

HONORABLE MARSHA J. PECHMAN

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UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON AT SEATTLE

SUE ELLEN DUMDIE, Individually and
on Behalf of all Others Similarly Situated,

Lead
Plaintiff,

v.

WM TRUST I, WM TRUST II, WM
STRATEGIC ASSET MANAGEMENT
PORTFOLIOS, LLC, WM ADVISORS,
INC., WM FUNDS DISTRIBUTOR, INC.,
WILLIAM G. PAPESH, DANIEL L.
PAVELICH, RICHARD C. YANCY,
KRISTIANNE BLAKE, EDGE ASSET
MANAGEMENT, INC., PRINCIPAL
FINANCIAL GROUP, INC., PRINCIPAL
INVESTORS FUND, INC., PRINCIPAL
FUNDS DISTRIBUTOR, INC.,

Defendants.

No. C-08-1251 MJP

**DEFENDANTS' MOTION TO DISMISS
THE SECOND AMENDED CLASS ACTION
COMPLAINT**

Noted for Issue: March 27, 2009
Action filed: August 20, 2008

MOTION TO DISMISS
No. C-08-1251 MJP


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1 **I. INTRODUCTION**

2 The centerpiece of the Second Amended Complaint (“SAC” or “Complaint”) filed by
 3 Lead Plaintiff Sue Ellen Dumdie (“Ms. Dumdie” or “Plaintiff”) is the claim that Defendants
 4 perpetrated a fraud because they merely disclosed that additional compensation “*may*” be made
 5 to broker-dealers in connection with certain mutual fund sales, when arrangements for those
 6 payments were already in place. Even if Plaintiff had accurately described Defendants’
 7 disclosures on this subject (which she did not), her claim amounts to what the Sixth Circuit
 8 Court of Appeals—the only federal appellate court that has addressed identical claims—
 9 dismissed as a “semantic quibble.” *Benzon v. Morgan Stanley Distrib., Inc.*, 420 F.3d 598, 612
 10 (6th Cir. 2005). Worse yet for Plaintiff’s case, the SEC filings by the mutual funds at issue in
 11 the WM Group of Funds (the “Funds”) *publicly disclosed* to Ms. Dumdie and the putative class¹
 12 the dealer agreements in use by the Funds, which set forth in detail the very fee-sharing
 13 arrangements that Ms. Dumdie complains were *not* disclosed. Those dealer agreements also
 14 specified that the fee-sharing arrangements could be changed or terminated on short notice,
 15 making the word “may” particularly appropriate to describe the arrangements in the Funds’
 16 class-period Prospectuses and Registration Statements. This is not the stuff of which a securities
 17 fraud claim is made.

18 Plaintiff pursues a second, equally vacuous theory of securities fraud: alleging that the
 19 Advisor Paid Fee (“APF”) paid to participating broker-dealers to encourage sale of the Funds
 20 was not 50 basis points as disclosed, but was in fact 75 basis points. This allegation is based
 21 entirely on Plaintiff’s untenable reading of a single marketing document directed to the broker-
 22 dealer community that states that the “*total fees*” that broker-dealers could earn by selling the
 23 Funds was 75 basis points. Since broker-dealers could earn 25 basis points in 12b-1 fees from
 24 WM Distributor and the 50 basis points in APF fees from WM Advisors, the document relied on

25 ¹ The SAC defines the putative class as: “All persons or entities that purchased or otherwise acquired shares, units
 26 or likewise interests in any of the WM Funds (including through the reinvestment of Fund dividends), between
 March 1, 2002, through December 31, 2006, inclusive.” (SAC ¶ 3 n.3.)

1 by Ms. Dumdie is fully consistent with Defendants' public disclosures of the particular fees
2 available to broker-dealers. The marketing document does not support Plaintiff's allegation of
3 fraud. Ms. Dumdie alleges nothing else in support of her speculation that the APF was 75 basis
4 points. Mere speculation does not meet the pleading requirements for securities fraud.

5 The SAC must be dismissed for at least several reasons. First, and most fundamentally,
6 it is black letter law—and common sense—that a material misstatement/omission claim cannot
7 be based on information that was neither misstated nor omitted. The SAC fails to allege a
8 material misstatement or omission because the Funds adequately, and repeatedly, disclosed the
9 APF and revenue sharing program. Ms. Dumdie admits that she and the putative class received
10 the Funds' Prospectuses during the class period, and is therefore on inquiry notice of both their
11 contents and the related Registration Statements filed with the SEC.

12 Second, the SAC does not—and cannot—plead scienter with particularity. Third, the
13 SAC fails to adequately allege reliance (“transaction causation”) by either Ms. Dumdie or the
14 putative class on the alleged misstatements. Fourth, the SAC does not establish a causal link
15 between alleged damages and information that investors knew (or should have known) at the
16 time they invested (i.e., “loss causation”). Fifth, because a reasonably diligent investor would
17 have known about the incentive payments of which Ms. Dumdie now complains, investors were
18 on inquiry notice of these claims in 2004. This action was filed on August 20, 2008, years after
19 the one- and two-year notice-inquiry-based statutes of limitations had already expired. (Many of
20 Ms. Dumdie's claims are also barred by statutes of repose.) Sixth, Ms. Dumdie never purchased
21 half of the Funds challenged in the Complaint, and therefore has no standing to assert claims
22 relating to them. Moreover, because the APF was only paid on the WM Portfolios Funds,
23 purchasers of the other Funds suffered no injury and therefore lack standing. Finally, the SAC's
24 control person liability claims fail because the SAC does not adequately state a claim for primary
25 liability and inadequately alleges control. In sum, the Complaint is tardy and baseless, and it
26 must be dismissed.

1 **II. STATEMENT OF FACTS**²

2 **A. Parties**

3 During the putative class period, Defendants WM Trust I, WM Trust II, and WM
4 Strategic Asset Management Portfolios, LLC (collectively, the “Registrants”) were registered
5 with the U.S. Securities and Exchange Commission (“SEC”) as open-end management
6 investment companies under the Investment Company Act of 1940. The Registrants issued
7 several series of shares reflecting specific investment strategies, commonly known as mutual
8 funds.³ These included the Funds allegedly purchased by Plaintiff. (SAC ¶ 16.)

9 Defendants WM Advisors, Inc. (“WM Advisors”) and WM Funds Distributor, Inc.
10 (“WM Distributor”) provided investment management and distribution services, respectively, to
11 the Funds. (SAC ¶ 21.)

12 After the close of the alleged class period, a subsidiary of Defendant Principal Financial
13 Group, Inc. acquired WM Advisors and WM Distributor, and renamed them Edge Asset
14 Management, Inc. and Principal Funds Distributor, Inc., respectively. Thereafter, in January
15 2007, all assets of the Funds were transferred to Defendant Principal Investors Fund, Inc., which
16 is a registered investment company, and all shareholders of the Funds became shareholders of
17 Principal Investors Fund, Inc.⁴ (SAC ¶¶ 82–83; *see* Request for Judicial Notice (“RJN”) and
18 Declaration of Andrew R. Escobar (“Escobar Decl.”), Ex. A at 3-4.)

19 The SAC names four individual defendants: William G. Papesh, the President, CEO and
20 Director of WM Trust I, WM Trust II, WM Portfolios, WM Advisors and WM Distributor
21 during the class period; Daniel Pavelich, Chairperson of the WM Funds Audit Committee during

22 ² This motion is based on the facts alleged in the SAC and those of which the Court may take judicial notice. *See, e.g., In re Silicon Graphics, Inc. Sec. Litig.*, 183 F.3d 970, 986 (9th Cir. 1999).

23 ³ The Funds included Money Market, Tax-Exempt Money Market, U.S. Government Securities, Income, High
24 Yield, Tax-Exempt Bond, REIT, Small Cap Value, Equity Income, Growth & Income, West Coast Equity, Mid Cap
25 Stock, California Money, Short Term Income, California Municipal, California Insured Intermediate Municipal,
26 Growth, International Growth, Small Cap Growth, Strategic Growth, Conservative Growth, Balanced, Conservative
Balanced, and Flexible Income. (SAC ¶ 1 n 2.)

⁴ WM Trust I, WM Trust II, and WM Strategic Asset Management Portfolios LLC have all been dissolved. (*See*
Escobar Decl., Exs. B–D.)

1 the class period; Richard Yancy, the Lead Trustee on the Funds' common Board of Trustees
2 during the class period; and Kristianne Blake, the Chairperson of the WM Operations and
3 Distribution Committee during the class period (Defendants Pavelich, Yancy, and Blake are
4 hereinafter collectively referred to as the "Independent Directors"). (SAC ¶¶ 22–25.)

5 The SAC alleges that, between March 1, 2002, and December 31, 2006, Ms. Dumdie
6 purchased and sold some but not all of the twenty-four Funds. (SAC ¶ 16.)

7 **B. The Zapien Action**

8 The Second Amended Complaint has many antecedents. On February 28, 2007, plaintiff
9 Luz Zapien, represented by Finklestein & Krinsk, one of the firms representing Plaintiff in this
10 action, filed a class action complaint in the United States District Court for the Southern District
11 of California. As in this case, the *Zapien* action alleged that investment advisors for the Funds
12 were making inadequately disclosed payments to the broker-dealers selling those funds, which
13 allegedly created an undisclosed conflict of interest. (SAC ¶¶ 86–87.) Defendants⁵ moved to
14 dismiss the *Zapien* first amended complaint for lack of standing, violation of the statute of
15 limitations, and failure to plead with particularity the required elements of material
16 misstatement, scienter, and loss causation. *Zapien v. Washington Mutual, Inc.*, No. 07-CV-385
17 DMS, 2008 U.S. Dist. LEXIS 67137, at *5 (S.D. Cal. June 17, 2008). Judge Sabraw dismissed
18 the complaint without prejudice for lack of standing on January 17, 2008, without addressing the
19 remaining defects in Zapien's claims. *Id.*, at *5.

20 On February 6, 2008, Zapien filed a second amended complaint. *Id.*, at *6. Since the
21 second amended complaint did not cure the standing and statute of limitations problems, let
22 alone the other shortcomings of its predecessor, defendants obtained permission to bifurcate their
23 motion to dismiss and to focus first on standing and the statute of limitations. (*Id.*) Judge
24 Sabraw granted the defendants' motion for lack of standing on June 17, 2008, dismissing the
25 *Zapien* action without leave to amend. *Id.*, at *9–11. Ms. Zapien moved for reconsideration on

26 ⁵ Neither Mr. Papesh nor the Independent Directors were defendants in the *Zapien* action.

1 July 1, 2008, and the court denied that motion on August 19, 2008. *Zapien v. Washington*
2 *Mutual, Inc.*, No. 07-CV-385 DMS, 2008 U.S. Dist. LEXIS 67136 (S.D. Cal. Aug. 19, 2008).
3 Ms. Zapien then filed a notice of appeal, which is currently pending before the Ninth Circuit
4 Court of Appeals. (SAC ¶ 90.)

5 **C. This Action**

6 On August 20, 2008—more than two months after the *Zapien* action was dismissed with
7 prejudice—original named plaintiff June Robinson filed this putative class action lawsuit.⁶
8 (Docket Entry (“D.E.”) No. 1.) Ms. Robinson also filed a Notice of Related Case, because every
9 Defendant named in the *Zapien* action was originally named in this litigation and both actions
10 raise the same basic allegations.

11 Ms. Robinson avoided an automatic stay of this action by filing the First Amended
12 Complaint on September 26, 2008, which dropped defendants Washington Mutual, Inc.
13 (“WMI”) and WM Financial Services (“WMFS”) from this action on the same day WMI filed
14 for bankruptcy. (D.E. Nos. 5, 22.) After the Court appointed Ms. Dumdie as the Lead Plaintiff
15 (D.E. No. 29), she filed the Second Amended Complaint on December 12, 2008 (D.E. No. 39).
16 The SAC is the subject of this motion to dismiss.

