UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

CASE NO.: 07-22601-CIV-HUCK/O'SULLIVAN

SPENCER ABRAMS, individually and on
behalf of all others similarly situated,

Plaintiffs,
vs.

MICRUS ENDOVASCULAR CORP.,
JOHN KILCOYNE, and ROBERT STERN,

Defendants.
_______________________________________/

ORDER GRANTING MOTION TO DISMISS
CONSOLIDATED CLASS ACTION COMPLAINT

This is a shareholder class action suit brought against Micrus Endovascular Corporation (the "Company"), John Kilcoyne, and Robert Stern (collectively, "Defendants"), pursuant to Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 (the "Exchange Act"). On October 3, 2007, the first of two class action complaints was filed in this case. The two complaints were then consolidated, and Plaintiffs Spencer Abrams, Terrill Weiss, and Oppenheimer Asset Management Services (collectively, "Lead Plaintiffs") filed the operative consolidated class action complaint (the "Complaint") on February 6, 2008 [D.E. #33]. On February 26, 2008, Defendants filed a Motion to Dismiss [D.E. #34], which is now fully briefed and ripe for determination. For the reasons discussed below, the Defendants' Motion to Dismiss is GRANTED, and the Complaint is DISMISSED WITHOUT PREJUDICE.

BACKGROUND

Lead Plaintiffs brought this securities class action on their behalf and on behalf of all other similarly situated persons who purchased the Company's stock between February 12, 2007 and

September 17, 2007 (the "Class Period") (collectively, "Plaintiffs"). The Complaint alleges that during the Class Period the Defendants overstated the Company's future prospects and failed to disclose material facts about the Company's financial condition in violation of Sections 10(b) and 20(a) of the Exchange Act, resulting in artificial inflation of the Company's stock price. The Complaint contains the following allegations in support of those claims:

1. The Company, which was formed in 1996 and became publicly-traded in 2005, develops, manufactures, and markets implantable and disposable medical devices used in the treatment of cerebral vascular diseases and intracranial aneurysms. In recent years, the Company has been engaged in an aggressive growth strategy marked by product development and geographic expansion, particularly in Asia.

2. Defendant John Kilcoyne served as the Company's President and CEO beginning in November 2004, and he held that position throughout the Class Period.

3. Defendant Robert Stern served as the Company's CFO beginning in November 2004, and he held that position throughout the Class Period.

4. The Complaint contains allegations based on information from four confidential witnesses who had been Company employees. However, one of those witnesses was no longer a Company employee at the time the Class Period began, and the other three witnesses were no longer Company employees by the end of the Class Period.

5. According to the confidential witnesses, the Company was having significant problems with the quality of its products during the Class Period. One of the witnesses, a former marketing manager, said that "all of [the Company's] products were breaking." Manufacturing and quality issues delayed the unveiling of a new product, the ENZO catheter, which the Company had "hyped" for years. Moreover, when the ENZO catheter was demonstrated to physicians at a

conference in early August 2007, the feedback was "not as good as expected." The Company was also having significant problems with its "bread and butter" products – its microcoils – which represented approximately 90% of the Company's revenues. The Company was beginning to lose its microcoil business to competitors as early as the middle of 2006.

6. In September 2005, the Company entered into an exclusive agreement with a distributor in Japan, and the Company's growth strategy became increasingly focused on entering the Asian market. However, according to one confidential witness, the products that the Company sold to the Japanese distributor "filled the distributor's warehouses and never moved." One of the Company's competitors "owned" the Japanese market, making it difficult for the Company to gain any ground in Japan. By the end of April 2007, it was clear that the Company's distributor in Japan was not ordering additional products from the Company beyond a $1.1 million shipment which the Company had already booked as revenue. Part of the reason for the lag in sales to Japan was that the Company did not receive some desired Japanese regulatory approvals until December 2007, which was later than had been expected.

7. Plaintiffs claim that the facts stated above were known to Defendants but that Defendants nevertheless issued the following statements about the Company's business prospects:

- On February 12, 2007, Defendant Kilcoyne stated that the Company's third quarter Fiscal Year 2007[1] revenues were "evidence of our ability to gain market share." Also, during an earnings conference call that same day, Defendant Stern noted that the Company had received regulatory approval for only one of their products but that "Japan continues to be really strong."

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[1] The Company's fiscal year ("FY__") runs from April 1st of each year to March 31st of the following year.

