

1 Robert S. Green (State Bar No. 136183)
2 **GREEN WELLING LLP**
3 595 Market Street, Suite 2750
4 San Francisco, CA 94105
5 Telephone: (415) 477-6700
6 Facsimile: (415) 477-6710
7 cand.uscourts@classcounsel.com
8 *Liaison Counsel for Plaintiff*

9 William B. Federman
10 **FEDERMAN & SHERWOOD**
11 10205 N. Pennsylvania Ave.
12 Oklahoma City, OK 73120
13 Telephone: (405) 235-1560
14 Facsimile: (405) 239-2112
15 *Lead Counsel for Plaintiff*

16 **UNITED STATES DISTRICT COURT**
17 **NORTHERN DISTRICT OF CALIFORNIA**
18 **SAN FRANCISCO DIVISION**

19 _____)
20 ROSENBAUM CAPITAL, LLC,)
21 Plaintiff,)
22 v.)
23 JOHN E. MCNULTY, TIM STEINKOPF)
24 AND SECURE COMPUTING)
25 CORPORATION,)
26 Defendants,)
27 _____)

Case No. 07-CV-0392-SC

**PLAINTIFF'S OPPOSED
APPLICATION TO FILE
SURREPLY TO THE REPLY
MEMORANDUM IN SUPPORT
OF DEFENDANTS' MOTION TO
DISMISS FOR FAILURE TO
STATE A CLAIM**

1 Lead Plaintiff Rosenbaum Capital, LLC (“Plaintiff”) moves the Court for leave to file the
2 Plaintiff’s Opposed Application to file a Surreply to Defendants’ Reply Memorandum in Support of
3 Defendants Motion to Dismiss for Failure to State a Claim. Plaintiff’s proposed Surreply is attached
4 hereto as Exhibit 1. In support of this Application, Plaintiff states as follows:

5 1. On July 2, 2007, Plaintiff filed its Amended Complaint in this action. Plaintiff
6 alleged, among other things, that during the Class Period, Defendants mislead investors to believe
7 that Defendant Secure Computing Corporation (“Secure” or the “Company”) had fully integrated its
8 recently acquired subsidiary CyberGuard Corporation (“CyberGuard”) into Secure, that
9 CyberGuard’s the “Classic” customers were transitioning to Secure’s Sidewinder product and that
10 CyberGuard was a lucrative and beneficial acquisition for the Company. *See* Amended Complaint at
11 ¶¶19-20, 77. In reality, as set forth in Plaintiff’s Amended Complaint and as Plaintiff’s confidential
12 sources disclosed, this was simply not true. According to Plaintiff’s confidential sources, Secure and
13 the Individual Defendants knew, or in the absence of extreme recklessness should have known, that
14 the integration of CyberGuard into Secure was not completed, contrary to Defendants’
15 misrepresentations to investors and analysts. *Id.* at ¶42, ¶¶38-77. Plaintiff further alleged that
16 Defendants had no reasonable basis to believe it could meet project its revenues and earnings
17 guidance issued to analysts and investors on May 4, 2006. *Id.* at ¶35, ¶¶ 17-18, 77.

18 3. On August 16, 2007, Defendants filed their Motion to Dismiss for Failure to State a
19 Claim. Defendants, in their brief, largely ignored the alleged “integrations” misrepresentations,
20 instead, choosing to focus their attack on the financial results projections.

21 4. After Plaintiff filed its Memorandum of Law in Opposition to their Motion to Dismiss,
22 arguing and addressing both the allegedly misleading financial guidance and the “integration
23 misrepresentations, Defendants filed their Reply Memorandum in Support of Defendants’ Motion to
24 Dismiss for Failure to State a Claim on October 31, 2007. Therein, Defendants asserted, for the first
25 time, that Plaintiff had failed to allege loss causation with respect to Defendants’ misrepresentations
26 and omissions related to the integration of CyberGuard into Defendant Secure.

1 5. Plaintiff respectfully requests leave of the Court to file a surreply for the limited
2 purpose of addressing this issue which was raised for the first time in Defendants' Reply
3 Memorandum.

4 6. Plaintiff has conferred with Defendants' counsel and has been advised that Defendants
5 oppose this Application and the relief requested.

6 Accordingly, Plaintiff's Opposed Application to File Surreply to the Reply Memorandum in
7 Support of Defendants' Motion to Dismiss for Failure to State a Claim should be granted.