17 At its heart, the SAC alleges two material misrepresentations in the Funds’ five
18 prospectuses from 2002 through 2006. First, like its five predecessors, the SAC claims that
19 Defendants failed to disclose the revenue-sharing arrangement because the public filings only
20 said that such arrangements “may” exist. (SAC ¶ 10.) Second, Ms. Dumdie claims that
21 Defendants misstated the size of the payments to broker-dealers. (*Id.* ¶ 4.) Based on these
22 allegations, the SAC asserts five claims under Sections 11, 12(a), and 15 of the Securities Act,
23 and Sections 10(b) and 20(a) of the Exchange Act.

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⁶ Plaintiff Robinson was also represented by counsel for Ms. Dumdie.

1 **III. LEGAL STANDARD ON MOTION TO DISMISS**

2 Under Rule 12(b)(6), a complaint must be dismissed when it fails to plead sufficient facts
 3 stating a claim to relief that is “plausible on its face.”⁷ *See Bell Atlantic Corp. v. Twombly*, 127
 4 S. Ct. 1555, 1974 (2007) (dismissing complaint where “plaintiffs have not nudged their claims
 5 across the line from conceivable to plausible”). In ruling on a 12(b)(6) motion, the court may
 6 consider the facts alleged in the complaint, documents attached to or specifically referenced
 7 within the complaint, and matters of which the court may take judicial notice. *See United States*
 8 *v. Ritchie*, 342 F.3d 903, 908 (9th Cir. 2003). Conclusory allegations and unwarranted
 9 inferences are insufficient to defeat a motion to dismiss. *Warren v. Fox Family Worldwide, Inc.*,
 10 328 F.3d 1136, 1139 (9th Cir. 2003). Moreover, a court is not required to accept facts in the
 11 complaint that contradict facts in documents referred to in the complaint. *Steckman v. Hart*
 12 *Brewing Inc.*, 143 F.3d 1293, 1295–96 (9th Cir. 1998).

13 Ms. Dumdie’s securities fraud claims are subject to the heightened pleading requirements
 14 of the Private Securities Litigation Reform Act (“PSLRA”) and Federal Rule of Civil Procedure
 15 9(b). To state a claim that is plausible on its face, her complaint must “state with particularity
 16 both the facts constituting the alleged violation, and the facts evidencing scienter.”⁸ *Tellabs, Inc.*
 17 *v. Makor Issues & Rights, Ltd., et al.*, 127 S. Ct. 2499, 2504 (2007); *see also Zucco Partners*
 18 *LLC v. Digimarc Corp.*, ___ F.3d ___, No. 06-35758, 2009 WL 57081, at *5 (9th Cir. Jan. 12,
 19 2009). The SAC utterly fails to meet this standard and its claims must be dismissed.

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 21
 22 ⁷ In addition to Rule 12(b)(6), Defendants also move to dismiss for lack of jurisdiction over the subject matter of this
 23 case as a result of Ms. Dumdie’s lack of standing to sue under Article III of the Constitution because she did not
 own half of the mutual funds in question.

24 ⁸ Despite the SAC’s disclaimers to the contrary (SAC ¶¶ 98, 106, 115), its Securities Act claims are subject to the
 25 heightened pleading requirements of Rule 9(b). *See Falkowski v. Imation Corp.*, 309 F.3d 1123, 1133-34 (9th Cir.
 26 2002); *In re Stac Elec. Sec. Litig.*, 89 F.3d 1399, 1404-05 & n.2 (9th Cir. 1996) (applying Rule 9(b) to Securities Act
 claims that sound in fraud); *Fouad v. Isilon Sys., Inc.*, No. C07-1764 MJP, 2008 WL 5412397, at *3 (W.D. Wash.
 Dec. 29, 2008) (holding that Section 11 and Section 12 claims that necessarily allege fraudulent conduct are subject
 to Rule 9(b)).

1 **IV. THE SAC FAILS TO PLEAD A MATERIAL MISSTATEMENT OR OMISSION**

2 The SAC does not sufficiently allege the essential element of a material misstatement or
3 omission by Defendants. Nor can she do so in light of the facts actually disclosed by the Funds.
4 The securities laws do not mandate disclosure of the additional details concerning compensation
5 to broker-dealers that Ms. Dumdie alleges should have been set forth in the Prospectuses at
6 issue. As such, to assert a claim under either the Securities Act or the Exchange Act, the SAC
7 must allege *particular facts* concerning the omitted details, showing that their omission rendered
8 the affirmative statements in the 2002 through 2006 Prospectuses materially misleading. *See*
9 *Benzon*, 420 F.3d at 611–12; *In re Solomon Smith Barney Mutual Fund Fees Litig.*, 441 F. Supp.
10 2d 579, 587 (S.D.N.Y. July 26, 2006); *see also In re Merrill Lynch & Co., Inc. Research Reports*
11 *Sec. Litig.*, 289 F. Supp. 2d 429, 434 (S.D.N.Y. 2003). It has failed to do so. The disclosures in
12 the Registration Statements show that the Prospectuses were not misleading, much less
13 materially so.

14 The SAC alleges two categories of misrepresentations. First, the SAC claims that the
15 Funds' Prospectuses provided inadequate disclosure when they stated that the investment
16 advisors "may" make payments to broker-dealers when, in fact, WM Advisors and WM
17 Distributor had already entered into some revenue-sharing arrangements with broker-dealers.
18 (SAC ¶ 10.) This claim fails because every one of the Funds' Registration Statements (which
19 included that year's Prospectus) adequately disclosed the revenue-sharing arrangement, even
20 attaching or incorporating a form of broker-dealer agreement with the specific terms of the
21 arrangement.

22 Second, the SAC claims that the Funds' Prospectuses and Registration Statements "never
23 publicly disclosed the fact that the APF was 75 Bps instead of the 50 Bps as represented by the
24 Registrants in the Prospectuses." (*See, e.g., SAC* ¶¶ 57, 61.) As discussed below, this argument
25 fails to meet the pleading standard for fraud claims because the Registration Statements
26 accurately disclosed the size of the payments to broker-dealers (50 Bps). Ms. Dumdie's claims

1 to the contrary are premised entirely on a single marketing document that does not support Ms.
2 Dumdie's reading that the APF was 75 Bps.

3 **A. There Is No Duty to Disclose the Allegedly Omitted Information**

4 Mutual funds, also known as Open-Ended Management Investment Companies, must use
5 SEC Form N-1A to register under the Investment Company Act of 1940 and offer shares for sale
6 under the Securities Act. (*Registration Form Used by Open-Ended Management Investment*
7 *Cos.*, SEC Release Nos. 33-7512, 34-39748, 63 Fed. Reg. 13916, 13916 (Mar. 23, 1998),
8 attached as Escobar Decl., Ex. E at 2, 4-5.) This form provides the federal requirements for the
9 information that must be disclosed in a mutual fund's registration statement, which includes its
10 prospectus and its statement of additional information ("SAI"). (*Id.* at 4-5.) Moreover, Form
11 N-1A was designed by the SEC to delineate those disclosures that are material to investors in
12 making their investment decisions *without* overwhelming them with less essential information.
13 (*Id.* at 2-4.)

14 Ms. Dumdie does *not* allege that any of the Registration Statements or Prospectuses cited
15 in the SAC failed to comply with the disclosure obligations set forth by the SEC in Form N-1A.
16 And aside from her unsupported claim that the APF was 75 Bps,⁹ she does not claim that the
17 class period Registration Statements or Prospectuses omitted any of the total costs borne by
18 investors in connection with the purchase, sale, or holding of Fund shares. There is no question
19 that the Prospectuses disclosed in detail the total management and distribution fees charged
20 against the Funds by WM Advisors and WM Distributor, respectively. (*See, e.g.*, Escobar Decl.,
21 Ex. F at 5-14.) There is also no question that the SEC's Form N-1A does not require disclosure
22 of the information Ms. Dumdie alleges was improperly omitted from the Prospectuses she
23 alleges to be false. *See In re Morgan Stanley & Van Kampen Mutual Fund Sec. Litig.*, No. 03
24 Civ. 8208 RO, 2006 WL 1008138, at *7 (S.D.N.Y. Apr. 18, 2006). Indeed, the Director of the

25 _____
26 ⁹ Ms. Dumdie's argument that the APF was 75 Bps and was not adequately disclosed in the Funds' public filings is
addressed in Section IV.C, *infra*.

1 SEC's Division of Investment Management expressly confirmed this in testimony before
 2 Congress in 2003, when the SEC was considering legislation (never enacted) to mandate further
 3 disclosure. (Paul Roye, *Testimony Concerning the Mutual Funds Integrity and Fee*
 4 *Transparency Act of 2003*, at 6 (June 18, 2003), available at
 5 www.sec.gov/news/testimony/061803tspfr.htm (“Revenue-sharing payments are not a fund
 6 expense because they are made from the adviser’s own resources, rather than fund assets. As a
 7 result, mutual funds are not required to disclose these payments.”), attached at Escobar Decl.,
 8 Ex. G at 7.) “The current SEC regulations impose no duty on defendants to disclose the
 9 allocation of broker compensation. . . . [Form N-1A] does not require disclosure of how
 10 differential compensation is allocated. Nor does it require disclosure of sales contests or
 11 management bonuses.” *Morgan Stanley*, 2006 WL 1008138, at *7; *see also Benzon*, 420 F.3d at
 12 612 (“Current SEC regulations, including Form N1-A, do not impose a disclosure obligation
 13 with respect to broker compensation.”); *Hoffman v. UBS-AG*, No. 05 Civ. 6817 (LBS), 2008 WL
 14 4684168, at *6 (S.D.N.Y. Oct. 22, 2008) (dismissing fraud claims premised on failure to disclose
 15 compensation paid to brokers in excess of 12b-1 fees where defendant’s prospectus disclosed the
 16 types of additional compensation that “may be spent” on brokers). In short, Ms. Dumdie cannot
 17 allege, as a basis for either her Securities Act or her Exchange Act claims, that the Funds had a
 18 duty to disclose the allegedly omitted information in the Registration Statement or Prospectus.¹⁰

19
 20
 21 ¹⁰ As referenced in the SAC, the SEC has *proposed* a rule that would have changed the disclosure requirements for
 22 revenue-sharing programs. (*See Confirmation Requirements and Point of Sale Disclosure Requirements for*
 23 *Transactions in Certain Mutual Funds and Other Securities, and Other Confirmation Requirement Amendments,*
 24 *and Amendments to Registration From for Mutual Funds*, Release Nos. 33-8358, 34-49148, IC-26341, 59 Fed. Reg.
 25 6438 (Feb. 10, 2004) (cited in the SAC ¶ 12) attached at Escobar Decl., Ex. H.) This was merely a proposed rule
 26 during the entire Class Period, and remains so today. “Proposed rules that have yet to be adopted have no force at
 law. The possible imposition of a duty of disclosure after the fact does not support a cognizable securities fraud
 claim.” *In re Merrill Lynch & Co., Inc. Research Reports Sec. Litig.*, 289 F. Supp. 2d 429, 437 (S.D.N.Y. 2003).
 Furthermore, Plaintiff’s vague quotation of SEC official Linda Chatman Thomsen’s press release about an
 enforcement proceeding not involving Defendants, but other parties under different facts, is irrelevant to this
 litigation. (SAC ¶ 12.) Further, the statement Plaintiff quotes concerned a *non-litigated, administrative settlement*.
 Such settlements are not, and cannot be, legal precedent, as they have neither been tested by the adversary system
 nor subjected to judicial scrutiny. *See Morgan Stanley*, 2006 WL 1008138, at *5.

1 **B. The Prospectuses Accurately and Adequately Disclosed the Revenue-Sharing**
2 **Arrangement**

3 Since there is no statutory disclosure requirement, Ms. Dumdie’s claims fail unless she
4 can allege an affirmative material misstatement in the Prospectuses and Registration Statements,
5 or that the omission of certain material facts rendered an affirmative statement misleading. *See*
6 *Benzon*, 420 F.3d at 611–12. Under Rule 9(b), this means that she is required to allege facts
7 providing “an explanation as to why the statement or omission complained of was false or
8 misleading.” *In re Stac Elec. Sec. Litig.*, 89 F.3d at 1404. The SAC falls well short of the
9 minimum pleading standard.