- On May 10, 2007, the Company issued a press release which projected that FY08 revenues would be $80 - $85 million. That press release stated, "[w]e believe our growth momentum will continue in the current fiscal year with the continued launch of new products."
- On August 7, 2007, Defendants issued a press release stating that they "expect[ed] strong revenue growth and market share gains throughout fiscal 2008, with greater acceleration in the second half of the fiscal year." Also, during an earnings conference call that same day, Defendant Kilcoyne stated that "the ENZO [catheter] had been very well received."

8. Plaintiffs allege that Defendants Kilcoyne and Stern knew about all the problems with the Company's products because they were very actively involved in the Company's operation. Moreover, one confidential witness stated that he had attended meetings, at which Kilcoyne and Stern were present, where these problems were discussed.

9. On September 17, 2007, the Company issued a press release which lowered its FY08 revenue projection from $80 - $85 million to $65 - $75 million. The announcement caused the price of the Company's shares to decrease by $6.20 a share, or approximately 26%, resulting in tens of millions of dollars in investor losses.

Defendants have moved to dismiss the Complaint on the grounds that: (1) Plaintiffs have failed to allege specific facts which establish that any of the challenged statements were false or misleading when made, as required by the Private Securities Litigation Reform Act (the "Reform Act"); (2) Plaintiffs have failed to specifically allege facts showing that their confidential witnesses were in a position to know about the truth or falsity of the challenged statements; and (3) Plaintiffs have failed to allege specific facts which establish that Defendants acted with the requisite scienter.

In addition, Defendants argue that the challenged statements are forward-looking statements, protected by the Reform Act's "safe harbor" provision.

STANDARD OF REVIEW

In reviewing a motion to dismiss, a court must assume that the allegations in the complaint are true, and must view all facts and inferences in the light most favorable to the non-moving party. *Scott v. Taylor*, 405 F.3d 1251, 1253 (11th Cir. 2005). Dismissal is only appropriate "when the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Horsley v. Feldt*, 304 F.3d 1125, 1131 (11th Cir. 2002).

"[W]hen considering a motion to dismiss in a securities fraud case, [a court] may take judicial notice . . . of relevant public documents required to be filed with the SEC, and actually filed." *Bryant v. Avado Brands, Inc.*, 187 F.3d 1271, 1278 (11th Cir.1999).

ANALYSIS

I. Claim under Section 10(b) of the Exchange Act

A. Legal Standard for Liability under Section 10(b)

To state a meritorious claim under Section 10(b) of the Exchange Act, a plaintiff must allege: (1) a misstatement or omission; (2) of a material fact; (3) made with scienter; (4) on which plaintiff relied; and (5) that proximately caused the plaintiff's injury. *Ziemba v. Cascade Int'l, Inc.*, 256 F.3d 1194, 1202 (11th Cir. 2001). Furthermore, under the Reform Act, a plaintiff who alleges violations of Section 10(b) must "specify each statement alleged to have been misleading, [and] the reasons why the statement is misleading." 15 U.S.C. § 78u-4(b)(1). The plaintiff must specify the time place, and content of a defendant's alleged false representations. *Ziemba*, 256 F.3d at 1202; *see also Garfield v. NDC Health Corp.*, 466 F.3d 1255, 1262 (11th Cir. 2006) ("A sufficient level of factual support for a 10(b) claim may be found where the circumstances of the fraud are pled in detail. This

means the who, what, when, where, and how: the first paragraph of any newspaper story."). The Court concludes that Plaintiffs have failed to meet these pleading requirements.

B. Misstatements or Omissions of Material Facts versus "Mere Puffing"

Plaintiffs argue that various statements made by Defendants during the Class Period were false or misleading when made. However, the statements to which Plaintiffs point represent the type of "corporate optimism" or "mere puffing" which is not covered by the Exchange Act. Such statements are not actionable under the Exchange Act because they are not capable of objective verification and because "no reasonable investor would make an investment decision based on [such] statement[s]." *In re Winn-Dixie Stores, Inc. Secs. Litig.*, 531 F. Supp. 2d 1334, 1347 (M.D. Fla. 2007). For example, Defendant Stern's statement that "Japan continues to be really strong" is not a statement of verifiable fact. *See In re First Union Corp. Secs. Litig.*, 128 F.Supp.2d 871, 891 (W.D.N.C. 2001) (finding that the statement — "We are very pleased with our progress in integrating recent acquisitions and with the growth prospectus stemming from these transactions" — was immaterial puffery).[2] Defendant Kilcoyne's statement that the ENZO catheter "has been very well received" also falls into the category of non-verifiable puffery. *See Grossman v. Novell, Inc.*, 120 F.3d 1112, 1121-22 (10th Cir. 1997) (finding that a CEO's statements that his company had experienced "substantial success" in integrating with a newly merged company and that the merger was moving "faster than we thought it would" were "the sort of soft puffing statements, incapable of objective verification, that courts routinely dismiss as vague statements of corporate optimism"). Finally, the FY08 revenue projection of $80 - 85 million was also not an actionable

