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UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

SAN FRANCISCO DIVISION

UNITED STATES OF AMERICA,

Plaintiff,

vs.

GREGORY L. REYES.

Defendant.

CASE NO. CR 06 0556 CRB

(1) GREGORY L. REYES'S REPLY BRIEF IN SUPPORT OF MOTION FOR JUDGMENT OF ACQUITTAL; AND

***FILED UNDER SEPARATE COVER*: (2) DECLARATION OF RONDA J. MCKAIG IN SUPPORT THEREOF**

Hearing Date: July 19, 2007
Time: None set
Judge: Hon. Charles R. Breyer
Courtroom: 8, 19th Floor

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I. INTRODUCTION AND SUMMARY OF ARGUMENT

At the July 6, 2007 hearing on Mr. Reyes's motion for judgment of acquittal, the Court correctly noted that "this is a case about false accounting . . . false reporting, [and] false representation," not about the backdating of stock options. (7/6/07 RT 2228:1–2).[1] Indeed, as the Court aptly observed, "we all know it's not illegal to backdate stock options . . . . Mr. Reyes could have given them the stock. He could give them whatever he wants to give them, right? [T]hat's not illegal." *Id.* (7/6/07 RT 2228:8–11). Thus, in order to prevail, the prosecution must prove beyond a reasonable doubt that Mr. Reyes understood the relevant accounting opinions, realized that Brocade's stock option granting practices required an accounting charge, and intentionally falsified Brocade's financial statements and disclosures.

> Court: That's what the case is about. You tell the public one thing and you do another thing and you know when you go and tell the public about what you have done, you are misrepresenting the actual state of affairs as required by law. That's what the case is.
>
> * * * * *
>
> *It's a disclosure case, and in a disclosure case you have to show that [Mr. Reyes] knew what he had to disclose and he knew he wasn't disclosing it and you have to establish that.*

(*Id.* 2228:2–7, 12–14) (emphasis added).

The prosecution understood this as well. In a pre-trial hearing on August 9, 2006, the then-lead prosecutor expressly stated that, under *United States v. Tarallo*, 380 F.3d 1174, 1181 (9th Cir. 2004), the government had the burden to prove "that the *defendants made false statements and knew that those statements affected the financials*." (8/9/06 RT 11:6–20) (emphasis added); *see also id.* 22:16–22 (Prosecutor: "When [*Tarallo*] talks about [a] wrongful act, what it talks about is *knowingly making false statements*.") (emphasis added). More recently, in May 2007, the prosecution acknowledged in its own proposed jury instructions that an intent to cheat or deceive was an essential element of securities fraud. *See* United States' Proposed Jury Instructions (Doc. 318) at 35 (citing

[1] "RT" refers to the record of transcript of the proceedings in this case and is preceded by the date of the proceedings and followed by the applicable page and line numbers. The cited transcript pages are attached to the Declaration of Ronda J. McKaig as Exhibit A. All cited trial exhibits are also attached to the McKaig Declaration.

Ninth Circuit Model Criminal Jury Instructions, 3.17 ("An intent to defraud is an intent to deceive or cheat.") (2000 ed.).

At the July 6 hearing, however, the Court expressed skepticism that the record contained *any* proof from which a rational juror could find such a *mens rea* — *i.e.*, proof that Mr. Reyes understood the accounting opinions at issue, knew that Brocade's stock option practices warranted an accounting charge, knew that Brocade's financial statements and related disclosures were inaccurate, and intended to cheat or deceive investors. In response, the prosecution has suddenly, and dramatically, changed course, arguing for the first time that it is not even required to prove that Mr. Reyes thought that his conduct had any effect on Brocade's financial statements in order to convict him of securities fraud. (Government's Response ("Resp.") at 12). Indeed, the prosecution argues that the *only thing* it needs to prove to establish "criminal intent" is that Mr. Reyes thought that his conduct was "wrongful" in some undefined way, and that his conduct "involve[d] a significant risk of affecting" the securities laws. (Resp. at 3).

In an effort to defeat the deficiency identified by the Court, the prosecution's opposition to the Rule 29 motion undertakes two impossible tasks. First, contrary to its own prior articulations of the law, the prosecution seeks to re-write the central elements of fraud in order to eliminate the requirement that the prosecution prove a specific intent to cheat and deceive. Second, the prosecution seeks to spin the very same items of "evidence" that it listed at the July 6 hearing into proof of a criminal state of mind.

