citation omitted). While Defendants respectfully disagree with the Virginia district court's ruling, its analysis of statements about loss reserve adequacy in any event does not apply to the statements here regarding IPO plans, which are clearly forward-looking under 15 U.S.C. § 78u5(i)(1) and the Southern District of New York precedent cited above.

First, Genworth accompanied these forward-looking statements about the IPO with "meaningful cautionary language." *Slayton*, 604 F.3d at 766. The PSLRA defines language as "meaningfully cautionary" where it "identif[ies] important factors that could cause actual results to differ materially from those in the forward-looking statement." 15 U.S.C. § 78u–5(c). "To avail themselves of safe harbor protection under the meaningful cautionary language prong, defendants must demonstrate that their cautionary language was not boilerplate and conveyed substantive information." *Slayton*, 604 F.3d at 772. A company, however, "need not include the particular factor that ultimately causes its projection not to come true in order to be protected." *In re WEBMD Health Corp. Sec. Litig.*, 2013 WL 64511, at *8 (S.D.N.Y. Jan. 2, 2013) (quoting *Slayton,* 604 F.3d at 770 & n.5 (citing H.R. Rep. No. 104–369, at 44 (1995) (Conf. Rep.))).

Before and during the alleged class period, Genworth disclosed risks specific to the IPO. Genworth warned at every opportunity—in SEC filings, news releases, and earnings calls[16]—that the IPO was "subject to market conditions" and that "[a]dverse market or other conditions might delay or impede the planned IPO." *See* Facts Section C above. Indeed, as Plaintiffs acknowledge and allege in their complaint, Mr. Klein expressly cautioned during the class period that: "like any IPO there's a number of factors that impact timing …. One is obviously market conditions and the impact that has on valuation considerations. So it's not just looking at the equity markets, it's looking at the impact also in the Australian housing market and things of that nature." SAC ¶ 106.

Moreover, to the extent Plaintiffs allege that delinquencies and losses resulted in postponement of the IPO (SAC ¶ 108 (Defendants failed to disclose that the "spike in delinquencies and claims in excess of reserves would force the IPO to be delayed"); *see also*

SAC ¶¶ 97, 105), Genworth also specifically cautioned that adverse macro-economic conditions could result in higher delinquencies, defaults, and losses, and could adversely impact Genworth Australia's results. For instance, Genworth disclosed in its FY 2010 Form 10-K filed on February 25, 2011, that factors impacting "borrowers' ability to pay their mortgage," such as "rising unemployment rates" or a "deterioration in economic conditions internationally," could increase Genworth's risk of loss, as could a "decline in home prices" and, in particular, "economic downturns or reversals of recent significant home price appreciation in areas where a large portion of [Genworth's] business is concentrated." Ex. D (FY 2010 Form 10-K) at 67; *see also* Ex. B (Q3 2011 Form 10-Q) at 146 (incorporating these risk disclosures by reference). Genworth further disclosed in the same document that "natural disasters, including … floods," could "trigger an economic downturn in the areas directly or indirectly affected by the disaster … [and] result in a decline in business and increased claims from those areas, as well as an adverse effect on home prices in those areas, which could result in increased loss experience in our mortgage insurance businesses." Ex. D (FY 2010 Form 10-K) at 61; *see also* Ex. B (Q3 2011 Form 10-Q) at 146 (incorporating these risk disclosures by reference).

Each of these cautionary statements clearly "identif[ied] 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); *see also In re Sanofi Sec. Litig.*, 2015 WL 365702, at *21 (S.D.N.Y. Jan. 28, 2015) (language is "meaningful[ly] cautionary" where "statements conveyed substantive information about the risk that ultimately materialized"). As such, no "'reasonable investor could have been misled into thinking that the risk that materialized and resulted in his loss did not actually exist.'" *WEBMD*, 2013 WL 64511, at *8 (quoting *Halperin v. eBanker USA.com, Inc.*,

[16] On investor calls, Genworth advised investors to "read the cautionary note regarding forward-looking statements and our earnings release and the Risk Factors section of our most recent annual report on Form 10-K filed with the

295 F.3d 352, 359 (2d Cir. 2002)); *see also In re Duane Reade Inc. Sec. Litig.*, 2003 WL 22801416, at *6 (S.D.N.Y. Nov. 25, 2003) (unlike "children" investors "know that … when a company's officer makes predictions … they are not issuing guarantees") (citation omitted), *aff'd sub nom. Nadoff v. Duane Reade, Inc.*, 107 F. App'x 250 (2d Cir. 2004).