10 The SAC’s core allegation concerns a semantic quibble, not a material misstatement:
11 that the Funds’ Prospectuses provided inadequate disclosure when they stated that the
12 investment advisors “may” make payments to broker-dealers when, in fact, WM Advisors and
13 WM Distributor had already entered into some revenue-sharing arrangements. (SAC ¶ 10.) But
14 a complaint founded on allegations of securities fraud must be dismissed where, as here, “the
15 allegedly omitted or misrepresented information was in fact appropriately disclosed.” *See White*
16 *v. Melton*, 757 F. Supp. 267, 272 (S.D.N.Y. 1991); *see also In re Keyspan Corp. Sec. Litig.*, 383
17 F. Supp. 2d 358, 377 (S.D.N.Y. 2003) (“Even at the pleading stage, dismissal is appropriate
18 where the complaint is premised on the nondisclosure of information that was actually
19 disclosed”).

20 Defendants expressly disclosed the allegedly hidden incentive fees in every Registration
21 Statement during the class period, and either attached or incorporated by reference an exhibit
22 entitled the “Form of Dealer Agreement” between both WM Distributor and WM Advisors and
23 selling broker-dealers. The “Form of Dealer Agreement” identified the specific terms under
24 which WM Advisors made incentive payments to broker-dealers for selling shares of the WM
25 Strategic Asset Management Portfolios:

1 Whereas WM Advisors, Inc. recognizes that it will benefit from
2 the sale of Shares of WM Strategic Asset Management Portfolios,
3 LLC, WM Advisors, Inc. hereby agrees to pay to Selling Broker-
4 Dealer, with respect to Shares of WM Strategic Asset
5 Management Portfolios, LLC, a fee accrued daily and payable
6 monthly at the annual rate of 0.50% (0.25% for Class C Shares)
7 of the average daily net assets of such Shares held by Customers
8 for whom Selling Broker-Dealer is the dealer of record, which
9 fee is in addition to any dealer allowance, Sales Commissions
10 and/or service fees payable by WMFD as set forth above. WM
11 Advisors reserves the right to change the amount of, or to cease
12 paying, this fee upon fifteen (15) days prior written notice to
13 Selling Broker-Dealer.

14 (Escobar Decl., Ex. I at 13.) In fact, the Form of Dealer Agreement and 50 Bps APF had been
15 publicly disclosed by the Funds by at least the year 2000. (Escobar Decl., Ex. J at 8.) Thus,
16 there can be no legitimate dispute that the Funds' Registration Statements at issue disclosed the
17 revenue sharing program long before the start of the putative class period.

18 The Court can and should rely upon these publicly filed documents, which are referenced
19 in the SAC itself, in determining that the SAC's claims have no merit as a matter of law. *See In*
20 *re AIG Advisor Group Sec. Litig.*, No. 06 CV 1625 (JG), 2007 WL 1213395, at *7 (E.D.N.Y.
21 Apr. 25, 2007) (holding that the court "may consider publicly available documents—such as
22 prospectuses and SAIs—relied upon or referenced in the complaint"); *Whirlpool Fin. Corp. v.*
23 *GN Holdings, Inc.*, 67 F.3d 605, 610 (7th Cir. 1995) (holding that "a reasonable investor is
24 presumed to have information that is in the public domain") (quoted in *Berry v. Valence Tech.,*
25 *Inc.*, 175 F.3d 699, 703, n.4 (9th Cir. 1999)). Moreover, the SEC expressly confirms that mutual
26 funds need not include all publicly disclosed information in the prospectuses, and instead
expressly authorizes funds to disclose certain information in the prospectuses, while disclosing
other information only in other parts of the registration statement. (*See* Escobar Decl., Ex. K at
7-8 (Form N-1A and instructions).)

As in the *Zapien* action, Plaintiff here will likely counter that Defendants misled
investors by stating that WM Distributor "may, from time to time," make incentive payments to

1 broker-dealers when, in fact, WM Distributor was already making such payments. (SAC ¶ 10.)

2 But this argument fails for at least two reasons.

3 First, Ms. Dumdie’s argument fails as a matter of law because the statements about
4 which she complains did not suggest that there were no revenue-sharing arrangements. *See*
5 *Brody v. Transitional Hosp. Corp.*, 280 F.3d 997, 1007 (9th Cir. 2002) (public statement held
6 not materially misleading where it did not create false impression). To the contrary, all of the
7 Prospectuses and Registration Statements put Plaintiff and potential class members on notice of
8 the possibility of such arrangements. *See Benzon*, 420 F.3d at 612; *see also AIG*, 2007 WL
9 1213395, at *8 n.15. For exactly this reason, both the Sixth Circuit Court of Appeals and courts
10 in the Southern District of New York have *rejected* the very contention Ms. Dumdie attempts to
11 advance in this case—that it is materially misleading to state that a program possibly
12 encouraging brokers to sell particular mutual funds “may” exist when it does exist. *Benzon*, 420
13 F.3d at 612; *Hoffman*, 2008 WL 4684168, at *6; *AIG*, 2007 WL 1213395, at * 8 n.15.

14 Applying the exact same legal standards that control in this circuit, the Sixth Circuit held
15 that the difference between a disclosure that dealers “may” receive sales incentives and one
16 confirming that they “do” receive such incentives is merely “a semantic quibble.” *Benzon*, 420
17 F.3d at 612. The *Benzon* court explained:

18 If anything, the inclusion of this statement in the prospectus
19 (which, again, was not mandated by any current SEC regulation)
20 served to put prospective investors on notice that there was a
21 possibility that brokers were being compensated more highly for
the sale of certain class shares than others, such that investors
could pursue that line of inquiry with their financial advisors if
they were concerned about broker incentives.

22 *Id.* Judge Gleeson of the Southern District of New York agreed, rejecting the same argument
23 that “may” language is misleading in the context of mutual fund incentive programs. *AIG*, 2007
24 WL 1213395, at *8 n.15.

25 Plaintiff also challenges as supposedly misleading the Prospectuses’ statements that
26 certain payments were at the expense of WM Distributor and WM Advisor, merely because WM

1 Distributor and WM Advisor ultimately traced their revenues to fees paid to them by the Funds.
2 (SAC ¶ 66.) Nonsense. The Prospectuses and Registration Statements fully disclose that WM
3 Distributor derives its revenue from fees paid to it by the Funds. (*See* Escobar Decl., Ex. F at
4 12-13.) The purportedly omitted fact under Plaintiff’s strained argument—that any payment
5 made by WM Distributor or WM Advisor must come from sums that can be ultimately traced
6 back to fees paid to them from the Funds—is obvious from the express language of the
7 Prospectuses and Registration Statements. The fact that WM Distributor or WM Advisor chose
8 to spend a portion of the fully disclosed fees they received from the Funds on payments to
9 broker-dealers does not make those payments any less “at [their] expense”; for example, they
10 could choose not to make those payments and yet retain the entire fee they receive from the
11 Funds. (*See, e.g.*, Escobar Decl., Ex. F at 13 (noting that even if fees paid to WM Distributor
12 exceed WM Distributor’s expenses, WM Distributor may keep the entire fee).) When testifying
13 before Congress, then Director of the SEC’s Division of Investment Management Paul Roye
14 used almost the same terms as those challenged by Plaintiff to explain why mutual funds were
15 not required to disclose their investment advisors’ revenue-sharing arrangements, even though
16 such advisors, just like mutual fund distributors, ultimately trace their revenue to fees paid by the
17 mutual funds from investment principal. As Mr. Roye explained, “Revenue-sharing payments
18 are *not a fund expense* because they are made from the adviser’s *own resources, rather than fund*
19 *assets.*” (Escobar Decl., Ex. G at 7 (emphasis added).)

20 Second, in this case, not only was the term “may” not misleading, it was accurate. The
21 Form of Dealer Agreement during the class period stated that “WM Advisors reserves the right
22 to change the amount of, or to cease paying, this fee upon fifteen (15) days prior written notice
23 to Selling Broker-Dealer.” (Escobar Decl., Ex. I at 13.) Mutual fund prospectuses and
24 registration statements, however, may be effective for as long as 16 months and are usually
25 updated only once per year. *See* 15 U.S.C. § 77j(a)(3) (prospectus must not use information
26 more than 16 months old); 17 C.F.R. § 270.8b-16 (SEC rule requiring annual amendment of

1 mutual fund registration statement, within 120 days of fiscal year end). WM Distributor could
2 enter into different arrangements with different selling dealers, and was not mandated to provide
3 “additional compensation” to all of them. Given the fact that the Funds’ Prospectuses and
4 Registration Statements could outlast the revenue-sharing arrangements in place at the time
5 those documents were publicly filed, the term “may” was more accurate than more static terms
6 such as “do” or “will.” Thus, the SAC’s claims must be dismissed because Defendants actually
7 (and accurately) disclosed the information alleged by Ms. Dumdie to be concealed or misstated.

8 If the arguments in *Zapien* are any indication, Ms. Dumdie will urge that these claims
9 are supported by *Siemers v. Wells Fargo & Co.*, in which a district court in San Francisco
10 allowed fraud claims based on “may” language to survive the pleading stage. *Siemers v. Wells*
11 *Fargo & Co.*, No. C 05-04518 WHA, 2006 WL 2355411, at *5 (N.D. Cal. Aug. 14, 2006). But
12 *Siemers* is distinguishable on its facts. Unlike here, the defendants in *Siemers* never disclosed
13 the full nature of the revenue-sharing arrangement in the registration statement or SAI. *Id.*, at
14 *5-*6. In addition, unlike here, the plaintiffs in *Siemers* alleged that Wells Fargo mutual fund
15 advisers caused the funds’ portfolios to be traded through Wells Fargo’s broker-dealers at
16 inflated commission rates, thus guaranteeing the broker-dealers a steady flow of commission
17 revenue (known as “directed brokerage”) that was not disclosed to investors. *Id.*, at *3. There
18 are no allegations of directed brokerage here.

19 In sum, the “may” language was appropriate, not misleading—both as a matter of law
20 and based on the flexible nature of the incentive program. Any ambiguity, whether real or
21 imagined, was cured by the additional details disclosed in each of the Registration Statements
22 and their exhibits. For all of these reasons, the SAC must be dismissed because it fails to plead a
23 material misstatement or omission with particularity.

1 **C. Defendants Did Not Misstate or Omit the Amounts of Their Advisor Paid**
2 **Fees**

3 Ms. Dumdie has embellished the Complaint with an additional allegation that contradicts
4 earlier versions of the *Zapien* complaints and all of the Funds' public disclosures, which all
5 stated that the **total** compensation to brokers was a 25 Bps 12b-1 fee from WM Distributors and
6 a potential 50 Bps APF from WM Advisors. Plaintiff alleges that the APF was really 75 Bps.
7 (SAC ¶ 4.) The sole support for this allegation is a marketing document that explains that the
8 "**Total** Fee Income" to brokers for the sale of Portfolios funds is "75 Bps." (SAC Ex. A
9 (emphasis added).) Pointedly, the document on which Plaintiff relies does not say that the APF
10 is 75 Bps. The marketing piece is targeted to the broker-dealer community and simply sets forth
11 the total fees that could be earned by selling the Funds: 75 Bps. Since broker-dealers could earn
12 a 25 Bps 12b-1 fee and a potential 50 Bps APF, this summary marketing document was both
13 accurate and consistent with Defendants' more particularized disclosure of these fees. Plaintiff's
14 reading of this marketing document is completely untenable since it implies that the total fee
15 income available to broker-dealers is 100 Bps, something that contradicts the face of the
16 document and all public disclosures. Plaintiff fails to point to any other support for her
17 allegation that the APF itself was 75 Bps. Rank speculation does not support an adequate
18 allegation of securities fraud. *See Bell Atlantic Corp.*, 127 S. Ct. at 1974 (pleading must nudge
19 claims beyond the conceivable to the plausible). Here, Plaintiff's proposed reading of the
20 marketing document is facially implausible and contradicts the actual, specific disclosure of the
21 components of the total fees that could be earned by broker-dealers selling the Funds. The Court
22 is not required to accept this alleged "fact" at the pleading stage. *Steckman*, 143 F.3d at 1295-96
23 (holding that a court is not required to accept facts in the complaint that contradict facts in
24 documents referred to in the complaint).