Respectfully, the Court should reject the prosecution's legal argument as it requires the Court to sweep aside over a hundred years of case law and common law holding that a specific intent to cheat and deceive is at the heart of every fraud case, whether it be common law fraud, mail fraud, wire fraud, or federal securities fraud, as the prosecution has charged here. The government's slimmed-down, intent-free, "all you have to prove is that the defendant thought it was wrong" version of securities fraud is simply not the law.

The prosecution's creative attempt to rewrite the law, moreover, cannot change the evidence — or, in this case, *lack of evidence* — in the record. At the July 6 hearing, the Court put it plainly to the

prosecution: show me the evidence that proves that Mr. Reyes understood APB 25 and was aware that stock option compensation expenses were not being properly recorded on the company's financial statements and disclosed in its SEC filings. In response, the prosecution identified no new evidence, relying instead on the same arguments already advanced and seemingly rejected by the Court at the July 6 hearing. Because the prosecution's legal arguments are flawed, and because it has presented no new evidence from the record demonstrating Mr. Reyes's knowledge about the relevant accounting principles or about the inaccuracies in Brocade's financial statements (because there is no such evidence in the record), the Court should grant Mr. Reyes's motion for judgment of acquittal.

II. ARGUMENT

A. The Prosecution Must Prove that Mr. Reyes had a Specific Intent to Cheat and Deceive and That He Acted "Willfully"

In a criminal prosecution for securities fraud, the prosecution must prove two essential elements that speak to the defendant's *mens rea*.[2] First, the prosecution must prove that defendant acted with "scienter," which means a "mental state embracing intent to deceive, manipulate or defraud." *United States v. Stewart*, 305 F. Supp. 2d 368, 371 (S.D.N.Y. 2004) (quoting *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193, 96 S. Ct. 1375, 1381 (1976)); *see also United States v. Tarallo*, 380 F.3d 1174, 1181 (9th Cir. 2004) (requiring that the government prove "specific intent to defraud, mislead, or deceive"). Second, "the Government must *also* prove that the defendant acted 'willfully,' that is, with a realization that she was acting wrongfully." *Stewart*, 305 F. Supp. 2d at 371 (citation omitted) (emphasis added).

Recognizing that it cannot overcome the fatal factual shortcomings in its evidence, the prosecution tries to tilt the playing field by writing the specific intent requirement out of the law altogether[3] and watering down the "willfulness" requirement. The prosecution insists that it only has

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[2] The government must also prove several other elements to prove securities fraud, including that defendant's statements were "material" and that defendant "used the means and instrumentalities of interstate commerce," *see* Reyes's Jury Instructions, No. 38 (Doc 321) at 41, but those do not pertain to defendant's state of mind, or *mens rea*.

[3] Contrary to the prosecution's apparent belief (Resp. at 3–8, 12), a "specific intent" to defraud does not mean an intent to violate a known statutory or regulatory provision. Accordingly, the fact that the *(cont'd)*

to prove three basic elements to support a charge of securities fraud: *first*, that defendant acted "willfully" or "wrongfully"; *second*, that defendant's conduct violated the securities laws; and *third*, that defendant's conduct, "whether he knew it or not," involved "a significant risk of affecting the violation [of the securities law] that has occurred." (Resp. at 3). The prosecution contends that as long as "the evidence establishes that the defendant acted knowing that he was doing a wrongful act," the government need do no more to prove the required "criminal intent." (*Id.*). Indeed, the prosecution asserts that it need not even prove that Mr. Reyes "had knowledge of the [applicable] accounting rules" or "knew that his wrongful conduct had accounting implications for Brocade." (*Id.* at 12). In the prosecution's view, it is apparently enough if the defendant "willfully participated in an act that involves a 'significant risk' of violating the securities laws," whether or not he understood the relevant accounting provisions. (*Id.* at 5). The prosecution contends that this admittedly "'modest' level of proof of scienter" is justified in securities fraud cases because "a criminal conviction under those laws 'necessarily involves fraudulent conduct.'" (*Id.* at 7).

