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RICHARD W. WIEKING
CLERK, U.S. DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

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16 Plaintiff Fred Kessler

17 **IN THE UNITED STATES DISTRICT COURT**
18 **FOR THE NORTHERN DISTRICT OF CALIFORNIA**
19 **SAN FRANCISCO DIVISION**

C 01 - 0555
Case No.

EDL

PSLRA

20 **FRED KESSLER**, on behalf of himself and all others
21 similarly situated,

22 **Plaintiff,**

23 **v.**

24 **CRITICAL PATH, INC.; DAVID THATCHER;**
25 **WILLIAM RINEHART,**

26 **Defendants.**

CLASS ACTION COMPLAINT FOR VIOLATIONS OF SECURITIES EXCHANGE ACT OF 1934

JURY TRIAL DEMANDED

27 Plaintiff makes the following allegations upon information and belief, except as to allegations
28 specifically pertaining to Plaintiff and his counsel, based on the facts alleged below, predicated upon
the investigation undertaken by and under the supervision of Plaintiff's counsel, and Plaintiff believes
that further substantial evidentiary support will exist for the allegations set forth below after a
reasonable opportunity for discovery.

1 **JURISDICTION AND VENUE**

2 1. The claims asserted herein arise under and pursuant to Sections 10(b) and 20(a) of the
3 Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § § 78j(b) and 78t(a), and
4 Rule 10b-5 promulgated thereunder by the Securities and Exchange Commission ("SEC"), 17 C.F.R.
5 § 240.10b-5.

6 2. This Court has jurisdiction of this action pursuant to Section 27 of the Exchange Act,
7 as amended, 15 U.S.C. § 78aa, and 28 U.S.C. §§ 1331 and 1337.

8 3. Venue is properly laid in this District pursuant to Section 27 of the Exchange Act and
9 28 U.S.C. § 1391(b) and (c). The acts, conduct, combination and conspiracy complained of,
10 including the preparation, issuance and dissemination of materially false and misleading information to
11 the investing public, occurred in substantial part in the Northern District of California. Critical Path,
12 Inc. ("CPI" or the "Company") maintained its principal place of business in this District at all relevant
13 times.

14 4. In connection with the acts, conduct, combination and conspiracy alleged in this
15 Complaint, Defendants, directly or indirectly, used the means and instrumentalities of interstate
16 commerce, including the mails and telephonic communications and the facilities of the NASDAQ
17 National Market System, a national securities exchange.

18 **INTRADISTRICT ASSIGNMENT**

19 5. This action is properly assigned to the San Francisco Division, as CPI maintained its
20 principal place of business in the City and County of San Francisco at all relevant times, and a
21 substantial part of the events or omissions giving rise to the asserted claims occurred in the City and
22 County of San Francisco.

23 **PARTIES**

24 6. Plaintiff Fred Kessler, as set forth in the accompanying certification, purchased CPI
25 common stock at artificially inflated prices during the Class Period, and has been damaged thereby.

26 7. CPI is a California corporation with its principal executive offices located at 320 First
27 Street, San Francisco, California 94105. CPI is a provider of complete end-to-end Internet
28

1 messaging and collaboration solutions for Internet service providers, telecommunications providers,
2 Web hosting companies, web portals, and corporations.

3 8. The individual defendants identified below served, at times material to the claims set
4 forth herein as senior officers of CPI in the positions set forth opposite their names (the "Individual
5 Defendants"):

6 Name	7 Position
8 David Thatcher ("Thatcher")	9 President
10 William Rinehart ("Rinehart")	11 Vice President, Worldwide Sales

12 9. As officers and/or controlling persons of a company which is registered with the SEC
13 under the federal securities laws, whose common stock is registered with the SEC, traded on the
14 NASDAQ National Market System, and governed by the provisions of the federal securities laws, the
15 Individual Defendants had a duty to disseminate promptly accurate and truthful information with
16 respect to the Company's operations, business, products, markets, management, earnings and present
17 and future business prospects, to correct any previously issued statements from any source that have
18 become materially misleading or untrue, and to disclose any trends that would materially affect
19 earnings and the present and future operating results of CPI, so that the market price of the
20 Company's publicly traded securities is based upon truthful and accurate information. The
21 Defendants' representations during the Class Period violated these specific requirements and
22 obligations.