8 Submitted herewith is a proposed Order.

9
10 Dated: November 15, 2007

GREEN WELLING LLP

11
12 By: /s/ Robert S. Green
13 Robert S. Green

14 595 Market Street, Suite 2750
15 San Francisco, CA 94105
16 Telephone: (415) 477-6700
17 Facsimile: (415) 477-6710
18 *Liaison Counsel for Plaintiffs*

19 William B. Federman
20 **FEDERMAN & SHERWOOD**
21 10205 North Pennsylvania Ave.
22 Oklahoma City, OK 73120
23 Telephone: (405) 235-1560
24 Facsimile: (405) 239-2112
25 wfederman@aol.com

26 *Lead Counsel for Plaintiffs*
27
28

EXHIBIT 1

1 Robert S. Green (State Bar No. 136183)
2 **GREEN WELLING LLP**
3 595 Market Street, Suite 2750
4 San Francisco, CA 94105
5 Telephone: (415) 477-6700
6 Facsimile: (415) 477-6710
7 cand.uscourts@classcounsel.com

8 *Liaison Counsel for Plaintiff*

9 William B. Federman
10 **FEDERMAN & SHERWOOD**
11 10205 North Pennsylvania Ave.
12 Oklahoma City, OK 73120
13 Telephone: (405) 235-1560
14 Fax: (405) 239-2112
15 *Lead Counsel for Plaintiff*

16
17 **UNITED STATES DISTRICT COURT**
18
19 **NORTHERN DISTRICT OF CALIFORNIA**
20
21 **SAN FRANCISCO DIVISION**

22 ROSENBAUM CAPITAL, LLC,)
23 Plaintiff,) Case No. 07-CV-0392-SC
24 v.)
25 JOHN E. MCNULTY, TIM)
26 STEINKOPF AND SECURE) **PLAINTIFF'S SURREPLY TO**
27 COMPUTING CORPORATION,) **DEFENDANTS' REPLYMEMORANDUM**
28 Defendants.) **IN SUPPORT OF DEFENDANTS'**
) **MOTION TO DISMISS FOR FAILURE TO**
) **STATE A CLAIM**

1 Lead Plaintiff Rosenbaum Capital, LLC (“Plaintiff”) submits this Memorandum of Law
2 in Surreply to Defendants’ Reply Memorandum in Support of Defendants’ Motion to Dismiss for
3 Failure to State a Claim. This submission is made for the limited purpose of addressing an issue
4 raised for the first time in Defendants’ Reply Memorandum: Defendants’ contention that
5 Plaintiff has failed to allege loss causation with respect to Defendants’ misrepresentations and
6 omissions related to the integration of CyberGuard Corporation (“CyberGuard”) into Defendant
7 Secure Computing, Inc. (“Secure” or the “Company”). Specifically, Defendants contend that
8 Plaintiff “can point to no corrective disclosures in their Complaint relating to the supposed
9 misrepresentations about the CyberGuard integration, negating any attempt to plead loss
10 causation for these statements. Defendants’ Reply at 2, 13. Defendants are simply wrong.

11 **Plaintiff Has Sufficiently Alleged Loss Causation with Respect to Its “Integration” Claims**

12 During the Class Period, as forth in Plaintiff’s Opposition Brief, Defendants, through a
13 series of false and misleading statements, misled investors to believe that Secure and
14 CyberGuard were fully integrated into one company, that CyberGuard’s “The Classic” customers
15 were transitioning to Secure’s Sidewinder product and that CyberGuard was a lucrative and
16 beneficial acquisition for the Company. ¶¶19-20, 77.¹ In reality, as further set forth in Plaintiff’s
17 Opposition Brief, and as Plaintiff’s confidential sources disclosed, this was simply not true.
18 According to Plaintiff’s Confidential Sources, Secure and the Individual Defendants knew, or in
19 the absence of extreme recklessness should have known, that the integration of CyberGuard into
20 Secure was not completed, contrary to Defendants’ representations to investors and analysts
21 during the Company’s May 4, 2006 conference call. ¶42; see ¶¶38-77. The failure to disclose
22 this, and other information, made the Defendants’ Class Period statements false and misleading,
23 ¶77; and was also, as alleged by Plaintiff, a contributing cause of Plaintiff’s losses. See ¶¶23,
24 27-28.

25
26
27 ¹ Citations to the Amended Complaint are referenced as “¶ ___” or “¶¶ ___”.