Based on this novel view of the law, the prosecution argues that "the common elements of the securities fraud violations at issue in this trial" can be reduced to two questions: *First*, did the defendant do something that he knew was "wrongful"? *Second*, "did the defendant's conduct involve a 'serious risk'" of violating the securities laws? (Resp. at 8). The prosecution claims that it has satisfied this first element merely by showing that Mr. Reyes signed stock option grant minutes with earlier dates on them, and that it has satisfied the second element because the misdated grant lists ultimately led to the misstatements in the financial statements. (*Id.*). But the prosecution's view of the law – and its circular logic, that a lesser standard of scienter is required for securities law cases because they "necessarily involve[] fraudulent conduct" (*Id.* at 7) — has never been adopted by the Ninth Circuit or any other federal court.

(cont'd from previous page)
government need not prove a "specific intent" to violate a known law (cf. *Tarallo*, 380 F.3d at 1181) does not absolve it from the burden of proving a specific intent to cheat and deceive.

1. The Prosecution Has Not Proved That Mr. Reyes Had A Specific Intent to Cheat and Deceive Investors

The central element of securities fraud, as with any other form of fraud, is the requirement that the government prove "scienter," which consists of a specific "intent to deceive, manipulate, or defraud." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, ___ S. Ct. ___, 2007 WL 1773208, at *7 (June 21, 2007) ("To establish liability under §10(b) and Rule §10b–5, a private plaintiff must prove that the defendant acted with scienter, 'a mental state embracing intent to deceive, manipulate or defraud'") (citation omitted); *Ernst & Ernst,* 425 U.S. at 193, 96 S. Ct. at 1381 (plaintiffs must prove specific intent to defraud in civil action for securities fraud); *United States v. Milwitt*, 475 F.3d 1150, 1156 (9th Cir. 2007) (government must prove "a specific intent to defraud" to prove bankruptcy fraud); *United States v. Tarallo*, 380 F.3d 1174, 1181 (9th Cir. 2004) (government must prove "specific intent to defraud, mislead, or deceive" in criminal securities fraud case); *United States v. Sayakhom*, 186 F.3d 928, 941 (9th Cir.), *amended by* 197 F.3d 959 (9th Cir. 1999) ("government must prove specific intent to defraud" to convict for mail fraud); *United States v. Bonallo*, 858 F.2d 1427, 1433 (9th Cir. 1988) ("specific intent to deceive or defraud" required to convict for mail or wire fraud); *United States v. Brown*, 578 F.2d 180, 1284 (9th Cir. 1978) ("specific intent" required to convict for securities fraud). Indeed, the model jury instructions in this Circuit clearly instruct that "an intent to defraud is an intent to deceive or cheat." *Ninth Circuit Model Criminal Jury Instructions,* Instruction No. 3.17 (2000 ed.). In fact, the intent to cheat or deceive has been the hallmark of fraud cases in the United States, civil or criminal, common law or statutory, for well over a hundred years. *See*, *e.g., Lord v. Goddard*, 54 U.S. 198, 211, 14 L. Ed. 111 (1851) ("Fraud means an intention to deceive. If there was no such intention; if the party honestly stated his own opinion, believing at the time that he stated the truth, he is not liable in this form of action . . . .") (reversing jury verdict against defendant in common law fraud case).

In *Ernst & Ernst*, for example, plaintiffs brought civil claims against Ernst & Ernst, a large national accounting firm, under Section 10(b) of the Securities Exchange Act, 15 U.S.C. § 78j(b) and SEC Rule 10b–5 — the same provisions at issue here — alleging that Ernst had negligently failed to uncover a large fraud committed by a brokerage firm during Ernst's audits of the firm. 425 U.S. 185.

In rejecting the plaintiffs' claims that Section 10(b) could support a claim for negligence, the Court noted that the use of the word "manipulative" was "especially significant" in connection with the "securities markets." *Id.* at 199. "It connotes intentional or willful conduct *designed to deceive or defraud investors* by controlling or artificially affecting the price of securities." *Id.* (emphasis added). The Court noted, moreover, that "[t]he words 'manipulative or deceptive' used in conjunction with 'device or contrivance' strongly suggest that § 10(b) was intended to proscribe knowing or intentional misconduct." *Id.* at 197 (citing *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 868 (2d Cir. 1968) (Friendly, J. concurring)).