23 10. The Individual Defendants participated in the drafting, preparation, and/or approval of
24 the various public and shareholder reports and other communications complained of herein and were
25 aware of or recklessly disregarded the misstatements contained therein and omissions therefrom, and
26 were aware of their materially misleading nature. Because of their executive and managerial positions
27 with CPI, each of the Individual Defendants had access to the adverse non-public information about
28 CPI's business prospects and financial condition as particularized herein and knew that those adverse
29 facts rendered the positive statements made by and about CPI and its business and future sales,
30 materially false and misleading.

1 NASDAQ National Market System, an efficient market. The precise number of Class members is
2 unknown to Plaintiff at this time, but Class members are believed to number in the thousands. In
3 addition, the names and addresses of the Class members can be ascertained from the books and
4 records of CPI or its agents.

5 15. Plaintiff will fairly and adequately represent and protect the interests of the members
6 of the Class. Plaintiff has retained competent counsel experienced in class action litigation under the
7 federal securities laws to further ensure such protection and intends to prosecute this action
8 vigorously.

9 16. Plaintiff's claims are typical of the claims of the other members of the Class, because
10 the damages of Plaintiff and all other Class members arise from and were caused by the same false
11 and misleading representations and omissions made by or chargeable to Defendants. Plaintiff does
12 not have interests antagonistic to, or in conflict with, the Class.

13 17. A class action is superior to other available methods for the fair and efficient
14 adjudication of this controversy. As the damages suffered by individual Class members may be
15 relatively small, the expense and burden of individual litigation make it virtually impossible for the
16 Class members to seek redress for the wrongful conduct alleged. Plaintiff knows of no difficulty that
17 will be encountered in the management of this litigation which would preclude its maintenance as a
18 class action.

19 18. Common questions of law and fact exist as to all members of the Class and
20 predominate over any questions affecting solely individual members of the Class. Among the
21 questions of law and fact common to the Class are:

22 (a) Whether the federal securities laws were violated by Defendants' acts as
23 alleged herein;

24 (b) Whether Defendants participated directly or indirectly in the concerted action
25 or common course of conduct complained of herein;

26 (c) Whether the documents, filings, releases and statements disseminated to the
27 investing public omitted and/or misrepresented material facts about the business and financial
28 condition of CPI;

1 (d) Whether Defendants acted willfully, knowingly, or recklessly in directly or
2 indirectly omitting to state and/or misrepresenting material facts;

3 (e) Whether the market price of the Company's common stock during the Class
4 Period was artificially inflated due to the non-disclosures and/or misrepresentations complained of
5 herein; and

6 (f) The extent of injuries sustained by members of the Class and the appropriate
7 measure of damages.

8 19. The names and addresses of the record owners of the shares of CPI's common stock
9 purchased during the Class Period are available from the Company's transfer agent. Notice can be
10 provided to such record owners by a combination of published notice and first-class mail using
11 techniques and a form of notice similar to those customarily used in class actions arising under the
12 federal securities laws.

13 **FRAUD-ON-THE-MARKET DOCTRINE**

14 20. Plaintiff will rely, in part, upon the presumption of reliance established by the fraud-
15 on-the-market doctrine in that, among other things:

16 (a) CPI common stock met the requirements for listing, and was listed, on the
17 NASDAQ National market System, a highly efficient and automated market;

18 (b) As a regulated issuer, the Company filed periodic public reports with the SEC;

19 (c) The trading volume of the Company's stock was substantial, reflecting
20 numerous trades each day;

21 (d) CPI was followed by securities analysts employed by several major brokerage
22 firms who wrote reports that were distributed to the sales force and certain customers of such firms
23 and that were available to various automated data retrieval services;

24 (e) Defendants made public statements that failed to disclose material facts during
25 the Class Period;

26 (f) The omissions and misrepresentations were material;

27 (g) The misrepresentations alleged would tend to induce a reasonable investor to
28 misjudge the value of the Company's securities; and

1 (h) Plaintiff and the other members of the Class purchased CPI common stock
2 without knowledge of the omitted and misrepresented facts.