1 To plead loss causation a Section 10(b) complaint need only make a “short, plain
2 statement showing that “the pleader is entitled to relief. *Dura Pharmaceuticals, Inc. v.*
3 *Broudo*, 544 U.S. 336, 345 (2005) (quoting F.R.C.P.8(a)); *Plumbers & Pipefitters Local 572*
4 *Pension Fund v. Cisco Systems, Inc.*, 411 F. Supp. 2d 1172, 1178 (N.D. Cal. 2005). The
5 complaint must give the defendant “fair notice of what the plaintiffs’ claim is and the grounds
6 upon which it rests. *Id.* (quoting *Dura*, 125 S.Ct. at 1634). To satisfy this Rule 8 pleading
7 standard the complaint need only “provide the defendant with *some indication* of the loss and the
8 causal connection that plaintiff has in mind. *Cisco*, 411 F.Supp.2d at 1025 (quoting *Dura*,
9 125 S.Ct. at 1634) (emphasis added by the district court).

10 One way a plaintiff can allege loss causation is by pleading that the truth was revealed
11 through a corrective disclosure or series of corrective disclosures. *See In re Enron, Sec., Driv.*
12 *& “ERISA” Litigation*, 439 F. Supp. 2d Gaz, 701 (S.D. Tex 2006) (“The pleading of a single
13 formal corrective measure is not necessary after *Dura*). To be corrective, a disclosure need
14 only partially disclose the purported fraud. *See, e.g., Dura*, 544 U.S. at 342 (a complete
15 corrective disclosure is not required to precede a stock’s decline for loss causation purposes). A
16 plaintiff, moreover, “is not necessarily precluded from establishing loss causation where a
17 corrective disclosure does not, on its face, specifically identify or explicitly correct a previous
18 representation, or expressly disclose the particular fraudulent scheme plaintiff alleges. *In re*
19 *Motorola Sec. Litig.*, 2007 WL 487738 at *34 (D. Ill. Feb. 8, 2007) (loss causation adequately
20 alleged under *Dura* even where some of the partial disclosures did not directly implicate the
21 fraud alleged); *see also In re Bradley Pharmaceuticals Inc. Sec. Litig.*, 421 F. Supp. 2d 822, 828
22 (D.N.J. 2006). The plaintiff is also not required to show “that a misrepresentation was the *sole*
23 reason for the investments decline in value in order to establish loss causation. *In re Daou*
24 *Systems, Inc.*, 411 F. 3d 1006, 1025 (9th Cir. 2005) (quoting *Robbins v. Koger Propes. Inc.*,
25 116 F.3d 1441, 1447 n. 5 (11th Cir. 1997), *cert. denied*, 546 v.s. 1172 (2006), (emphasis supplied
26 by the Court). “[A]s long as the misrepresentation is one substantial cause of the investments’
27

1 decline in value, other contributing forces will not bar recovery under the loss causation
2 requirement but will play a role “in determining recoverable damages. *Id.*

3 In *Daou*, plaintiff contended that Daou fraudulently inflated the price of its stock by
4 reporting revenues before they were earned in violation of GAAP and the company’s own
5 revenue recognition policies. 411 F. 3d at 1012. Specifically, plaintiffs alleged the company
6 employed an accounting method known as the percentage of completion (“POC”) method which
7 is primarily used to account for progress of long term projects. *Id.* Under this method, revenue
8 from these projects can only be recognized based on the percentage of labor costs incurred to
9 date compared to the total estimated labor costs for the project. *Id.* at 1012-13. Plaintiffs
10 alleged, however, that defendants would prematurely recognize revenue in contravention of the
11 POC method, without regard to labor costs incurred or estimated. *Id.* at 1013, 1017.

12 The district court held that the plaintiffs had failed to allege “loss causation, finding that
13 “Daou’s improper use of the POC method was not linked to the decline in Daou’s share price:

14
15 It is undisputed that Daou’s 3Q98 financial results were dismal, and that this led
16 to the precipitous drop in the Company’s stock value. However, in the TAC,
17 Plaintiffs have not adequately been able to link the decline in share price to any
18 purported improper revenue recognition by Defendants. Plaintiffs point to the fact
19 that market analysts questioned whether Defendants had been “cooking Daou’s
20 books after the 3Q98 results were revealed, but this is merely speculation.
21 Notably, the TAC does not allege that there were any negative public statements,
22 announcements or disclosures at the time the stock price dropped that Defendants
23 were engaged in improper accounting practices.

24 *Id.* at 1025-1026.