Similarly, in *Tarallo*, a case that the prosecution relies upon heavily, the Ninth Circuit held that "a defendant may be convicted of securities fraud only if the government proves specific intent to defraud, mislead, or deceive." 380 F.3d at 1181. The defendant in *Tarallo* was involved in a telemarketing scheme that solicited people to invest in various fictitious businesses. Defendant and his co-defendants falsely represented to the investors, among other things, that one company they were investing in was affiliated with Tom Brokaw and operated weight loss clinics around the country; another company had recently won FDA approval for a detoxification system and expected to generate $187 million in revenue in the coming year; and that all the investors' money would be safe and held in a trust. *Id.* at 1180. In affirming the securities fraud convictions, the Ninth Circuit noted that there was ample evidence from which "[a] reasonable [juror] could have found beyond a reasonable doubt that Defendant knew of the fraudulent nature of the scheme in which he was participating." *Id.* at 1181. *See also Stewart*, 305 F. Supp. 2d at 375–78 (granting defendant's Rule 29 motion on grounds that "the evidence and inferences" regarding Martha Stewart's three public statements regarding her sale of ImClone stock were "simply too weak to support a finding beyond a reasonable doubt" that Stewart had "criminal intent" to defraud investors in her own company).

Here, no rational juror could find beyond a reasonable doubt an intent to defraud because there is no evidence that Mr. Reyes understood the relevant accounting opinions, realized that Brocade's stock option granting practices required accounting charges, and knew that Brocade failed to properly

report those accounting charges in its financial statements and public filings. Mr. Reyes's motion for a judgment of acquittal should therefore be granted.

2. The Prosecution Has Not Proved that Defendant Acted "Willfully"

The prosecution argues that in lieu of proving that defendant had the specific intent to cheat or deceive and knowledge that his statements were false, the government need only prove that the defendant acted "wrongfully" and that his conduct "involve[d] a significant risk of affecting the violation that has occurred." (Resp. at 3:8–13) (citing *Tarallo*, 380 F.3d at 1187). Indeed, the prosecution suggested at the July 6 hearing that all it had to prove "with respect to scienter" was that Mr. Reyes believed that the "look backs" were "wrongful" in some vague and undefined way. (7/6/07 RT 2239:5–11) (Mr. Crudo: "[I]f he [i.e., Mr. Reyes] understands that what he's doing is wrongful, that satisfies the scienter requirement"). This is simply not the law, however. The "willfulness" or "wrongfulness" element is something which must be proved ***in addition to, not in place of,*** a specific intent to cheat and deceive. See *Tarallo*, 380 F.3d at 1185–89; *Stewart*, 305 F.Supp.2d at 371 ("the Government must *also* prove that defendant acted 'willfully'") (emphasis added). While the government need not prove that the defendant was aware of the particular statute or SEC regulation he violated, the government must, at the very least, prove that the defendant willfully and intentionally engaged in the conduct that led to the alleged crime, that he intended the consequences of his conduct, and that he knew the ultimate result was in some way wrongful. *See Tarallo*, 380 F.3d at 1187.[4]

The case law suggests that the "willfulness" requirement has three sub-elements. First, the prosecution must prove that the defendant's conduct was intentional, that is, that it was "not the product of accident or mistake." *Tarallo*, 380 F.3d at 1187. Second, in cases such as this, where the defendant is charged with making a false or misleading representation, the prosecution must prove that the

[4] It bears emphasis that these elements are all part of the willfulness requirement, and that, as discussed above, the prosecution *also* has to prove a specific intent to defraud. (Resp. at 3 (presenting the willfulness criteria as if they alone established "criminal intent"). So much is made clear by the discussion in *Tarallo* itself. Only *after* concluding that the government had successfully established that the defendant acted with "specific intent to defraud," 380 F.3d at 1181–82 — an element that must be proved in civil and criminal securities fraud cases alike — did the Court then turn its attention to the willfulness element, which is, of course, unique to the criminal context, *see id.* at 1188.

defendant knew the representation was false (or at the very least, that defendant made the representation with a reckless indifference to its truth or falsity). *Id.* at 1188. Third, the charged conduct must be done with "a realization on the defendant's part that he was doing a wrongful act." *United States v. Charnay*, 537 F.2d 341, 352 (9th Cir. 1976) (citation omitted). For purposes of this case, the important elements are the second and third above.