3 21. Based upon the foregoing, Plaintiff and the other members of the Class are entitled to
4 a presumption of reliance upon the integrity of the market for the purpose of class certification as well
5 as for ultimate proof of the claims on their merits. Plaintiff will also rely, in part, upon the
6 presumption of reliance established by material omission and upon the actual reliance of the Class
7 members.

8 **FACTUAL ALLEGATIONS**

9 22. On February 2, 2001, shortly after the market opened, CPI issued a press release
10 stating that the Company had suspended two of its principal officers and had engaged a Special
11 Committee to conduct an investigation into certain misleading revenue recognition practices that
12 rendered certain of the Company's prior financial disclosures materially false and misleading. Although
13 the press release vaguely suggests that only the Company's financial disclosures pertaining to the
14 Company's fourth quarter of fiscal year 2000 were false and misleading, the extraordinary nature of
15 the disclosure, combined with the summary suspension of two of the Company's principal officers,
16 strongly suggests that the Company's financial disclosures, including the endorsement of prior
17 earnings guidance to analysts, was false and misleading at least for the past several months.

18 **Class Period Events**

19 23. The Class Period commences on November 29, 2000, the date on which CPI first
20 disclosed that its then-Chief Financial Officer was leaving the Company. At the time, the Company
21 attempted to minimize this mid-quarter departure, suggesting that the departure was for "personal
22 reasons" and specifically urging to analysts and the investment community that the Company's prior
23 earnings guidance and fiscal fourth quarter earnings performance expectations were completely
24 unrelated to the departure, and that the Company's fourth quarter was on track.

25 24. For example, the next day, analyst Robert W. Baird & Co. issued a report strongly
26 urging investors to "Buy" the Company's stock and declaring that the Company's "fundamentals"
27 were strong, and that the Company was on track to perform well in the fourth quarter of 2000. The
28

1 report, expressly based on Company guidance, stated that the Company was on track to earn \$0.01
2 per share in the quarter.

3 25. Likewise, on December 7, 2000, Chase H&Q issued a report on the Company entitled
4 "Critical Path Makes Management Change, Maintain Strong BUY Recommendation." This report
5 similarly included a Company-endorsed estimate that the Company would earn \$0.01 per share. This
6 opinion was reiterated by Chase H&Q on January 4, 2001. Many other analysts followed the
7 Company and regularly communicated with the Company and issued similar reports that downplayed
8 management changes in the Company's financial control positions, while simultaneously endorsing
9 estimates that the Company was anticipated to achieve substantial revenue growth and quarterly
10 profitability as described above.

11 26. Critical Path stock traded at over \$28.00 per share on November 28, 2000. It closed
12 at \$25.00 per share on November 29, 2000, and slipped further in the ensuing days. By late-
13 December, however, amid the repeated assurances that the Company was on track, the stock rose to
14 over \$30.00 per share.

15 27. On January 18, 2001, after the market closed, Critical Path issued an earnings
16 announcement that stated in pertinent part:

17 Revenue for the quarter reached \$52.0 million, a 16 percent sequential increase over
18 revenue of \$45.0 million in the third quarter of 2000, and a 534 percent increase over
19 revenue of \$8.2 million in the fourth quarter of 1999. The net loss for the quarter,
20 excluding special charges, was \$11.5 million, or \$0.16 per share, compared with a net
21 loss, excluding special charges, of \$8.7 million, or \$0.14 per share, in the third quarter
of 2000, and a net loss of \$11.0 million, or \$0.26 per share, in the fourth quarter of
1999. The Company also reported gross profit, excluding special charges, of
\$29.1 million, a 15 percent increase over gross profit of \$25.3 million in the third
quarter of 2000.