1 **V. THE SAC DOES NOT ALLEGE SCIENTER WITH PARTICULARITY**

2 To adequately plead scienter under the PSLRA for its Section 10(b) claim, the SAC must
3 “state with particularity facts giving rise to a strong inference that the defendant acted with the
4 required state of mind.” 15 U.S.C. § 78u-4(b)(2). In the Ninth Circuit, a plaintiff must “show
5 that defendants engaged in ‘knowing’ or ‘intentional’ conduct.” *South Ferry LP, #2 v. Killinger*,
6 542 F.3d 776, 782 (9th Cir. 2008) (referencing *In re Silicon Graphics Inc. Sec. Litig.*, 183 F.3d at
7 975) (noting that reckless conduct may also meet this standard if “it reflects some degree of
8 intentional or conscious misconduct”...[or] “deliberate recklessness.”). A plaintiff must plead
9 specific allegations as to **each** defendant’s state of mind. *See Fouad*, 2008 WL 5412397, at *8;
10 *see also In re New Century*, ___ F. Supp. 2d ___, No. CV 07-00931 DDP (JTLx), 2008 WL
11 5147991, at *13 (C.D. Cal. Dec. 03, 2008) (stating that the majority of reported district court
12 cases in the Ninth Circuit hold that the group pleading doctrine is no longer viable).

13 As the Supreme Court explained in *Tellabs, Inc.*, to “qualify as ‘strong’ ... an inference
14 of scienter must be more than merely plausible or reasonable—it must be cogent and at least as
15 compelling as any opposing inference of nonfraudulent intent.” 127 S. Ct. at 2504–05. This
16 standard requires the SAC to raise a strong inference of “scienter—i.e., a strong inference that
17 the defendant acted with an intent to deceive, manipulate, or defraud.” *Metzler Inv. GMBH v.*
18 *Corinthian Coll., Inc.*, 540 F.3d 1049, 1061 (9th Cir. 2008) (internal references omitted). In
19 making this determination, courts must engage in a “holistic” review of the allegations that
20 analyzes whether “all of the facts alleged, taken collectively, give rise to a strong inference of
21 scienter.” *Tellabs*, 127 S. Ct. at 2511 (emphasis in original); *see also South Ferry*, 542 F.3d at
22 784. When conducting this holistic review, the court must take into account plausible opposing
23 inferences, and “only allow the complaint to survive a motion to dismiss if the malicious
24 inference is at least as compelling as any opposing innocent inference.” *Zucco Partners LLC*,
25 2009 WL 57081, at *5 (holding that Ninth Circuit courts should conduct a dual inquiry to first
26

1 determine whether any allegation standing alone sufficiently alleges scienter before conducting
2 the holistic review of the same allegations).

3 Under either prong of the dual inquiry espoused by the Ninth Circuit in *Zucco Partners*,
4 the SAC has failed to allege facts giving rise to a strong inference of scienter because each of the
5 facts in the SAC is more plausibly explained by a proper motivation. As a result, the SAC fails
6 to supply the Court with any inference of scienter that is as cogent and at least as compelling as
7 any opposing inference of nonfraudulent intent. We debunk each scienter allegation individually
8 before explaining why they also fall short collectively.

9 **A. The “Evolution” and “Minimize Potential Liability” Allegations Support No**
10 **Inference of Scienter**

11 First, the SAC claims that scienter is shown because the “fact that the disclosures came
12 after the Steering Programs were put in place and evolution of the purported disclosures over
13 time demonstrate that the Registrants intentionally sought to disclose as little information as
14 possible about the Steering Programs.” (SAC ¶ 62.) Moreover, the SAC claims that Defendants
15 only disclosed additional information about the revenue-sharing program in 2004 “in a
16 transparent and belated attempt to ‘clean up’ their disclosures and minimize their potential
17 liability” following “the illegal activities and scandals in the mutual fund industry.” (SAC ¶ 68.)
18 This allegation is nothing more than pleading “fraud by hindsight,” a practice that has been
19 universally condemned. *See In re Cabletron Sys., Inc.*, 311 F.3d 11, 37 (1st Cir. 2002);
20 *Teachers’ Retirement Sys. v. Hunter*, 477 F.3d 162, 183 (4th Cir. 2007), *see also In re Vantive*
21 *Corp. Sec. Litig.*, 283 F.3d 1079, 1084–85 (9th Cir. 2002) (“The purpose of the [Reform Act’s]
22 heightened pleading requirement was generally to eliminate abusive securities litigation and
23 particularly to put an end to the practice of pleading ‘fraud by hindsight.’”). That the Registrants
24 further refined their earlier disclosures of the APF and revenue-sharing program beginning in
25 2004 says nothing about any Defendant’s state of mind with respect to the earlier Prospectuses
26 on which Plaintiff’s claims are based. Plaintiff was required to allege facts creating a strong

1 inference that the Registrants knew or must have known that the statements were materially
2 misleading *when the statements were made*. She has not done so.

3 The Registrants slightly modified the 2004 Prospectus by moving the disclosure of the
4 APF's amount (50 Bps) from the SAI to the Prospectus. (SAC ¶ 54.) The Registrants made
5 additional modifications to this disclosure in the December 30, 2004 revised Registration
6 Statement and final February 27, 2005 version—both publicly filed with the SEC. (Escobar
7 Decl., Ex. L at 19-20, 22-23; SAC ¶ 56 (language in 2005 Prospectus).) These refinements,
8 which built on the disclosures in the earlier Registration Statements and added additional details,
9 further demonstrate Defendants' efforts to adjust the Funds' disclosures in a shifting landscape.
10 Given that an SEC spokesperson refused to criticize even the early iterations of the disclosure
11 employed here, despite the fact that the SEC was in 2004 (and still is) in the midst of its
12 rulemaking process for increased disclosures of mutual fund fee allocation, Defendants were
13 reasonable in their belief that the law did not require further disclosure at the time they filed the
14 Registration Statements in question. *See In re Morgan Stanley & Van Kampen*, 2006 WL
15 1008138, at *11; *Castillo v. Dean Witter Discover & Co.*, No. 97 Civ. 1272(RPP), 1998 WL
16 342050, at *8 (S.D.N.Y. June 25, 1998); *Merrill Lynch Inv. Mgmt. Funds Sec. Litig.*, 434 F.
17 Supp. 2d 233, 238 (S.D.N.Y. 2006) (holding that mutual funds are not required to disclose the
18 allocation of a portion of the total fees to pay for "shelf-space" programs); *see also* Escobar
19 Decl., Ex. G at 7 (noting that revenue-sharing arrangements need not be disclosed in mid-2003).
20 Though around the time that the Funds filed the 2004 Registration Statement, Congress and the
21 SEC considered enacting new laws requiring additional disclosures for revenue-sharing
22 arrangements, no such laws were yet enacted. (*See generally* Escobar Decl., Ex. G (testimony
23 before Congress regarding potential federal legislation); Ex. H (proposed SEC regulation).
24 Indeed, both the Sixth Circuit and courts in the Southern District of New York have found no
25 material inaccuracy in similar mutual fund prospectus disclosures stating that brokers "may"
26 receive additional compensation. *Benzon*, 420 F.3d at 612; *AIG*, 2007 WL 1213395, at *8 n.15.

1 This strongly supports that Defendants in this case acted reasonably and without fraudulent
2 intent when they decided to provide additional information about the APF in response to pending
3 legislation and potential new SEC rules. Going above and beyond the required level of
4 disclosure does not suggest scienter.

5 **B. The SAC Offers No Factual Support For Its Allegations Concerning the So-**
6 **Called Cerulli Report**

7 The SAC also tries to establish scienter by making the unsupported allegation that
8 Defendant Papesh commissioned a third-party consultant to the mutual fund industry, Cerulli
9 Associates, to prepare a report on the APF only to disregard its conclusion that the APF was
10 “highly problematic and should be discontinued immediately.” (SAC ¶ 63.) Ms. Dumdie has
11 not offered any particularized facts to support this allegation. She has not attached the report
12 itself, nor has she cited corroborating statements from a confidential witness or any other source
13 to bolster her bare assertion about the alleged report. Indeed, Ms. Dumdie’s allegations
14 concerning the purported Cerulli Report imply that she received this (mis)information from a
15 third-party source, but she supplies absolutely no supporting evidence to test the allegations’
16 reliability. This type of pleading is completely insufficient to give rise to a strong inference of
17 scienter under the PSLRA. *Cf. Zucco Partners*, 2009 WL 57081, at *9–10 (holding that
18 confidential witnesses must be described with sufficient particularity to establish their reliability
19 and personal knowledge).

20 **C. The SAC’s Misinterpretation of the Broker-Dealer Brochure Also Does Not**
21 **Support an Inference of Scienter**

22 The SAC also misplaces its reliance on the broker-dealer marketing document to prove
23 scienter. (*See* SAC ¶ 64.) As explained above in Section IV.C, this document simply confirms
24 that the total fees payable to broker-dealers was 75 Bps, not that the APF was 75 Bps. Since
25 broker-dealers were eligible to receive 25 Bps in 12b-1 fees and 50 Bps in APF, the SAC’s
26 allegations on this point do not enhance Plaintiff’s scienter argument.

1 **D. The SAC’s Motive Allegations Do Not Create a Strong Inference of Scienter**

2 The SAC’s motive allegations also do not create a strong inference of scienter. The SAC
3 claims that the fact that Defendants had “the Steering Program(s) in place indicates that the
4 Registrants know and believe that such Programs drive and increase sales.” (SAC ¶ 65.) It also
5 alleges that “the Registrants, the WM Advisor and WM Distributor reaped huge profits from the
6 Steering Programs and had an incentive to keep them secret.” (*Id.* ¶ 67.) The trouble with these
7 allegations, however, is that the economic incentive for brokers to sell the WM Portfolios Funds
8 was disclosed in all of the Registration Statements during the class period. *See Castillo*, 1998
9 WL 342050, at *10 (rejecting motive allegations where plaintiffs pointed to no motive other than
10 economic gain that was disclosed in the prospectus). Thus, these allegations that Defendants
11 were motivated to make misstatements to conceal the revenue-sharing program are absurd on
12 their face because the economic incentive was disclosed.¹¹

13 **E. A Holistic Review of These Allegations Creates an Equally Feeble Inference**
14 **of Scienter**

15 Viewing these feeble scienter allegations collectively brings the SAC no closer to
16 satisfying the *Tellabs* standard. To the contrary, the sum of the innocent inferences far
17 outweighs an inference of fraudulent intent: (1) the Funds’ disclosures complied with the laws
18 governing such disclosures that were in force at the time (and are still in effect); (2) when
19 Congress and the SEC considered changing these laws to require more fulsome disclosures,
20 Defendants stayed ahead of the curve by providing greater detail about the Funds’ revenue
21 sharing program *long before* any stricter disclosure laws could go into effect; (3) the broker-
22 dealer marketing supports Defendants’ disclosure of the 75 Bps of total fees available; (4) the
23 Cerulli Report allegation is completely unsubstantiated; and (5) the SAC’s motive allegations are
24 ineffective because the economic incentive created by the revenue-sharing program was fully

25 _____
26 ¹¹ Even if the SAC had made coherent allegations on this subject, allegations of motive and opportunity to defraud, without more, are generally insufficient to satisfy the PSLRA’s requirements for pleading scienter. *See In re Silicon Graphics Inc. Sec. Litig.*, 183 F.3d at 974.

1 disclosed. Thus, under either prong of the *Zucco Partners* dual inquiry, the SAC fails to plead
2 scienter with particularity and its Section 10(b) claim must therefore be dismissed.