(a) The prosecution has not proved that Mr. Reyes understood the relevant accounting opinions and knew that Brocade's financial statements were inaccurate – "generalized imputations of knowledge do not suffice, regardless of the defendant's position within the company[5]

Despite the Court's express admonition at the July 6 hearing that this is an accounting fraud case, and that the government must prove, beyond a reasonable doubt, that Mr. Reyes understood the relevant principles underlying the accounting opinions (7/6/07 RT 2228:2–7, 12–14), the prosecution tries to circumvent the requirement that the defendant knew that his statements were false. Section 32 of the Exchange Act, 15 U.S.C. § 78ff, the penalty provision for all the substantive counts in the Indictment, specifically requires the prosecution to prove that Mr. Reyes "willfully" or "willfully and knowingly" made false statements in the relevant Form 10-Ks and other documents charged in the Indictment.[6] 15 U.S.C. §§ 78j(b), 78ff. As the Ninth Circuit has observed, "'willfully' in the context of section 78ff mean[s] 'voluntarily and knowingly wrongful.'" *Tarallo*, 380 F.3d at 1189.[7] A defendant

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[5] *In re Advanta Corp. Sec. Litig.*, 180 F.3d 525, 539 (3d Cir. 1999).

[6] Counts Five through Seven allege that Mr. Reyes "knowingly and willfully" made or caused Brocade to make false statements (or omit to state material facts) in the Form 10-Ks for the fiscal years ending October 2001, October 2002, and October 2003. (Indictment, ¶¶ 40-48). These counts, thus, track the language in the second clause of 15 U.S.C. § 78ff, which requires the government to prove that defendant acted "willfully and knowingly."

[7] Although *Tarallo* upheld the use of the recklessness standard, it did so in a different setting and it is not clear that it would apply here. *Tarallo* did not involve false filings counts subject to the second clause in section 78ff, but rather particular transactions that occurred as part of an independently and obviously fraudulent scheme or practice. *See Tarallo*, 380 F.3d at 1184. *Tarallo*, therefore, did not involve the second provision of section 78ff, but rather a violation of Rule 10b-5's prohibition against fraudulent schemes and practices, which are criminally punishable "under the first provision of § 78ff." *Id.* at 1187. For false statement counts such as those at issue in Counts Two and Five through Seven, however, the statute requires that the defendant *make false statements* willfully and knowingly, a standard that cannot be met by mere recklessness.

cannot make false statements in a "knowingly wrongful" manner without knowing the statements are false. *See, also, United States v. O'Hagan*, 139 F.3d 641, 647 (8th Cir. 1998) (on remand from Supreme Court, 521 U.S. 642 (1997)).[8]

Significantly, the prosecution is now trying to backtrack on the very legal standard it already endorsed, accepted, and assumed at the outset of this case almost a year ago. The prosecution now claims that a CEO may be convicted of felony securities fraud even if he had absolutely no idea that any of his conduct could affect the company's financial statements or affect investors, the public, or the market. The prosecution had it right back in August, 2006. The government simply cannot seek to convict a defendant for making false or misleading statements in the company's financial statements, or anywhere else, without first proving that the defendant knew that the statements were false.

The district court's decision in *SEC v. Lucent Technologies, Inc.* is directly on point. 2005 WL 1206841 (D. N.J. May 20, 2005) (granting defendant Dorn's motion to dismiss SEC's complaint, pursuant to F.R.C.P. 9(b) and 12(b)(6)). In *Lucent*, the SEC charged that Alice Dorn, a vice-president of sales for Lucent had engaged in a pattern of orally entering into side agreements with two of Lucent's distributors that resulted in Lucent improperly recognizing and reporting millions of dollars of revenues on its financial statements. *Id.* at * 3. Although the SEC alleged that Dorn knew or was "reckless in not knowing, that the verbal side agreements made revenue recognition improper under

[8] The Ninth Circuit in *Tarallo* held that recklessness as to the falsity of a statement, rather than actual knowledge thereof, could suffice to prove that a defendant "willfully" violated Rule 10b-5. *See* 380 F.3d at 1186-88. For at least three reasons, that holding has no bearing here. First, in this case, where the prosecution is charging Mr. Reyes with "knowingly and willfully" failing to properly record Brocade's stock option expenses in Brocade's financial statements and Form 10-Ks (*see*, *e.g.*, Indictment, ¶¶ 37, 41-42, 44-45, 47-48), it is hard to imagine how the recklessness standard could even apply because the allegations of false statements that Mr. Reyes is accused of making necessarily encompass and rely upon the prosecution's claims that Mr. Reyes *knew* and *understood* the relevant accounting opinions. If Mr. Reyes did not know that these opinions required Brocade to record expenses for its stock option program — and there is no evidence in the record that he did — then the prosecution cannot possibly establish that Reyes's statements were knowingly or even recklessly false. Second, given the technical nature of the accounting opinions at issue here, it is hard to imagine how the prosecution could prove "recklessness" short of eliciting testimony that Mr. Reyes was somehow informed that the financial statements were inaccurate, and that he consciously disregarded that information and caused them to be filed anyway. The government, of course, presented no such evidence. Thus, even if recklessness *were* enough, the case still should not go to the jury.