Plaintiffs cannot credibly argue that the risk that ultimately materialized—postponement of the IPO due to unanticipated, higher losses—was not fully, repeatedly, and expressly disclosed to investors throughout the class period. On this basis alone, regardless of whether Plaintiffs have pleaded that Defendants' statements were knowingly false when made, Plaintiffs' challenge to Genworth's statements concerning the expected timing of the IPO fails. *Gissin*, 739 F. Supp. 2d at 511 n.144 (the court "need not consider whether [defendants] had 'actual knowledge' that their statements were false" because defendants "prevail on the 'meaningful cautionary language' prong of the safe harbor"). In other words, if the language is meaningfully cautionary, Plaintiffs' challenge to Defendants' forward-looking statements fails.

Second, even if Defendants' forward-looking statements were not accompanied by cautionary language, Plaintiffs do not state a Section 10(b) claim because Plaintiffs fail to plead that these statements were "made with actual knowledge that [they] w[ere] false or misleading." *Slayton*, 604 F.3d at 766. "[A]ctual knowledge" of falsity is "stricter than [the scienter requirement] for statements of current fact" and requires "proof of knowing falsity." *Id.* at 773 (citation omitted). As discussed in Point I.C above, nowhere in the complaint do Plaintiffs plead particularized facts showing that Defendants did not "expect[]" or "anticipate" a "second-quarter 2012 execution" for the IPO if market and other conditions permitted. *See id.* at 776 (dismissing for failure to plead actual knowledge); *WEBMD*, 2013 WL 64511, at *15 (dismissing "[b]ecause

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SEC in February 2011." Ex. A (11/4/2011 Tr.) at 2; *see also* Ex. J (2/3/2012 Tr.) at 1-2; Ex. K (3/29/2012 Tr.) at 1.

Plaintiffs have failed to prove that Defendants made forward-looking statements with actual knowledge of their falsity").

IV. PLAINTIFFS FAIL TO STATE A CLAIM AGAINST THE INDIVIDUAL DEFENDANTS

Finally, in the March 25 Order, the Court instructed that "the Second Amended Complaint must allege, 'with respect to each act or omission' that is false and misleading, and with 'particularity,' the facts giving rise to a strong inference that the defendant acted with scienter. 15 U.S.C. §78u-4(b)(2). *The showing must be specific to the company as well as to each of the two individual defendants*." Dkt. No. 41 at 3-4 (emphasis added). Although Plaintiffs continue to allege Section 10(b) claims against Mr. Fraizer and Mr. Klein individually, they fail to plead *any* facts specifically supporting that either Mr. Fraizer or Mr. Klein acted with scienter or made a false statement.

As a threshold matter, Plaintiffs fail to plead that either Mr. Fraizer or Mr. Klein acted with any motive or intent to defraud, nor is Mr. Fraizer or Mr. Klein alleged to have personally benefited from the alleged "fraud" in any way. *See Shemian v. Research In Motion Ltd.*, 2013 WL 1285779, at *14 (S.D.N.Y. Mar. 29, 2013) ("Plaintiff cannot rely on allegations of motive and opportunity to support his claim" because "Plaintiff has failed to identify any 'concrete and personal' benefit that would have motivated the Individual Defendants to engage in securities fraud") (citing *ECA,* 553 F.3d at 198), *aff'd*, 570 F. App'x 32 (2d Cir. 2014).

Instead, unable to plead motive, Plaintiffs appear to proceed under a theory that some unspecified internal information contradicted Mr. Fraizer's and Mr. Klein's remarks and was available to them at the time of the challenged statements, and that both men recklessly disregarded it—but Plaintiffs provide *none* of the requisite particularized allegations to support this theory of liability.