3 **F. The SAC Also Fails to Meet the Pleading Standard of Rule 9(b) and the**
4 **PSLRA as to the Independent Directors**

5 In addition, Plaintiff fails to set forth her allegations against the Independent Directors
6 with the precision, specificity, and particularity necessary to state a fraud claim in the Ninth
7 Circuit. Instead, Plaintiff offers only conclusory statements, sounding in fraud and asserted
8 against all Defendants as a group, that fall short of the heightened pleading standard of Rule 9(b)
9 of the Federal Rules of Civil Procedure, as well as the PSLRA.

10 To comply with Rule 9(b), a complaint sounding in fraud “must provide allegations that
11 are specific enough to explain what about the defendant’s conduct is false or misleading, so that
12 the defendant can formulate a specific denial.” *Pennsylvania Ave. Funds v. Borey*, No. C06-
13 173RAJ, 2008 WL 426509, at *2 (W.D. Wash. Feb. 13, 2008). A fraud claim must (1) state
14 precisely the time, place, and nature of the specific acts of fraud, (2) state the reasons why each
15 specific act is misleading and (3) set forth particular facts that give rise to a strong inference that
16 the defendant acted with the required state of mind. *In re Oak Tech. Sec. Litig.*, No. 96-20552
17 SW, 1997 WL 448168, at *3 (N.D. Cal. Aug. 1, 1997). To satisfy the “state of mind”
18 requirement for securities fraud, a complaint must “show that defendants engaged in ‘knowing’
19 or ‘intentional’ conduct.” *South Ferry LP*, #2, 542 F.3d at 782 (referencing *In re Silicon*
20 *Graphics Inc. Sec. Litig.*, 183 F.3d at 975) (noting that reckless conduct may also meet this
21 standard if “it reflects some degree of intentional or conscious misconduct”...[or] “deliberate
22 recklessness.”).

23 The PSLRA imposes an even higher burden on a plaintiff seeking to plead violation of
24 federal securities law. *Pennsylvania Ave. Funds*, 2008 WL 426509, at *2. The PSLRA requires
25 a plaintiff to “specify each statement alleged to have been misleading, and, if an allegation
26 regarding the statement or omission is made on information and belief, the complaint shall state

1 with particularity all facts on which that belief is formed.” 15 U.S.C. § 78u-4(b)(1). In the
2 Ninth Circuit, the PSLRA is viewed as the “death knell for the ‘customary latitude’ a court
3 affords a complaint in considering a motion to dismiss.” *Pennsylvania Ave. Funds*, 2008 WL
4 426509, at *2 (citing *Gompper v. Visx, Inc.*, 298 F.3d 893, 896 (9th Cir. 2002)).

5 Plaintiff’s generalized allegations of fraud against the Independent Directors fail to meet
6 any of the Rule 9(b) or PSLRA requirements. In her Complaint, Plaintiff alleges generally that
7 all Defendants failed to make certain disclosures and that “defendants . . . knew at the time they
8 were issuing statements that the statements contained false and misleading information and thus
9 lacked any reasonable basis for making them.” (SAC ¶¶ 61, 69.) Ninth Circuit courts have held
10 that similar conclusory statements that fail to list specific acts or statements of fraud, or offer any
11 facts pertaining to the defendant’s state of mind or any possible motive, do not meet the criteria
12 of Rule 9(b) and the PSLRA. *See, e.g., Pennsylvania Ave. Funds*, 2008 WL 426509, at *4–5
13 (motion to dismiss granted for failure to comply with the PSLRA and Rule 9(b) when the
14 plaintiff failed to provide detailed facts to support its claims of the defendant’s violation of
15 federal securities laws); *In re Oak Tech. Sec. Litig.*, 1997 WL 448168, at *3 (requiring plaintiff
16 to meet the particularity requirement of Rule 9(b) when alleging control person liability).

17 Plaintiff’s allegations are also deficient because they are asserted generally against all
18 Defendants, each of whom has a different relationship to Plaintiff. *See Swartz v. KPMG LLP*,
19 476 F.3d 756, 764–65 (9th Cir. 2007) (“Rule 9(b) does not allow a complaint to merely lump
20 multiple defendants together but requires plaintiffs to differentiate their allegations when suing
21 more than one defendant and inform each defendant separately of the allegations surrounding his
22 alleged participation in the fraud.”); *In re New Century*, 2008 WL 5147991, at *13.

23 Accordingly, Plaintiff’s generalized and nonspecific allegations of fraud against the Independent
24 Directors fail to meet the standards of Rule 9(b) and the PSLRA and must be dismissed.

1 **VI. THE SAC FAILS TO PLEAD TRANSACTION CAUSATION WITH**
2 **PARTICULARITY**

3 The SAC's Section 10(b) claim must also be dismissed because it fails to plead reliance
4 (also known as transaction causation) with particularity. Reliance is a required element of
5 Section 10(b) and Rule 10b-5 claims and it must be pleaded with particularity under Federal
6 Rule of Civil Procedure 9(b) and the PSRLA. *See Basic Inc., et al., v. Levinson*, 485 U.S. 224,
7 243 (1988) (noting that reliance is a necessary element of a Rule 10b-5 cause of action); *Dura*
8 *Pharms., Inc. v. Broudo*, 544 U.S. 336 (2005); *In re Daou Sys., Inc.*, 411 F.3d 1006, 1014 (9th
9 Cir. 2005) ("It is well established that claims brought under Rule 10b-5 and section 10(b) must
10 meet the particularity requirements of Federal Rule of Civil Procedure 9(b).").

11 Nevertheless, under certain circumstances, securities plaintiffs are able to meet this
12 heightened pleading requirement for reliance by utilizing the "fraud on the market" theory. This
13 theory allows reliance to be presumed where shares are traded in an *efficient* market, because in
14 an efficient market all available public information is factored into the stock's market price. *See,*
15 *e.g., In re Van Wagoner Funds, Inc. Sec. Litig.*, 382 F. Supp. 2d 1173, 1187 (N.D. Cal. 2004).
16 When this presumption applies, plaintiffs need only show that they relied "on the integrity of the
17 price of the stock as established by the market, which in turn is influenced by information or the
18 lack of it." *In re Van Wagoner Funds, Inc.*, 382 F. Supp. 2d at 1188 (citing *In re Convergent*
19 *Techs. Sec. Litig.*, 948 F.3d 507, 512 n.2 (9th Cir. 1991)).

20 Here, Ms. Dumdie must plead transaction causation with particularity because the "fraud
21 on the market" theory does *not* apply to securities fraud claims based on mutual funds. As
22 numerous courts have explained, the "fraud on the market" theory is not available in the mutual
23 funds context because the price of mutual funds is not determined by the market and thus is not
24 affected by any alleged misrepresentations or omissions. *See In re Van Wagoner Funds, Inc.*,
25 382 F. Supp. 2d at 1188 (holding that because the plaintiffs failed to plead "particular facts
26 establishing an efficient market and because a mutual fund share price is not determined by the

1 market, but the underlying asset value,” the plaintiffs had not properly pleaded “fraud on the
 2 market reliance.”); *McPhail v. First Command Fin. Planning, Inc.*, 247 F.R.D. 598, 613 (S.D.
 3 Cal. 2007); *Young v. Nationwide Life Ins. Co.*, 183 F.R.D. 502, 510 (S.D. Tex. 1998); *Clark v.*
 4 *Nevis Capital Mgmt., LLC*, No. 04 Civ. 2702, 2005 WL 488641, at *18 (S.D.N.Y. Mar. 2, 2005).

5 Ms. Dumdie apparently concedes this reality because nowhere in the SAC does she claim
 6 reliance on the Funds’ NAV or the “fraud on the market” presumption. Indeed, she even
 7 acknowledges that critical and determinative differences exist between mutual funds and
 8 corporate stock traded in an efficient market: “A mutual fund company is very different from a
 9 traditional corporation” and “mutual fund shares do not trade at a price set by the public market.”
 10 (SAC ¶¶ 70, 72.) And because, as Ms. Dumdie admits, mutual funds are not traded “at a price
 11 set by the public market,” she may not rely upon the “fraud on the market” theory to presume
 12 transaction causation for her securities fraud claims. As a result, Ms. Dumdie must plead
 13 reliance with particularity.¹² This she has not done.

14 The SAC makes only one attempt to satisfy the reliance pleading requirement: “Plaintiff
 15 and members of the Class would not have purchased the WM Funds or paid the related
 16 commissions and fees . . . had the existence or nature of the Steering Programs been disclosed.”
 17 (SAC ¶ 77.) This conclusory allegation does not pass muster under the heightened pleading
 18 requirements because it falls short of a statement that Ms. Dumdie actually read the Prospectuses
 19 and Registration Statements and relied on them in making her purchase. It fails to adequately
 20 show that “but for the fraud, the plaintiff would not have engaged in the transaction at issue.”
 21 *See In re Daou Systems, Inc.*, 411 F.3d at 1025. It is not enough to merely assert that Ms.
 22 Dumdie and the Class would not have purchased the Funds but for the fraud. In *Van Wagoner*

23 ¹² Indeed, even if the SAC survives Defendants’ Motion to Dismiss—and it should not—Ms. Dumdie faces a steep
 24 uphill battle at class certification because, without being able to rely on the “fraud on the market” presumption,
 25 individual questions of reliance will almost certainly predominate and the proposed class will fail. *See, e.g., Oscar*
 26 *Private Equity Inv. v. Allegiance Telecom, Inc.*, 487 F.3d 261, 264 (5th Cir. 2007) (“This [fraud on the market]
 theory permits a trial court to presume that each class member has satisfied the reliance element of their 10b-5
 claim. Without this presumption, questions of individual reliance would predominate, and the proposed class would
 fail.”).

1 *Funds*, a case also involving mutual funds, the court dismissed similarly worded allegations for
2 failure to plead reliance with particularity. 382 F. Supp. 2d at 1187–88. Specifically, the *Van*
3 *Wagoner Funds* court found the plaintiffs’ allegations lacking because they did not allege that
4 the plaintiffs had actually read the annual reports or registrations statements and relied on them
5 when purchasing the mutual funds at issue. *Id.*; see also *Clark*, 2005 WL 488641, at *18
6 (dismissing a fraud claim in the mutual funds context because the plaintiff did not allege direct
7 reliance upon the misrepresentations or omissions alleged in the mutual funds context). Here,
8 the SAC’s failure to plead anything but a conclusory allegation of reliance is fatal to
9 Ms. Dumdie’s claims. As a result, her Section 10(b) claim (Count IV) must be dismissed for this
10 separate and additional reason.

11 **VII. PLAINTIFF FAILS TO PROPERLY PLEAD DAMAGES AND LOSS**
12 **CAUSATION**

13 **A. The SAC Has Not Alleged Damages to Support the Securities Act Claims**

14 Ms. Dumdie’s Securities Act claims are also deficient because she has failed to plead that
15 she suffered recoverable damages, which in this context must take the form of an out-of-pocket
16 loss resulting from depreciation in the Funds’ value. Sections 11 and 12(a)(2) of the Securities
17 Act allow only for recovery of depreciation in value of the subject security. See 15 U.S.C.
18 §§ 77k(e), 771(a)(2), (b); *In re Merrill Lynch & Co. Research Reports Sec. Litig.*, 272 F. Supp.
19 2d 243, 253–54 (S.D.N.Y. 2003); *In re Mutual Funds Inv. Litig.*, 384 F. Supp. 2d 845, 866–67
20 (D. Md. 2005). If the Funds have instead appreciated in value between the time of their
21 acquisition during the class period and when they were sold (or if not sold, at the time of suit),
22 then there can be no recovery under the Securities Act. See *In re Mutual Funds Inv. Litig.*, 384
23 F. Supp. 2d at 867 (dismissing Section 11 and 12 claims because plaintiffs failed to allege that
24 they did sell, or could have sold at the time of suit, their shares for an amount less than they
25 paid).

1 Here, Ms. Dumdie merely alleges that she sustained damages as a result of the purported
2 violations of the Securities Act, but nowhere alleges that her shares in the Funds depreciated in
3 value following her acquisition. (SAC ¶¶ 16, 70–78.) To the contrary, all but one of the Funds
4 purchased by Ms. Dumdie increased in value during the class period. (Escobar Decl., Exs. M,
5 N.) And because Ms. Dumdie has not alleged that she sold her shares in the Funds at a loss, or
6 could have sold them at a loss at the time of filing suit, her Securities Act claims are deficient
7 and should be dismissed. *See In re Mutual Funds Inv. Litig.*, 384 F. Supp. 2d at 867.