22 The reported revenues for the quarter do not include \$7.0 million related to a large
23 enterprise license agreement that was executed during the quarter. Due to complex
24 and evolving rules governing revenue recognition for software license arrangements,
25 the Company, in consultation with its outside auditors, determined that the revenue
26 from this transaction required deferral as of December 31, 2000. The Company
27 anticipates recognizing the revenue from this transaction on a "sell-through" basis in
28 the future rather than as an up-front license fee in the fourth quarter of 2000, as
anticipated.

"Despite a difficult economic environment, Critical Path achieved solid revenue
growth and improved gross margins, while adding over 200 new customers and
further solidifying our category leadership position," said Doug Hickey, Critical Path's
CEO.

1 According to Chief Financial Officer Larry Reinhold, other factors in addition to the
2 deferred revenue mentioned previously had an impact on results in the fourth quarter
3 of 2000. These factors included a non-operating foreign exchange loss due primarily
4 to currency fluctuations in U.S. dollar-denominated European revenues, higher than
5 expected operating expenses in the recently acquired PeerLogic business as full
6 synergies have not yet been achieved, and the provision of a significant allowance for
7 doubtful accounts.

8 "While we are disappointed with the bottom-line impact of these charges, we are
9 evaluating and will be taking concrete steps to control the underlying factors
10 impacting these areas," said Reinhold.

11 28. Finally, on February 2, 2001, the Company issued the announcement described above,
12 disclosing that the Company's prior financial disclosures, at least as to its fourth quarter of fiscal
13 2000, were materially false and misleading. The Company stated, among other things:

14 On January 18, 2001, the Company announced Fourth Quarter revenue of \$52 million
15 in revenue and net loss, excluding charges, of \$11.5 million. The Company now
16 believes that these results may be materially misstated.

17 29. Upon these revelations, NASDAQ trading of CPI stock was halted, and trading of CPI
18 on the Island ECN reduced its shares to approximately \$5.00 per share. Market losses in the stock
19 are devastating.

20 **Defendants Misrepresented And Failed To Disclose Material Facts**

21 30. In knowing or reckless disregard of the truth and/or as part of their ongoing efforts to
22 continue the illusion of CPI's business success, and market leadership, Defendants issued and/or
23 participated in the issuance of materially false and misleading statements to the investing public as
24 particularized above. These representations were materially false and misleading when made for the
25 reasons set forth above and in that they falsely stated and/or failed to disclose the following material,
26 adverse facts about CPI's business operations and financial condition, which facts were known to or
27 recklessly disregarded by Defendants that:

28 (a) They falsely overstated the Company's financial condition, and materially
overstated sales and revenues, gross profit, income and earnings per share.

(b) They falsely stated or implied that CPI's financial statements were prepared in
accordance with generally accepted accounting principles and in accordance with the federal
securities laws and SEC regulations concerning fair reporting.

1 34. Defendants engaged in such a scheme to artificially inflate the price of CPI securities in
2 order to facilitate transactions involving the use of Company stock as currency.

3 35. Moreover, the Individual Defendants engaged in such a scheme to inflate the price of
4 CPI securities in order to (i) protect and enhance their executive positions and the substantial
5 compensation and prestige they obtained thereby; (ii) enhance the value of their personal holdings of
6 CPI securities; and (iii) facilitate substantial and extremely profitable insider sales of CPI stock.

7 36. The market for CPI's common stock was open, well-developed and efficient at all
8 relevant times. As a result of the above-described false and misleading statements and failures to
9 disclose the full truth about CPI and its business and future prospects, the Company's common stock
10 traded at artificially inflated prices during the entire Class Period until the time the adverse
11 information described above was finally provided to and digested by the securities market. Plaintiff
12 and other members of the Class purchased or otherwise acquired CPI common stock relying upon the
13 integrity of the market price of CPI stock and market information related to the Company, or in the
14 alternative, upon Defendants' false and misleading statements, and in ignorance of the adverse,
15 undisclosed information and false financial statements know to Defendants, and have been damaged
16 thereby. Upon disclosure of the true facts regarding the Company, trading was halted in the sale of
17 the common stock. Had Plaintiff and other members of the Class known of the materially adverse
18 information not disclosed by Defendants, they would not have purchased or acquired CPI's common
19 stock at the artificially inflated prices that they did.