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[2] Moreover, Defendants' statements in this case indicated that Japanese regulatory approval had been obtained for some but not all of its products. It is therefore unclear what false or misleading statement or omission of a material fact is alleged regarding the Company's involvement in the Japanese market.

statement of fact. *See In re S1 Corp. Secs. Litig.,* 173 F.Supp.2d 1334, 1350-51 (N.D.Ga. 2001) (observing that "sales figures, forecasts and the like only rise to the level of materiality when they can be calculated with substantial certainty"); *In re Winn-Dixie Stores, Inc. Secs. Litig.*, 531 F. Supp. 2d at 1347 (granting motion to dismiss a Section 10(b) case because the defendant's statement that "continued improvement in gross profit dollars is anticipated" was non-verifiable, immaterial puffery).[3]

Plaintiffs also suggest that Defendants had an affirmative obligation to disclose problems that the Company was allegedly having with its products. However, Plaintiffs have not pointed to specific, material facts which Defendants had a duty to disclose. A duty to disclose arises where a defendant's failure to speak would render some of the defendant's statements misleading or deceptive. *Ziemba*, 256 F.3d at 1206. "[T]he question is not simply whether the defendants omitted information potentially of interest to investors. To be actionable, the omission must render the statements *actually made* misleading." *In re S1 Corp. Secs. Litig.,* 173 F.Supp.2d at 1350 n.12 (emphasis in original). Plaintiffs have not pointed to, and the Court has not found, case law which suggests that there is an affirmative duty to disclose internal challenges similar to those that were allegedly occurring with the Company's products in this case. *See, e.g., In re Telecom Ltd. Secs. Litig.,* 116 F.Supp.2d 446, 459 (S.D.N.Y. 2000) ("A company is generally not obligated to disclose

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[3] Because the Court concludes that none of the challenged statements in this case are material statements of verifiable fact, it need not address whether those statements are also protected under the Reform Act's safe harbor for"forward-looking statements." Nevertheless, the Court notes that most of the challenged statements in this case were specifically identified as "forward-looking statements" and were "accompanied by meaningful cautionary statements" which warned that the results of the Company's projections could vary based on, *inter alia,* "the Company's dependence on developing new products," "challenges associated with complying with applicable ... international regulations," and "the Company's ability to compete with large, well-established ... manufacturers." *See, e.g., Company Press Release, dated May 10, 2007, attached as Exh. B to the Complaint*; *see also* 15 U.S.C. § 78u-5(c)(1)(A)(I) (explaining the standard for the "forward-looking statement" safe harbor).

internal problems because the securities laws do not require management to bury the shareholders in internal details and because public disclosure of internal management and engineering problems falls outside the securities laws."); *In re Allscripts, Inc. Secs. Litig.,* 2001 WL 743411 at *6 (N.D. Ill., June 29, 2001) (holding that a duty to disclose declines in customer satisfaction with a company's products "would not comport with the way the business world works").

C. Scienter

Even if the Court were to find that some of the challenged statements were misleading due to the Defendants' failure to disclose material facts, the Complaint fails to sufficiently allege that Defendants acted with the required scienter. Scienter is defined as "a mental state embracing intent to deceive, manipulate, or defraud." *Bryant*, 187 F.3d at 1281-82. The Reform Act provides that a plaintiff must "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2). The particular facts alleged may be aggregated to infer scienter. *Phillips v. Scientific-Atlanta, Inc.*, 374 F.3d 1015, 1017 (11th Cir. 2004). "The inquiry . . . is whether *all* of the facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegation, scrutinized in isolation, meets that standard." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S. Ct. 2499, 2509 (2007) (emphasis in original). Moreover, "[t]he inference that the defendant acted with scienter need not be irrefutable, *i.e.*, of the 'smoking gun' genre, or even the 'most plausible of competing inferences.'" *Id.* at 2510. Rather, the relevant inquiry is whether "a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged." *Id.*