8 **B. Plaintiff Has Not Alleged Loss Causation on the Exchange Act Claims**

9 The SAC also fails to plead “loss causation”—that some acts or omissions by Defendants
10 actually caused the alleged losses that Ms. Dumdie seeks to recover. *See Dura Pharms., Inc. v.*
11 *Broudo*, 544 U.S. 336, 341 (2005). To properly plead loss causation, Ms. Dumdie must link her
12 alleged losses not merely to her ownership of the Funds, but also to the purported failure to
13 adequately disclose the incentive arrangement. *See id.*; *see also Metzler Inv. GMBH*, 540 F.3d at
14 1063 (“the complaint must allege that the practices that the plaintiff contends are fraudulent ...
15 caused the resulting losses”); *In re Gilead Sciences Sec. Litig.*, 536 F.3d 1049, 1054, 1057–58
16 (9th Cir. 2008) (requiring causal connection between disclosure of alleged fraud and plaintiff’s
17 alleged loss). Ms. Dumdie does not adequately allege such a link.

18 A mutual fund’s price is determined by the “net asset value” (“NAV”) of the fund. (SAC
19 ¶ 72.) The NAV is calculated by subtracting the mutual fund’s liabilities, such as fees and
20 commissions, from its assets. *See In re Morgan Stanley & Van Kampen*, 2006 WL 1008138, at
21 *9 (listing the formula for calculating NAV). In the context of mutual funds, loss causation
22 requires the SAC to allege that the NAV would have been higher had the Funds more fully
23 disclosed the incentive arrangement. *See Castillo v. Dean Witter Discover & Co.*, 1998 WL
24 342050, at *5 (rejecting theory that failure to disclose that a portion of certain mutual fund fees
25 was paid to brokers as an incentive for selling shares could cause plaintiffs’ loss). But, as
26 explained in *Castillo*, any decline in the NAV relates “to the success of the investment strategies

1 of that fund ... and bears no relationship to the compensation arrangements of the brokers.” *Id.*
2 Put differently, only the total fees charged—not their allocation—impacts NAV. *See id.; In re*
3 *Morgan Stanley & Van Kampen*, 2006 WL 1008138, at *9. Thus, whether or not the various
4 Prospectuses and Registration Statements fully disclosed the allocation of these fees, and
5 regardless of whether the fee-sharing arrangements were in place or not, the Funds’ NAV could
6 only be impacted by the total fees charged to the Funds. And because these fees were disclosed
7 in full detail, Ms. Dumdie’s only theory for loss causation is that the allocation of the fees
8 “reduce[d] the price at which the fund’s shares are bought and sold.” (SAC ¶ 71.) This
9 allegation, however, is incorrect as a matter of law and cannot establish loss causation. *See In re*
10 *Morgan Stanley & Van Kampen*, 2006 WL 1008138, at *9 (holding plaintiff’s claim that value
11 of mutual fund shares would have been less if incentive fees to brokers were disclosed is
12 “incorrect as a matter of law”); *Castillo*, 1998 WL 342050, at *5–6.

13 **VIII. PLAINTIFF FAILS TO PLEAD “SCHEME LIABILITY” UNDER RULE 10B-5**

14 To the extent the SAC relies on a theory that the Registrants and Principal Investors Fund
15 engaged in a “scheme to defraud” investors in violation of Rule 10b-5(a) and (c) (*see* SAC
16 ¶ 123) to state its Section 10(b) claim against them, this theory collapses for failure to plead a
17 fraudulent scheme and failure to plead reliance on the scheme.

18 A complaint cannot adequately allege “scheme liability” under Rule 10b-5(a) and (c)
19 unless it pleads specific facts showing that a defendant engaged in a “deceptive act,” meaning a
20 transaction or conduct that had “the *principal purpose and effect* of . . . creat[ing] the false
21 appearance of fact” in connection with the purchase or sale of a security. *See Simpson v. AOL*
22 *Time Warner Inc.*, 452 F.3d 1040, 1048–50 (9th Cir. 2006), *vacated on other grounds*. The SAC
23 pleads no such facts for this makeweight argument. *In re Ditech Networks, Inc. Deriv. Litig.*,
24 No. C 06-5157 JF, 2007 WL 2070300, at *6 (N.D. Cal. July 16, 2007) (dismissing scheme
25 liability claim for failure to plead the fraudulent conduct with particularity). In addition, as the
26 Supreme Court recently held in *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta*, 128 S. Ct.

1 761 (2008) there can be no “scheme” liability under 10b-5 without a showing that plaintiff
 2 actually relied upon the scheme in connection with the purchase or sale decision. Here, the
 3 claims of the SAC are premised upon the allegedly incomplete disclosure of broker
 4 compensation. As pointed out elsewhere, the nature and total amount of such compensation was
 5 disclosed and the misrepresentation and omission claims consequently fail. Invoking the
 6 alternative of “scheme” liability does nothing to correct this deficiency. Moreover, as discussed
 7 *supra* in Section VI, there is no allegation that Plaintiff specifically relied upon the Prospectuses
 8 at issue in making her purchases of the Funds. For these reasons, a “scheme” liability theory
 9 does not help Plaintiff.

10 **IX. THE COMPLAINT MUST BE DISMISSED BECAUSE ITS CLAIMS ARE STALE**

11 Every one of the SAC’s claims is time-barred by the statute of limitations, statute of
 12 repose, or both.¹³ As described below, the Funds’ public disclosures throughout the Class
 13 Period placed reasonably diligent investors on inquiry notice beginning on February 28, 2002, of
 14 any claims. Because the SAC was not filed until August 20, 2008, even the Section 10(b) claims
 15 carrying the more generous two-year statute of limitations are stale by over four years.
 16 Moreover, the applicable statutes of repose—which set outer limits for bringing an action,
 17 irrespective of when an investor could have discovered her claim—further require that most of
 18 the SAC’s claims be dismissed. Finally, Ms. Dumdie’s reliance on the *Zapien* lawsuit to toll her
 19 claims is not only incorrect, but also ineffective, because *Zapien* also was filed after the statutes
 20 of limitations had expired. Accordingly, this Court should dismiss the SAC in its entirety.

21 **A. The SAC’s Claims Are Time-Barred Because Ms. Dumdie and the Putative**
 22 **Class Were Placed on Inquiry Notice of the APF Long Before This Suit Was**
 23 **Filed**

24 The SAC’s claims under the Securities Act carry a one-year statute of limitations that
 25 runs from the date of actual or inquiry notice. *In re Stac Elec. Sec. Litig.*, 89 F.3d at 1411. The

26 ¹³ See *Malone v. Clark Nuber, P.S.*, No. C07-2046 RSL, 2008 WL 2545069, at *5 (W.D. Wash. June 23, 2008)
 (explaining the difference between statute of limitations and statute of repose under federal securities laws).

1 Exchange Act claims are subject to a two-year statute of limitations from the date of actual or
 2 inquiry notice. 28 U.S.C. § 1658(b). Both statutes of limitations begin to run when a reasonable
 3 investor should have been aware of the alleged fraud if exercising reasonable diligence. *Betz v.*
 4 *Trainer Wortham & Co., Inc.*, 519 F.3d 863, 876 (9th Cir. 2008).

5 Plaintiff was put on inquiry notice of her claims on February 28, 2002, when the Funds
 6 filed a Registration Statement (including the Prospectus) with the SEC that told investors that
 7 WM Advisors and WM Distributor may enter into revenue-sharing arrangements with broker-
 8 dealers.¹⁴ (Escobar Decl., Ex. O at 23, 28.) Ms. Dumdie alleges that she and the members of the
 9 proposed class received all of the Class Period Prospectuses, including the 2002 Prospectus
 10 (SAC ¶¶ 53, 55), and are thus charged with knowledge of these documents' contents throughout
 11 the Class Period. The 2002 Prospectus therefore put every Funds' purchaser on notice that WM
 12 Advisors and WM Distributor may, at their own expense, pay additional fees to dealers for
 13 selling the WM Portfolios Funds. Moreover, the Funds' 2002 Registration Statement (of which
 14 the Prospectus was a part) incorporated by reference an earlier-filed specimen "Form of Dealer
 15 Agreement" between WM Distributor and WM Advisors and broker-dealers, specifically
 16 disclosing the material terms under which WM Distributor and WM Advisors agreed to pay
 17 broker-dealers in connection with sales of the Funds. (Escobar Decl., Ex. J.) In particular, the
 18 "Form of Dealer Agreement" clearly listed that broker-dealers that sell shares in the WM
 19 Portfolios Funds will receive an Advisor Paid Fee ("APF") of 50 basis points. (*Id.* at 8.) These
 20 public disclosures started the clock on the statute of limitations for the SAC's claims. *See, e.g.*,
 21 *Salinger v. Projectavision, Inc.*, 934 F. Supp. 1402, 1410 (S.D.N.Y. 1996) (holding that public

22 _____
 23 ¹⁴ The Funds filed their Registration Statement with the SEC on Form N1-A, which included the Funds' Prospectus,
 24 Statement of Additional Information ("SAI"), and other information concerning the Funds, including the Form of
 25 Dealer Agreement. (Escobar Decl., Ex. O at 29.) The Prospectus, which was delivered to all purchasers, informed
 26 investors that additional information about the Funds was available through multiple sources. (Escobar Decl., Ex. O
 at 24, 27 ("You may . . . request other information about the WM Group of Funds . . . by contacting your financial
 advisor, by calling toll-free 1-800-222-5852, or by visiting www.wmgrouppoffunds.com . . . [¶] You may also access
 reports and other information about the Portfolios and Funds on the EDGAR database on the [SEC's] Internet
 website at <http://www.sec.gov>.").

1 disclosure of information in SEC filings puts investors on notice of that information); *accord*
 2 *Whirlpool Fin. Corp.*, 67 F.3d at 610 (“A reasonable investor is presumed to have information in
 3 the public domain, and therefore . . . is imputed with constructive knowledge of this
 4 information.”); *In re Infonet Serv. Corp. Sec. Litig.*, 310 F. Supp. 2d 1106, 1114 n.7 (C.D. Cal.
 5 2003) (same). This includes information in a registration statement exhibit, such as the “Form of
 6 Dealer Agreement.” *See, e.g., Eckstein v. Balcor Film Investors*, 58 F.3d 1162, 1168 (7th Cir.
 7 1995).¹⁵ The 2003 and 2004 Registration Statements attached newer versions of the “Form of
 8 Dealer Agreement” that continued to reference the 50 Bps APF. (Escobar Decl., Exs. F at 5-14,
 9 I at 13, P at 13, Q at 16.)

10 On December 30, 2004, the Funds filed a revised Registration Statement that further
 11 spelled out the revenue-sharing arrangement in the following terms:

12 **WM ADVISORS ALSO OFFERS REVENUE SHARING**
 13 **PAYMENTS, REFERRED TO AS AN “ADVISOR PAID**
 14 **FEE” TO ALL FINANCIAL INTERMEDIARIES WITH**
 15 **ACTIVE SELLING AGREEMENTS WITH THE**
 16 **DISTRIBUTOR. THE ADVISOR FEE IS PAID AT AN**
 17 **ANNUAL RATE OF UP TO 0.50% OF THE AVERAGE NET**
 18 **ASSETS OF CLASS A AND CLASS B SHARES OF THE**
 19 **PORTFOLIOS SOLD THROUGH SUCH**
 20 **INTERMEDIARIES.... THESE PAYMENTS ARE MADE**
 21 **FROM WM ADVISORS’ PROFITS AND MAY BE PASSED**
 22 **ON TO YOUR INVESTMENT REPRESENTATIVE AT THE**
 23 **DISCRETION OF HIS OR HER FINANCIAL**
 24 **INTERMEDIARY FIRM. THESE PAYMENTS MAY**
 25 **CREATE AN INCENTIVE FOR THE FINANCIAL**
 26 **INTERMEDIARIES AND/OR INVESTMENT**
REPRESENTATIVES TO RECOMMEND OR OFFER
SHARES OF THE PORTFOLIOS OVER OTHER
INVESTMENT ALTERNATIVES.