GAAP," *id.* at *2, and that Dorn had even falsely told Lucent's chief accountant that there were no verbal agreements or side deals, the court dismissed the claims against Dorn because there were "no allegations from which the Court could infer that Dorn had any knowledge of accounting principles or that she had any role in Lucent's decisions to recognize revenue" in connection with the subject transactions. *Id.* at *5. In justifying its decision, the court noted that the SEC had failed to offer any "compelling reason why this Court should charge regular business people with knowledge of accounting principles." *Id.* (noting that "'[g]eneralized imputations of knowledge do not suffice, regardless of the defendant's positions within the company'") (citing Advanta, 180 F.3d at 539) (alteration in original).

The same is true here. If a district court cannot infer a defendant's knowledge of the relevant accounting opinions on a civil motion to dismiss, surely a rational juror in a criminal case cannot infer beyond a reasonable doubt that Mr. Reyes understood the relevant accounting opinions based purely on the prosecution's meager "evidence" and Mr. Reyes's position as the CEO.[9]

(b) The prosecution has not proved that Mr. Reyes's conduct was wrongful

In response to Mr. Reyes's Rule 29 motion, the prosecution must also prove, beyond a reasonable doubt, that Mr. Reyes knew his conduct was "wrongful" and that his sense of "wrongfulness" was connected in some way to the underlying criminal allegations. *United States v.*

[9] It is well-established that an officer or director's signature or electronic signature on a financial statement or Form 10-K alone, without additional evidence of his or her knowledge that the statement contains false or misleading information, is not enough even to survive a civil motion to dismiss. And if it is not enough even to state a claim in a civil lawsuit, it certainly cannot be the basis for surviving a Rule 29 motion in a criminal case. *See e.g., In re Cendant Corp. Sec. Litig.*, 76 F. Supp. 2d 539, 547 (D.N.J. 1999) ("[a]llegations that a director or officer signed public disclosures and/or was involved in the company's daily operations, standing alone, will not satisfy the pleading requirements of the PSLRA or Rule 9(b)") (citation omitted); *In re Keyspan Corp. Sec. Litig.*, 383 F. Supp. 2d 358, 388 (E.D.N.Y. 2003) (plaintiff's argument that the CEO and CFO signed the allegedly false statements say "nothing about whether they intended to defraud investors in doing so"); *Goplen v. 51job, Inc.*, 453 F. Supp. 2d 759, 775 (S.D.N.Y. 2006) (that "CEO signed the SEC filing — without specific allegations of reasonably available facts that should have put him on notice that the reported financial results were false — does not give rise to a strong inference of scienter"); *Cf.*, *United States v. McCormick*, 72 F. 3d 1404, 1410 (9th Cir. 1995) (defendant's signature on bankruptcy documents was not sufficient evidence that she understood that their contents were false; conviction reversed for insufficiency of evidence).

Charnay, 537 F.2d 341, 352 (9th Cir. 1976) (citation omitted). In *Tarallo*, for example, the court held that in order to establish that defendant's actions were "willful" under Section 10(b) of the Exchange Act, the prosecution had to prove "'a realization on the defendant's part that he was doing a wrongful act.'" *Tarallo*, 380 F.3d at 1187 (quoting *United States v. Charnay*, 537 F.2d 341, 352 (9th Cir. 1976) (citation omitted)). The prosecution must also prove that "'the [defendant's] knowingly wrongful act involved a significant risk of effecting the violation that has occurred.'" *Charnay*, 537 F.2d at 352 (citation omitted).

Accordingly, the prosecution needs to prove beyond a reasonable doubt that Mr. Reyes understood that Brocade's option-granting practices required Brocade to take compensation expenses, knew that Brocade's financial statements were materially false, understood that these false statements were "wrongful," and *knew all of that at the time of the option grants at issue here*. It is not enough, as the prosecution has suggested, to prove merely that Mr. Reyes thought that the look-backs or backdating of options were "wrong" in some undefined way — especially when, as the Court has pointed out, backdating is not illegal. *See Tarallo*, 380 F.3d at 1188 (prosecution must prove that the defendant "undertook acts that he *knew at the time* to be wrongful") (emphasis added).