25 The Ninth Circuit disagreed:

26 An independent assessment of the TAC, however, indicates that the price of
27 Daou’s stock fell precipitously after defendants began to reveal figures showing
28 the company’s true financial condition. On August 13, 1998, Daou’ stock was
trading at \$18.50 per share. The TAC alleges that “beginning in August 1998,
defendants revealed that Daou’s operating expenses and margins were
deteriorating and, on October 28, 1998, defendants revealed that Daou had
dramatically missed its projected 3Q98 earnings and would have to report a loss
of \$0.17 a share. Notably, the TAC alleges that “Defendants further revealed
that the Company’s rapidly escalating work in progress account represented
over \$10 million dollars in unbilled receivables – *the direct result of*

1 *prematurely recognizing revenue.* (emphasis added). ... Finally, as the district
2 court also noted, the TAC anonymously quotes an analyst who allegedly stated,
3 “[w]hen you say one thing on the conference call and report something
different on the 10-Q, that raises concern.... You have got to question whether
they are manufacturing earnings.”

4 *Id.* at 1026 (emphasis supplied by the court). The Court found that the complaint sufficiently
5 alleged loss causation because the complaint provided the defendant with “some indication that
6 the drop in Daou’s stock price was related to Daou’s financial misstatements. *Id.* The
7 complaint’s assertion that a steep drop in Daou’s stock price followed the revelation of Daou’s
8 true financial situation was sufficient to enable the complaint to survive a motion to dismiss
9 under F.R.C.P. 12(b)(6). *Id.* at 1027.

10 *In Daou*, the fraudulent misrepresentations related to defendants’ misapplication of the
11 percentage of labor cost method of recognizing revenues by deliberately overestimating the
12 amount of labor performed on contracts. There was never any corrective disclosure as such in
13 which defendants acknowledged to the market that this was in fact what had transpired followed
14 by a drop in the price of the stock. Rather, there were allegations that poor financial results in
15 subsequent periods, that were disclosed and led to a drop in the price of the stock, resulted from
16 the premature recognition of revenue in earlier periods.

17 Here, Plaintiff has alleged what was found to be sufficient to allege loss causation in
18 *Daou*, and more. Plaintiff has alleged that Secure’s failure to achieve integration of CyberGuard
19 into Secure, contrary to Defendants’ express representations, led to Secure’s poor financial
20 results that were reported in the second quarter of 2006, which in turn partially led to the decline
21 in Secure’s stock price. Plaintiff has also alleged, however, that the decline in Secure’s stock
22 price was also caused by Defendants’ specific class period ending partial disclosures concerning
23 the Company’s failure to achieve integration of CyberGuard into Secure.

24 For instance during the question and answer session of the July 11, 2006 conference
25 call -- in which the truth was finally disclosed -- this exchange ensued: William Becklean, an
26 analyst for Oppenheimer & Co. Inc., asked, “To what extent is this related to the integration of
27 CyberGuard and confusion on the channel, sales force, products, whatever? ¶23. McNulty replied,

1 “That would be an easy excuse, Bill. Subject to the analysis, I’ll make a statement that I don’t think
2 that was the reason. Obviously there’s probably some deals that we can point to and say they slipped,
3 but that -- we need the two weeks to – ¶23. But Steinkopf interrupted McNulty and stated, “However,
4 John will agree with this next comment. It does appear to us, and again, we have to do a little bit more
5 analysis, that the length of time to close CyberGuard transaction, so we expected to close November. It
6 slipped into January. Those additional 60 days approximately seems to have really hurt our momentum
7 with those product lines...[b]ut it appears that we may be suffering a little bit more deal freeze and
8 momentum slowdown...than we realized last quarter. ¶23. In response to another analyst’s,
9 Katherine Egbert’s, question, “You bought CyberGuard and then you missed the March quarter, and
10 now you missed again in June and you’re attempting to buy CipherTrust. What gives investors
11 confidence that this cycle is not going to repeat itself?, ¶27, McNulty replied:

12
13 The CyberGuard acquisition overlaps our product substantially. Because of their
14 acquisition, they had not integrated Webwasher. They had not integrated
15 SnapGear or a couple other little companies they acquired. And the degree of
16 difficulty for that acquisition given multiple locations, multiple bookkeeping
17 systems and order entry systems for us was much, much harder than we anticipate
18 CipherTrust to be the thing that Tim brought up relative to the delay in closing
19 the CyberGuard transaction caused us to stall certain activity in the channel and in
20 the general marketplace.

21 ¶ 27.

22 Following these, and the Company’s other July 11, 2006 disclosures, including the revelation
23 of Secure’s disappointing second quarter 2006 financial results, the price of Secure stock plummeted
24 38% from \$8.07 per share on July 11, 2006 to \$4.99 per share on July 12, 2006 on very heavy trading
25 volume, ¶29; and Jefferies & Company Inc. analyst Katherine Egbert cut her rating to
26 “Underperform from “Hold and slashed her target price to \$5 from \$11, noting among other
27 things that Secure’s recent trend of missing its revenue guidance indicates the Company is facing
28 troubles with its core businesses. ¶30. Additional partial disclosures concerning the failure to
achieve integration of Secure and CyberGuard and its effect on the Company’s second quarter
2006 financial results followed on July 26, 2006. ¶¶32-34.