(Escobar Decl., Ex. L at 19, *emphasis in the original*.) In this Registration Statement, the Funds
 disclosed, in bold print, the following facts: (1) the nature of the payments made to selling

¹⁵ As the Seventh Circuit observed in *Eckstein*, 58 F.3d at 1168, “The registration statement is a public document, well known to all of the underwriters and dealers plus many of the brokers, and accessible to anyone else who wants it.” Accordingly, investors have constructive knowledge of the facts concerning purported misstatements they could look up in a registration statement. *See id.* at 1169.

1 dealers (including the 50 Bps APF); (2) broker-dealers and investment representatives may as a
 2 result be incited to recommend the WM Portfolios over other investment alternatives; and (3) if
 3 investors had any questions or concerns about these arrangements, they should “speak with
 4 [their] investment representative to learn more about the total amounts paid to [their] investment
 5 representative and his or her financial intermediary by the Portfolios, the Distributor, WM
 6 Advisors, and by sponsors of other mutual funds he or she may recommend to [them].”
 7 (Escobar Decl., Ex. L at 20, 22.) The Funds’ February 28, 2005 prospectus repeated these
 8 disclosures with additional specifics. (Escobar Decl., Ex. R at 8-18.)¹⁶ The disclosures in the
 9 December 30, 2004 and February 25, 2005 prospectuses mirror Plaintiff’s allegations and
 10 foreclose any argument that by December 30, 2004, even a casual reader would know what
 11 Plaintiff claims was hidden.

12 This lawsuit was not filed until August 20, 2008. But because the 2002 Prospectus and
 13 Registration Statement triggered inquiry notice on February 28, 2002, the one-year statute of
 14 limitations for Lead Plaintiff’s Securities Act claims expired on February 28, 2003, and the two-
 15 year statute of limitations for her Exchange Act claims expired on February 28, 2004. The
 16 SAC’s claims are therefore stale. But even if the Court uses either the December 30, 2004
 17 revised Registration Statement, the February 25, 2005 final Registration Statement, or the
 18 February 28, 2006 Registration Statement as the document that triggered inquiry notice, the
 19 SAC’s claims are still stale. As a result, the Court should dismiss the SAC in its entirety with
 20 prejudice.¹⁷

23 ¹⁶ These statements were repeated yet again in the 2006 Prospectus filed by the Funds on February 28, 2006.
 (Escobar Decl., Ex. S at 15-17, 19-20, 22, 24, 27-28.)

24 ¹⁷ The *Zapien* action—which levied near-verbatim allegations against nearly all the same defendants—also placed
 25 Ms. Dumdie on inquiry notice of her claims. (SAC ¶¶ 86–87.) (Indeed, Ms. Zapien was represented by Finkelstein
 26 & Krinsk, one of the firms representing Ms. Dumdie in this action.) Because *Zapien* was filed on February 28,
 2007, the SAC’s Securities Act claims are stale for this additional reason. *In re American Funds Sec. Litig.*, 556 F.
 Supp. 2d 1100, 1109 (C.D. Cal. 2008) (finding inquiry notice where earlier-filed complaint alleged nearly verbatim
 allegations).

1 **B. Almost All of the SAC's Claims Are Also Stale Under the Statutes of Repose**

2 Most of the SAC's claims are also time-barred under the applicable statutes of repose.
3 The Securities Act carries a three-year statute of repose. *See* 15 U.S.C. § 77m. For claims under
4 Section 11, the statute of repose runs from the effective date of the allegedly false registration
5 statement, and for claims under Section 12(a), it runs from the date of purchase. *See id.*; *In re*
6 *Metro. Sec. Litig.*, 532 F. Supp. 2d 1260, 1281 (E.D. Wash. 2007). Since this Complaint was
7 filed August 20, 2008, the Court should dismiss as time-barred any Section 11 claims based on
8 Prospectuses and Registration Statements dated before August 20, 2005, and any Section 12(a)
9 claims premised on purchases before August 20, 2005.

10 Section 10(b) of the Exchange Act carries a five-year statute of repose running from the
11 date of the alleged violation. 28 U.S.C. 1658(b)(2); *Betz v. Trainer Wortham & Co., Inc.*, 519
12 F.3d at 872. Thus, the Court should dismiss as time-barred any Section 10(b) claims based on
13 purported misrepresentations or omissions arising before August 20, 2003.

14 **C. The Zapien Action Did Not Toll Plaintiff's Claims**

15 Recognizing that the aforementioned statutes of limitation and repose doom this action,
16 the SAC seeks shelter under the *American Pipe* tolling doctrine by alleging that the *Zapien*
17 action tolled its claims, presumably from the date Ms. Zapien filed her class action—
18 February 28, 2007 (SAC ¶¶ 86–90). *See American Pipe & Constr. Co. v. Utah*, 414 U.S. 538,
19 553 (1974); *see also Crown, Cork & Seal Co. v. Parker*, 462 U.S. 345 (1983) (allowing putative
20 class members to file separate individual lawsuits following the denial of a class certification,
21 rather than requiring them to intervene as individual participants in the original lawsuit). But
22 *American Pipe* tolling cannot save Ms. Dumdie's stale claims. First, tolling is unavailable
23 where, as here, the original action was dismissed for lack of standing. Second, tolling permits
24 subsequent individual claims to be filed, not subsequent class claims. Third, even if this
25 Complaint were judged by *Zapien*'s February 28, 2007 filing date, all of its claims would still be
26

1 time-barred. Fourth, because Mr. Papesh and the Independent Directors were not named as
 2 defendants in the *Zapien* action, there can be no tolling of the claims against them in this case.

3 **1. There is No *American Pipe* Tolling Where the Original Action Was**
 4 **Dismissed for Lack of Standing**

5 When the original plaintiff (such as *Zapien*) does not have standing, *American Pipe* does
 6 not toll a subsequent action. For example, in *Palmer v. Stassinios*, the court held that “the filing
 7 of a purported class-action complaint by a plaintiff who lacks standing does not toll the statute of
 8 limitations for those who later seek to intervene as plaintiffs” because “federal courts may only
 9 decide only cases and controversies, and a plaintiff without standing presents no live case or
 10 controversy.” 236 F.R.D. 460, 465–66 (N.D. Cal. 2006). Similarly, in *Putkowski v. Irwin Home*
 11 *Equity Corp.*, the court held that there was no *American Pipe* tolling because when the original
 12 named plaintiff does not have standing, there is “nothing to toll.” 423 F. Supp. 2d 1053, 1064
 13 (N.D. Cal. 2006); *see also In re American Funds Sec. Litig.*, 556 F. Supp. 2d (refusing to apply
 14 *American Pipe* tolling where original class action had been dismissed in part for lack of
 15 standing). Many courts outside the Ninth Circuit concur.¹⁸ Accordingly, because it was
 16 dismissed with prejudice for lack of standing, the *Zapien* suit cannot toll the SAC’s claims.

17 **2. *American Pipe* Tolling Does Not Allow Subsequent Class Actions**

18 Moreover, even if tolling were available, it would only permit Ms. Dumdie to file an
 19 individual claim for relief—not a class action lawsuit such as this one. *Robbin v. Fluor Corp.*,
 20 835 F.2d 213, 215 (9th Cir. 1987) (extending *American Pipe* tolling doctrine to class actions
 21 “falls beyond its carefully crafted parameters into the range of abusive options”). In *In re*
 22 *American Funds Securities Litigation*—a mutual funds case raising the identical issue in the

23 ¹⁸ *See, e.g., In re Colonial Ltd. P’ship Litig.*, 854 F. Supp. 64, 82 (D. Conn. 1994) (“[I]f the original plaintiffs lacked
 24 standing to bring their claims in the first place, the filing of a class action complaint does not toll the statute of
 25 limitations for other members of the purported class.”); *In re Elscint, Ltd. Sec. Litig.*, 674 F. Supp. 374, 378 (D.
 26 Mass. 1987) (“[I]t would be improper to allow the filing of a class action by nominal plaintiffs who are wholly
 inadequate to represent the asserted class to have the effect of tolling limitation to permit the otherwise untimely
 intervention of proper class representatives.”); *Hobbs v. Police Jury of Morehouse Parish*, 49 F.R.D. 176, 178–81
 (W.D. La. 1970).

1 context of very similar claims—the class plaintiffs attempted to rely on *American Pipe* tolling to
 2 piggyback their class action onto an earlier one that had been dismissed for, *inter alia*, lack of
 3 standing. 556 F. Supp. 2d at 1111–12; *In re American Mutual Funds Fee Litig.*, No. CV 04-
 4 5593-GAF (RNBx), 2005 WL 3989803, at *1–2 (C.D. Cal. Dec. 16, 2005) (opinion dismissing
 5 original case). They argued that if the original class action placed them on inquiry notice, “the
 6 statute of limitations was tolled during the period that the [original] case was litigated as a class
 7 action.” *American Funds*, 556 F. Supp. 2d at 1111. Judge Feess rejected the argument,
 8 distinguishing *Catholic Social Serv. v. INS*, 232 F.3d 1139 (9th Cir. 2000), a case in which the
 9 Ninth Circuit permitted tolling because the class in the prior case had actually been certified
 10 before the case was dismissed. Judge Feess rejected tolling where the prior case had not
 11 involved a certified class, agreeing with “those circuits that have expressly addressed the issue”
 12 that tolling extends to individual claims but not subsequent class claims. *Id.* (citing *Sheppard v.*
 13 *Capital One Bank*, 06-7535 GAF (FFMx), 2007 U.S. Dist. LEXIS 70061, at *7 (C.D. Cal.
 14 July 12, 2007)). The vast majority of circuit courts to address this issue agree.¹⁹

15 As was the case in *American Funds*, *Catholic Social Services v. INS*, does not support
 16 tolling in this case. *Catholic Social Services* involved a complex, 15-year series of class actions.

18 ¹⁹ See, e.g., *Basch v. The Ground Round, Inc.*, 139 F.3d 6, 11 (1st Cir. 1998) (“Plaintiffs may not stack one class
 19 action on top of another and continue to toll the statute of limitations indefinitely”); *Griffin v. Singletary*, 17 F.3d
 20 356, 359 (11th Cir. 1994) (pendency of class action did not toll limitations period for subsequent class actions by
 21 members of original asserted class); *Andrews v. Orr*, 851 F.2d 146, 149 (6th Cir. 1988) (“pendency of a previously
 22 filed class action does not toll the limitations period for additional class actions by putative members of the original
 23 asserted class”); *Korwek v. Hunt*, 827 F.2d 874, 879 (2d Cir. 1987) (*American Pipe* tolling doctrine “does not apply
 24 to permit a plaintiff to file a subsequent class action following a definitive determination of the inappropriateness of
 25 class certification”); *Salazar-Calderon v. Presidio Valley Farmers Ass’n*, 765 F.2d 1334, 1350 (5th Cir. 1985)
 26 (putative class members may not “piggyback” one class action onto another and thus toll the statute of limitations
 indefinitely). But see *Yang v. Odom*, 392 F.3d 97, 111-12 (3rd Cir. 2004) (holding that *American Pipe* tolling is
 available where the court originally denied class certification due to defects in class representatives rather than a
 defect in the class itself, but emphasized that tolling would not continue indefinitely where plaintiffs repeatedly
 failed to put forth an adequate class representative); *In re Quarterdeck Office Sys. Inc. Sec. Litig.*, No. CV-92-3090-
 DWW (GHKx), 1994 WL 374452 (C.D. Cal. Mar. 24, 1994) (tolling allowed where the prior case resulted in a
 denial of certification based on a lack of typicality); *Pierce v. Novastar Mortgage, Inc.*, Civ. No. 05-5825 RJB, 2006
 US Dist LEXIS 62875, at *10-11 (W.D. Wash. Sept. 6, 2006) (finding the Third Circuit’s precedent to be
 “somewhat persuasive” but declining to “definitively rule on the unsettled question of tolling due to prior cases”
 because class certification was not proper for other reasons).