20 37. At all relevant times, the misrepresentations and omissions particularized in this
21 complaint directly or proximately caused or were a substantial contributing cause of the damages
22 sustained by Plaintiff and other members of the Class. As described herein, during the Class Period,
23 Defendants made or caused to be made a series of false statements about CPI's revenues and
24 earnings. These misstatements and omissions had the cause and effect of creating in the market an
25 unrealistically positive assessment of CPI, its profitability and its future business prospects, thus
26 causing the Company's common stock to be overvalued and artificially inflated at all relevant times.
27 Defendants' false portrayal of CPI, its business operations, and future prospects during the Class
28 Period resulted in Plaintiff's and other Class members' purchasing shares of the Company's common

1 stock at a disparity between their market price and their actual value, thus causing the damage
2 complained of herein.

3 **COUNT I**

4 **(Against All Defendants For Violations Of Section 10(b) Of The Exchange Act)**

5 38. Plaintiff repeats and realleges each and every allegation set forth above, and further
6 alleges as follows.

7 39. This claim is brought against Defendants with respect to the entire Class Period and on
8 behalf of the Class.

9 40. Defendants, individually and in concert, directly and indirectly, by the use of means or
10 instrumentalities of interstate commerce and/or of the mails, engaged and participated in a continuous
11 course of conduct to conceal adverse material information about the business, operations, and
12 prospects of CPI as specified herein. Defendants employed devices, schemes, and artifices to
13 defraud, while in possession of material adverse non-public information and engaged in acts,
14 practices, and a course of conduct as alleged herein in an effort to assure investors of CPI's value and
15 performance and continued substantial growth, which included the making of, or the participation in
16 the making of, untrue statements of material facts and omitting to state material facts necessary in
17 order to make the statements made about CPI and its business operations and prospects in the light of
18 the circumstances under which they were made, not misleading, at least to the extent set forth more
19 particularly herein, and engaged in transactions, practices and course of business which operated as a
20 fraud and deceit upon the purchasers of CPI securities during the Class Period.

21 41. Defendants had actual knowledge of the misrepresentations and omissions of material
22 facts set forth herein, or acted with reckless disregard for the truth in that they failed to ascertain and
23 to disclose such facts, even though such facts were available to them. Such Defendants' material
24 misrepresentations and/or omissions were done knowingly or recklessly and for the purpose and
25 effect of concealing CPI's operating condition and business prospects from the investing public and
26 supporting the artificially inflated price of its stock. As demonstrated by Defendants' misstatements
27 of the Company's business, operations, and financial condition throughout the Class Period,
28 Defendants, if they did not have actual knowledge of the misrepresentations and omissions alleged,

1 were reckless in failing to obtain such knowledge by deliberately refraining from taking those steps
2 necessary to discover whether those statements were false or misleading.

3 42. As a result of the dissemination of the materially false and misleading information and
4 failure to disclose material facts, as set forth above, the market prices of CPI securities were
5 artificially inflated during the Class Period. In ignorance of the materially false and misleading nature
6 of the reports and statements described above, Plaintiff and other members of the Class relied, to their
7 damage, on the reports and statements described above and/or on the integrity of the market prices of
8 CPI securities and the completeness and accuracy of the information disseminated to CPI investors in
9 connection with their purchases of the Company's securities.

10 43. At the times of said misrepresentations and omissions, Plaintiff and other members of
11 the Class were ignorant of their falsity, and believed them to be true. Plaintiff and other Class
12 members could not in the exercise of reasonable diligence have known the actual facts. In reliance on
13 said misrepresentations and in reliance upon the superior knowledge and expertise of Defendants and
14 on the integrity of the market, Plaintiff and other members of the Class were induced to and did
15 purchase CPI securities at artificially inflated prices. Had Plaintiff and other members of the Class
16 known the truth, they would not have taken such action.