Most of Plaintiffs' allegations regarding Defendants' state of mind are vague and simply conclude that Defendants knew certain information and intentionally hid that information from

investors. Plaintiffs rely heavily on the fact that Defendants Kilcoyne and Stern were actively involved in the operation of the Company and therefore must have known about the alleged problems. *See Plaintiff's Opposition to Defendants' Motion to Dismiss* at 10-11. However, "it is not enough to make conclusory allegations that Defendants had access to the 'true facts' in order to demonstrate scienter, particularly when the complaint fails to allege which defendant knew what, how they knew it, or when." *Coca-Cola Enters., Inc. Secs. Litig*., 510 F.Supp.2d 1187, 1201 (N.D.Ga. 2007). "Nor does a vague assertion that a defendant must have known about the fraud by virtue of his position of authority suffice to prove a strong inference of scienter." *Id.*

One of Plaintiffs' confidential witnesses states that he attended meetings, at which Defendants Kilcoyne and Stern were present, where the problems with various products were discussed. However, the Complaint contains no description of when those meetings occurred or what specifically was said, to whom, and in what context. Such vague reports of meetings are not sufficiently indicative of Defendants' state of mind when the challenged statements were made. *See Garfield*, 466 F.3d at 1264-65 (rejecting an attempt to establish scienter by alleging that the defendant had attended a meeting to discuss every aspect of the business, because the plaintiff did not explain "what was said at the meeting, to whom it was said, or in what context"); *In re Winn-Dixie Stores, Inc. Secs. Litig.*, 531 F. Supp. 2d at 1350 (holding that "vague allegations about meetings allegedly addressing the 'numbers' forecast... do not establish that Defendants were aware of any alleged problems... nor would Defendants' awareness of any such problems raise a strong inference of scienter as to the alleged 'fraud' in any event.").

The Court also finds it relevant that the confidential witnesses were not employed by the Company at the time some of the challenged statements were made. *See Marrari v. Med. Staffing Network Holdings, Inc.,* 395 F.Supp.2d 1169, 1188 (S.D.Fla. 2005) ("[A]nonymous sources may

be used to sustain complaints under the [Reform Act] so long as the sources are described with sufficient particularity to support the probability that a person in the position occupied by the source would possess the information alleged.”). While the confidential witnesses in this case may have had some knowledge of problems within the Company during the course of their employment, Plaintiffs have failed to allege with sufficient particularly how the witnesses had reason to be informed about either the alleged problems or Defendants’ knowledge of those problems at the time the challenged statements were made.

Finally, the Court notes that Plaintiffs have failed to allege any financial gain by Defendants. Indeed, as Defendants Kilcoyne and Stern indicated in their Motion to Dismiss, they each lost money when the Company voluntarily readjusted its FY08 revenue projections in September 2007. The absence of an apparent motive weighs against a finding of scienter in this case. *See Tellabs*, 127 S.Ct. at 2511 (holding that although “the absence of a motive allegation is not fatal” to a Section 10(b) claim, “motive can be a relevant consideration” in determining whether Defendants acted with scienter).

In conclusion, the Court finds that the Complaint fails to identify any actionable misstatements or omissions of material facts under Section 10(b) of the Exchange Act, and that the Complaint does not adequately allege that the Defendants acted with the requisite scienter.

II. Claim under Section 20(a) of the Exchange Act

In order to state a claim under Section 20(a) of the Exchange Act, Plaintiffs must allege “(1) a primary violation of the securities laws by a controlled person; (2) that the defendant had the power to control the general business affairs of the controlled person; and (3) that the defendant had the requisite power to directly or indirectly control or influence the specific corporate policy which resulted in the primary liability.” *Bruhl v. Conroy*, No. 03-23044-CIV,

2007 WL 983228, at *7 (S.D.Fla. Mar. 27, 2007) (citing *Theoharous v. Fong*, 256 F.3d 1219, 1227 (11th Cir. 2001)). Because the Complaint fails to state a claim under Section 10(b), the dependant Section 20(a) claim must also be dismissed for failure to properly allege "a primary violation of the securities law." *See Theoharous*, 256 F.3d at 1227 (11th Cir. 2001) (dismissing Section 20(a) count after finding no violation of Section 10(b)).

CONCLUSION

For the foregoing reasons, Defendants' Motion to Dismiss is GRANTED. It is ORDERED AND ADJUDGED that the Complaint is DISMISSED WITHOUT PREJUDICE. If Plaintiffs wish to file an amended complaint, they may do so on or before **Friday, May 30, 2008.** If Plaintiffs fail to amend the Complaint by that time, the Court will dismiss this case with prejudice and instruct the Clerk of the Court to mark this case closed.

DONE AND ORDERED in Chambers, Miami, Florida, this 19th day of May, 2008.

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Paul C. Huck
United States District Judge

Copies furnished to:
Counsel of Record