Plaintiffs allege that Messrs. Fraizer and Klein misled investors in February 2012 when they discussed the IPO during the class period, challenging Mr. Fraizer's statement that "we continue to move forward with our planned minority interest IPO of up to 40% of Australia Mortgage Insurance" and that "[w]e still anticipate second-quarter 2012 execution" and "have not encountered any regulatory or market conditions that would change that timing" (SAC ¶ 96), and Mr. Klein's statement that the "expected timing [for the IPO] would be sometime in the second quarter" (SAC ¶ 104). Plaintiffs also challenge Mr. Klein's statements one month later, in March 2012, that Genworth wanted to do the IPO "from a position of strength" and that Defendants were "working very actively to put ourselves in a position to execute this in the second quarter, as we've said" (SAC ¶ 106). But Plaintiffs fail to plead any specific facts remotely suggesting that either Mr. Fraizer or Mr. Klein, in either February or March 2012, did not genuinely hold their stated beliefs that the IPO would go forward as planned, or that they did not want Genworth to complete the IPO "from a position of strength," or that they and others at Genworth were not "working very actively" to complete the IPO in the second quarter of 2012. Plaintiffs' challenge to Mr. Fraizer's opinion that "Australia is transitioning as expected, absorbing the loss pressures coming from the early 2011 Queensland flood events" (SAC ¶ 91) fails for the same reason: Plaintiffs plead no facts suggesting that Mr. Fraizer did not genuinely hold his opinion that Australia was transitioning as he expected.

Rather, the claims against Mr. Fraizer and Mr. Klein rely solely on Plaintiffs' unsupported assertions that both individuals purportedly were aware of a material increase in delinquencies and claims at the time of the challenged statements. For all the reasons above, those assertions fail to support a Section 10(b) claim. But regardless, the assertions do not support a claim against Mr. Fraizer and Mr. Klein individually because there is *no* allegation that

the purportedly contradictory information was available to them in February or March 2012 at the time they made the challenged statements. CW1 is not alleged to have had any contact with either Mr. Fraizer or Mr. Klein or provided information to them. CW2 merely says that he prepared reports that Mr. Fraizer reviewed (SAC ¶ 70)—but critically the reports are not alleged to have contained any information that contradicted any of Mr. Fraizer's or Mr. Klein's alleged misstatements. Plaintiffs thus fail to state a claim against Messrs. Fraizer and Klein. *See Malin v. XL Capital Ltd.*, 499 F. Supp. 2d 117, 141 (D. Conn. 2007) (rejecting claims against individual defendants where there was no allegation that the purportedly contradictory information was "communicated … to any of the Individual Defendants or that the Individual Defendants otherwise knew about these issues"), *aff'd*, 312 F. App'x 400 (2d Cir. 2009); *Mechel OAO*, 811 F. Supp. 2d at 880 (rejecting CW allegations where the "confidential witness does not describe any communications with the Defendants or provide grounds to believe they were aware of the alleged scheme"); *Avon Prods.*, 2014 WL 4832321, at *22 (dismissing claims where plaintiffs failed to plead that sources "were privy to the Individual Defendants' knowledge or had direct contact with the Individual Defendants, such that the Individual Defendants are alleged to have knowledge of or access to contemporaneous information that would show that their representations were false") (citation omitted).

V. PLAINTIFFS FAIL TO PLEAD CONTROL PERSON LIABILITY UNDER SECTION 20(A) OF THE EXCHANGE ACT

Plaintiffs' Section 20(a) claim fails because the complaint pleads no primary violation of the federal securities laws. *See Rombach*, 355 F.3d at 178.

CONCLUSION

Plaintiffs have had three tries at stating a securities fraud claim against Defendants. Plaintiffs were on notice of the legal insufficiencies in their first amended complaint—fully

briefed in Defendants' first motion to dismiss and outlined by the Court in its March 25 Order (Dkt. No. 41 at 3)—and were unable to cure them. There is nothing to suggest that they will be able to do so in a fourth complaint. For the reasons above, the second amended complaint should be dismissed with prejudice in its entirety, with no leave to replead.

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Respectfully submitted,

/s/ Greg A. Danilow

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