17 44. By virtue of the foregoing, Defendants have violated Section 10(b) of the Exchange
18 Act, and Rule 10b-5 promulgated thereunder by the SEC.

19 45. Plaintiff and other members of the Class have been damaged by Defendants' violations
20 as described in this Count and seek recovery for the damages caused thereby.

21 COUNT II

22 **(Against The Individual Defendants For Violations Of Section 20(a) Of The Exchange Act)**

23 46. Plaintiff repeats and realleges each and every allegation made above and further alleges
24 as follows.

25 47. This Count is brought by Plaintiff against the Individual Defendants with respect to the
26 entire Class Period and on behalf of the Class.

27 48. By reason of their control over the operations of CPI, the Individual Defendants are
28 "controlling persons" of the Company within the meaning of Section 20(a) of the Exchange Act and

1 had the power and influence (which they exercised) to cause CPI to engage in the unlawful conduct
2 complained of herein, and could have prevented such violations from taking place but failed to do so.
3 49. Because each of the Individual Defendants is a "controlling person," as that term is
4 defined in Section 20(a) of the Exchange Act, of other persons primarily liable to Plaintiff and the
5 Class pursuant to the claims arising under Section 10(b) of the Exchange Act alleged above, each of
6 the Individual Defendants is secondarily liable for those primary violations pursuant to Section 20(a)
7 of the Exchange Act.

8 **PRAYER FOR RELIEF**

9 WHEREFORE, Plaintiff, on his own behalf and on behalf of the Class, prays for judgment as
10 follows:

- 11 A. Declaring this action to be a plaintiff class action properly maintained pursuant to Rule
12 23(a) and (b)(3) of the Federal Rules of Civil Procedure;
13 B. Awarding Plaintiff and other members of the Class damages together with interest
14 thereon;
15 C. Awarding Plaintiff and other members of the Class their costs and expenses of this
16 litigation, including reasonable attorneys' fees, accountants' fees and experts' fees, and
17 other costs and disbursements; and
18 D. Awarding Plaintiff and other members of the Class such other and further relief as may
19 be just and proper under the circumstances.

20 DATED: February 2, 2001

Respectfully submitted,

21 **GIRARD & GREEN, LLP**

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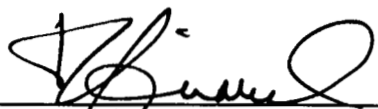
DEMAND FOR JURY TRIAL

Plaintiff hereby demands a trial by jury on all claims so triable.

DATED: February 2, 2001

Respectfully submitted,

GIRARD & GREEN, LLP

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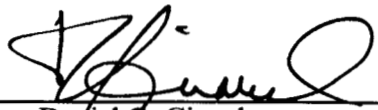
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Attorneys for Individual and Representative
Plaintiff Fred Kessler

CLASS ACTION CERTIFICATION

I declare as to the claims asserted under the federal securities laws that:

1. I have reviewed the complaint prepared by counsel in the above-captioned case and authorize the filing of the same or a similar complaint on my behalf.

2. I did not purchase the security that is the subject of the complaint at the direction of plaintiff's counsel or in order to participate in any private action arising under the federal securities laws.

3. I am willing to serve as a representative party on behalf of a class, including providing testimony at deposition and trial, if necessary.

4. During the period November 29, 2000 through February 1, 2001, I executed the following transactions relating to Critical Path securities (fill in dates and amounts of all transactions, indicating "bought" or "acquired" and "sold" and prices):

January 19, 2001, bought 1,000 shares at \$9.50 per share.

5. In the past three years, I have not sought to serve nor served as a representative party on behalf of a class in an action filed under the federal securities laws.

6. I will not accept any payment for serving as a representative party on behalf of a class beyond my pro rata share of any recovery, except such reasonable costs and expenses (including lost wages) directly relating to the representation of the Class as ordered or approved by the Court.

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct. Executed this 2d day of February, 2001.

Signed:

Fred Kessler
Fred Kessler

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02/02/2001 14:52 21258688005 SHALOV STONE BONNER PAGE 02/02