1 In the first lawsuit, the district court certified the proposed class, but the United States Supreme
2 Court eventually reversed for lack of ripeness. *Id.* at 1141–45; *see Reno v. Catholic Social Serv.,*
3 *Inc.*, 509 U.S. 43, 66–67 (1993). Five years later, after several intervening proceedings, a second
4 lawsuit was filed and the Ninth Circuit ultimately allowed the class action to proceed despite the
5 earlier dismissal. *Catholic Soc. Servs.*, 232 F.3d at 1142. *Catholic Social Services* is
6 distinguishable because it—unlike *American Funds* and unlike this case—involved an original
7 class action that had been certified and “therefore did not involve any effort to circumvent a
8 prior ruling of the court or to piggyback one class action on another.” *American Funds*, 556 F.
9 Supp. 2d at 1111–12. Specifically, *Catholic Social Services* only allowed tolling in that instance
10 because an earlier class had been certified, and “Plaintiffs in this case are not attempting to
11 relitigate an earlier denial of class certification, or to correct a procedural deficiency in an earlier
12 would-be class.” *Catholic Soc. Servs.*, 232 F.3d at 1149. Here, Ms. Dumdie’s action is
13 attempting to correct a more fundamental jurisdictional deficiency in the would-be *Zapien* class
14 action. Thus, under either *Catholic Social Services* or *American Funds*, tolling of the class
15 claims is not permitted. Therefore, even if *Zapien* had tolled Ms. Dumdie’s claims (and it did
16 not), that would only permit Ms. Dumdie to bring an individual claim. The class allegations
17 should still be dismissed.

18 3. Even if Tolled, Most Claims in the SAC are Still Stale

19 Finally, even if Ms. Dumdie receives the benefit of *Zapien*’s filing date, the SAC’s
20 claims remain time-barred. As discussed above, investors were on inquiry notice of their claims
21 by February 28, 2002, meaning that the one-year statute of limitations for Securities Act claims
22 expired on February 28, 2003, and the two-year statute of limitations for Exchange Act claims
23 expired on February 28, 2004. The *Zapien* complaint was filed on February 28, 2007. Thus,
24 even if tolling were appropriate, the SAC would still be tardy by at least three years.²⁰

25 _____
26 ²⁰ In addition, even if tolling were permitted, it would not save the claims against Mr. Papesh and the Individual
Directors because they were not named in the *Zapien* action.

1 **X. MOST OF LEAD PLAINTIFF’S CLAIMS SHOULD BE DISMISSED FOR LACK**
 2 **OF STANDING**

3 **A. Plaintiff Has No Standing for Claims Based on Funds She Did Not Own**

4 In a securities class action lawsuit, the court must take special care to ensure that standing
 5 requirements are met. *See Shurkin v. Golden State Vinters Inc.*, 471 F. Supp. 2d 998, 1022 (N.D.
 6 Cal. 2006) (“In a securities case, strict standing requirements are important to prevent potential
 7 vexatious litigation.”). Under Article III, federal courts only have jurisdiction to hear a dispute if
 8 it involves a “case” or “controversy.” U.S. Const. art. III, § 2; *see also Raines v. Byrd*, 521 U.S.
 9 811, 818 (1997) (stating that the Supreme Court has “consistently stressed that a plaintiff’s
 10 complaint must establish that he has a ‘personal stake’ in the alleged dispute, and that the alleged
 11 injury suffered is particularized as to him.”). Moreover, actions under the Securities Act or the
 12 Exchange Act may be brought only by purchasers or sellers of the securities at issue. 15 U.S.C.
 13 § 771(a); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 749 (1975); *Zapien*, 2008 U.S.
 14 Dist. LEXIS 67137, at *8; *AIG*, 2007 WL 1213395, at *11–12; *In re Bank of Boston*, 762 F.
 15 Supp. 1525, 1531 (D. Mass. 1991). Where, as here, many of the Plaintiff’s claims are based on
 16 securities she never purchased, the court should dismiss those claims for lack of standing. *See*,
 17 *e.g.*, *AIG*, 2007 WL 1213395, at *4 (“In this securities fraud case, the named plaintiffs can allege
 18 no injury from the purchase or sale of funds they never invested in.”); *American Mutual Funds*,
 19 2005 WL 3989803, at *1–2; *In re Eaton Vance Corp. Sec. Litig.*, 219 F.R.D. 38, 42 (D. Mass.
 20 2003).

21 Here, Ms. Dumdie only alleges purchases for half of the Funds at issue. (SAC ¶ 16.)
 22 And because Ms. Dumdie only has standing to sue on behalf of funds that she purchased, she
 23 does not have standing with respect to the remaining twelve Funds. As a result, the SAC’s
 24 claims as to those Funds do not present a “case” or “controversy” or meet the requirements of
 25
 26

1 statutory standing under the securities laws. Accordingly, the Court should dismiss all claims in
2 the SAC based on the mutual funds never owned by Ms. Dumdie.²¹

3 **B. This Action Only Presents a Case or Controversy for the WM Portfolios**
4 **Funds Owned by Ms. Dumdie**

5 The principal theory of recovery in the SAC is the alleged impropriety and illegality of
6 the allegedly undisclosed APF that was supposedly paid by WM Advisors to induce sales of
7 WM Portfolios, and not the WM Trust I and WM Trust II Funds. (SAC ¶ 43.) Because the
8 alleged misstatements, all deriving from the APF, relate only to the WM Portfolios, purchasers
9 of the WM Trust I and WM Trust II Funds suffered no injury that is fairly traceable to the
10 alleged unlawful conduct, and therefore have no standing to complain about this fee. *See*
11 *Hoffman*, 2008 WL 4684168, at *5 (“If a party, such as Plaintiffs in this case, is not personally
12 injured by the alleged action of a defendant then he is not entitled to come into court and litigate
13 that action, regardless of whether the disposition of his case necessarily requires the same result
14 as the case of another.”).

15 In sum, the Court should dismiss all claims based on any Funds other than the following
16 five WM Portfolios Funds owned by Ms. Dumdie: (1) WM SAM Conservative Balanced;
17 (2) WM SAM Flexible Income; (3) WM SAM Conservative Growth; (4) WM SAM Balanced;
18 and (5) WM SAM Strategic Growth.

19 **XI. THE SAC HAS NOT ESTABLISHED CONTROL PERSON LIABILITY**

20 The SAC has not only failed to meet the heightened standards of Rule 9(b) and the
21 PSLRA, but it has also failed to establish control person liability pursuant to Section 15 of the
22 Securities Act and Section 20(a) of the Exchange Act.²² To allege control person liability, a

23 _____
24 ²¹ Ms. Dumdie does not assert any interest in the following funds: Tax-Exempt Money Market, U.S. Government
25 Securities, Income, High Yield, Tax-Exempt Bond, REIT, Small Cap Value, California Money, Short Term Income,
California Municipal, California Insured Intermediate Municipal and International Growth.

26 ²² The standard for imposing liability under section 15 of the Securities Act is substantially the same as that for
imposing liability under section 20(a) of the Exchange Act. As a result, courts rely on section 20(a) cases in
evaluating section 15 matters. *In re Metro. Sec. Litig.*, 532 F. Supp. 2d at 1296 n.12.

1 plaintiff must plead and prove (1) a primary violation of federal securities law and (2) that the
 2 defendant exercised actual power or control over the alleged primary violator. *In re Metawave*
 3 *Comm. Corp. Sec. Litig.*, 298 F. Supp. 2d 1056, 1086 (W.D. Wash. 2003). The SAC fails to
 4 fulfill either requirement.

5 **A. Plaintiff Has Not Adequately Alleged a Primary Violation of Federal**
 6 **Securities Law Against Defendants Pavelich, Yancy, Blake, Papesh, WM**
 7 **Advisors or WM Distributor**

8 Since the SAC's underlying claims fail for the reasons set forth in this motion, the
 9 control person claims against the Independent Directors, Papesh, WM Advisors and WM
 10 Distributor fail, too. *See, e.g., Pennsylvania Ave. Funds*, 2008 WL 426509, at *8; *Limantour v.*
 11 *Cray Inc.*, 432 F. Supp. 2d 1129, 1162 (W.D. Wash. 2006); *F.L. Heywood v. Cell Therapeutics,*
 12 *Inc.*, No. C05-0396RSM, 2006 WL 5701625, at *8 (W.D. Wash. May 4, 2006); *In re*
 13 *Watchguard Sec. Litig.*, No. C05-678J, 2006 WL 2038656, at *12 (W.D. Wash. Apr. 21, 2006).

14 **B. Plaintiff Has Also Not Adequately Alleged Actual Control and Culpable**
 15 **Participation by the Independent Directors**

16 Even if Plaintiff could state a claim for primary violation of the securities laws,
 17 Plaintiff's "control person" claims against the Independent Directors still fail because Plaintiff
 18 does not plead specific facts sufficient to establish that the Independent Directors exercised
 19 actual power or control over the alleged primary violator(s). Plaintiff's conclusory pleading that
 20 the Independent Directors are controlling persons because they sit on the WM Group of Funds
 21 Board of Trustees and "by virtue of their positions of operational control in the Registrants, and
 22 the WM Distributor" does not set forth a relationship description sufficient to survive a motion
 23 to dismiss. (SAC ¶¶ 23–25, 118.) In the Ninth Circuit, a plaintiff asserting "controlling person"
 24 liability must show that there was a relationship between the controlling and controlled person
 25 and that actual power or influence was exerted over the alleged controlled person. *Durham v.*
 26 *Kelly*, 810 F.2d 1500, 1503–04 (9th Cir. 1987).

1 Plaintiff's allegations do not satisfy either of these requirements. Plaintiff's only
2 allegations against the Independent Directors are a simple description of the Independent
3 Directors as members of the WM Group of Funds Board of Trustees or members of certain
4 committees. (SAC ¶¶ 23-25.) This is not enough. Rather, Plaintiff must allege specific facts to
5 establish that the Independent Directors had control through their day-to-day involvement in the
6 WM Funds or that their positions involved control of or involvement with the Funds'
7 Prospectuses and Registration Statements that Plaintiff alleges contain the alleged
8 misrepresentations. *See e.g. In re Metawave Comm. Corp. Sec. Litig.*, 298 F. Supp. 2d at 1091
9 (references to individual's job title did not establish control person liability in the absence of
10 allegations of involvement in day-to-day affairs or in specific areas related to alleged
11 misrepresentations); *In re Washington Pub. Power Supply Sys. Sec. Litig.*, No. 551, 1988 WL
12 158948, *20 (W.D. Wash. July 14, 1988) (holding that the nonmember participants, who voted
13 the respective shares of other participants they represented, had no direct means of controlling
14 the supply system and were not liable as control persons).

15 Here, Plaintiff gives no such factual details, but instead merely pleads the generalized
16 allegation that the Independent Directors "could have" corrected or prevented the issuance of
17 allegedly fraudulent registration statements. (SAC ¶¶ 118, 134.) This vague allegation does not
18 establish that the Independent Directors have engaged in the level of knowing participation in
19 day-to-day affairs necessary to make them "control persons." *See, e.g., Lapin v. Goldman Sachs*
20 *Group, Inc.*, 506 F. Supp. 2d 221, 246-47 (S.D.N.Y. 2006) (requiring that plaintiff plead
21 elements of control person liability with particularity); *Waldock v. M.J. Select Global, Ltd.*,
22 No. 03 C 5293, 2005 WL 3542527, at *6 (N.D. Ill. Dec. 27, 2005) (same). As such, Plaintiff
23 fails to adequately allege that the Independent Directors culpably participated in the alleged
24 wrongdoing.

25 Accordingly, for these additional reasons, the SAC must be dismissed as to the
26 Independent Directors.

1 **XII. CONCLUSION**

2 For the foregoing reasons, the SAC should be dismissed without leave to amend.

3
4 DATED: January 26, 2009

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