1 The allegations of the Amended Complaint are more than sufficient to withstand
 2 Defendants' Rule 12(b)(6) motion concerning loss causation with respect to Defendants'
 3 "integration misrepresentations. *See Daou*, 411 F.3d at 1025-27; *In re InfoSonics Sec. Litig.*,
 4 2007 WL 2301757 at *3, 13 (S.D. Cal. Aug. 7, 2007); *see also In re Omnivision Technologies,*
 5 *Inc.*, 2005 WL 1867717 at *5 (N.D. Cal. July 29, 2005). Plaintiff is not required to show that a
 6 misrepresentation is a sole reason for the investment's decline in value in order to show loss
 7 causation. *Daou*, 411 F. 3d 1006, 1025; *In re High Energy Technologies, Inc.*, -- *Sec. Litig.*,
 8 2005 WL 3071250 at *4 (C.D. Cal. Oct. 25, 2005). To the extent that Defendants can undermine
 9 the causal link with other facts and data, such efforts may lead to a reduction in Plaintiff's
 10 recoverable damages; but Plaintiff has alleged loss causation sufficiently to survive Defendants'
 11 Motion to Dismiss. *Highenergy*, 2005 WL 3071250 at *4. Moreover, even if Plaintiff's
 12 Amended Complaint were somehow technically deficient for failure to summarily state that the
 13 "integration misrepresentations caused Plaintiff's losses, as Defendants' seem to suggest,
 14 Defendants' Reply at 13, any such defect can be easily cured through amendment.

15 Dated: November 15, 2007

Respectfully submitted,

GREEN WELLING LLP

18 By: _____
Robert S. Green

19 595 Market Street, Suite 2750
20 San Francisco, CA 94105
21 Telephone: (415) 477-6700
Facsimile: (415) 477-6710

22 Liaison Counsel for Plaintiff

23 William B. Federman
24 **FEDERMAN & SHERWOOD**
25 10205 N. Pennsylvania Avenue
26 Oklahoma City, OK 73120
Telephone: (405) 235-1560
Facsimile: (405) 235-2112

27 Lead Counsel for Plaintiff

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4
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21
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24
25
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Marc Henzel
LAW OFFICES OF MARC S. HENZEL
273 Montgomery Ave., Suite 202
Bala Cynwyd, PA 19004
Telephone: (610) 660-8000
Facsimile: (610) 660-8080

Additional Counsel for Plaintiff

1
2
3
4
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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN FRANCISCO DIVISION

ROSENBAUM CAPITAL, LLC,
Plaintiff,
v.
JOHN E. MCNULTY, TIM STEINKOPF
AND SECURE COMPUTING
CORPORATION,
Defendants,

Case No. 07-CV-0392-SC

**[PROPOSED] ORDER GRANTING
PLAINTIFF'S OPPOSED APPLICATION
TO FILE SURREPLY TO THE REPLY
MEMORANDUM IN SUPPORT OF
DEFENDANTS' MOTION TO DISMISS
FOR FAILURE TO STATE A CLAIM**

1 Plaintiff's Opposed Application to File Surreply to the Reply Memorandum in Support of
2 Defendants' Motion to Dismiss for Failure to State a Claim is granted. Plaintiff shall file its Surreply
3 to Defendants' Reply Memorandum in Support of Defendants' Motion to Dismiss for Failure to State
4 a Claim within three (3) court days of the date of this Order.

5
6 Dated: November _____, 2007

7 JUDGE OF THE UNITED STATES
DISTRICT COURT

8
9
10 Submitted by:

11 Robert S. Green (State Bar No. 136183)

12 **GREEN WELLING LLP**

13 595 Market Street, Suite 2750

14 San Francisco, CA 94105

15 Telephone: (415) 477-6700

16 Facsimile: (415) 477-6710

17 cand.uscourts@classcounsel.com

18 *Liaison Counsel for Plaintiff*

19 William B. Federman

20 **FEDERMAN & SHERWOOD**

21 10205 N. Pennsylvania Ave.

22 Oklahoma City, OK 73120

23 Telephone: (405) 235-1560

24 Facsimile: (405) 239-2112

25 *Lead Counsel for Plaintiff*