In seeking to demonstrate that this element has been satisfied, the prosecution makes an impermissibly large leap. It claims that merely by signing in February 2002 a grant document dated November 2001, Mr. Reyes was knowingly engaged in obviously wrongful conduct. (Resp. at 10:1–12). There is no evidence that Mr. Reyes thought his conduct in regard to the stock option grants for the years 2001 through 2002 was anything other than proper, however. And the government has not placed Mr. Reyes's conduct before or after that time at issue in this case.

The "wrongful" cases cited by the prosecution here involved conduct that was obviously improper and therefore easily distinguishable from Mr. Reyes's alleged acts. In *Tarallo*, for example, there was ample evidence that Mr. Tarallo "knew of the fraudulent nature of the scheme in which he was participating." 380 F.3d at 1181. Indeed, the entire telemarketing initiative was nefarious and Tarallo blatantly lied in the course of his participation — telling potential investors that their investments were safe (even though Tarallo knew that he was drawing his salary from them) and that

he was calling from Washington, D.C. when he was actually in California. *Id.* at 1182. The claim that he was an unwitting participant simply didn't pass the straight face test. Therefore, even if Tarallo did not specifically know he was violating the securities law, he certainly knew he was involved in an inherently deceitful and thus "wrongful" activity and that he was directly deceiving investors to obtain their money.

The same is true of the Ninth Circuit's decision in *United States v. Charnay*, 537 F.2d 341 (9th Cir. 1976) (reversing dismissal of an indictment alleging securities and wire fraud). The indictment in *Charnay* alleged that defendants entered into a secret deal to depress stock prices in retaliation for the board of directors rejecting a corporate buy-out. The district court called such alleged conduct "reprehensible," and the Ninth Circuit held that the indictment sufficiently alleged a violation of 15 U.S.C. § 78j(b) and Rule 10-b. *Charnay,* 537 F.2d at 345, 352.

Similarly, in *United States v. English*, the Court observed that "there can be no doubt about the inherently nefarious nature of English's fraudulent scheme." 92 F.3d 909, 915 (9th Cir. 1996). Thus, even though the government did not have to prove that the defendant knew he was breaking the law to satisfy the "willfulness" element of 15 U.S.C. §§ 77q(a) and 77x, the conviction did not run afoul of *Ratzlaf v. United States*, 510 U.S. 135, 114 S.Ct. 655 (1994), and similar authorities because the conduct at issue was "obviously evil." *English*, 92 F.3d at 916.

The activity in all of these cases was in some important respect *malum in se*. Mr. English took investors' money under false pretenses and used it to enrich himself rather than to make the investments and loans he promised to make. Even if he did not know this constituted mail and securities fraud, he knew he was doing something with a bad purpose. In *Charnay*, the defendants were charged with a complicated — and secret — scheme designed to depress their company's stock price in an act of revenge against the board of directors. And Mr. Tarallo blatantly lied to the victims of his fraud. The obviously "evil" nature of these offenses demonstrated the defendants' specific intent, so it did not matter whether they knew what law or laws they might be violating. They acted without regard to obvious legal ramifications of some sort.

The facts here are very different. All the prosecution has arguably proved Mr. Reyes to have done here was (1) signed grant lists and committee minutes that contained dates earlier than the dates on which Mr. Reyes signed them, and (2) signed Form 10-Ks or management representation letters that were later found to be inaccurate. There is no evidence that Mr. Reyes knew or had reason to believe that there was anything "wrongful" or nefarious about signing corporate documents that contained an earlier date. Indeed, even if he had thought so, as the Court has noted, "we all know it's not illegal to backdate options." (7/6/07 RT 2228:8–9). The only way that Mr. Reyes could have known that signing grant lists or committee minutes with earlier dates was somehow wrong or deceitful is if he had also understood the relevant accounting opinions and understood that the Finance Department was not accurately accounting for stock option expenses.

The same goes for Mr. Reyes's role in signing or causing the filing of the Form 10-Ks, certifications, and representation letters to Brocade's auditors. There is simply no evidence that Mr. Reyes knew that these documents were false, misleading or inaccurate. None. Not a single person has testified that he or she told Mr. Reyes that the financial statements or Form 10-Ks were inaccurate and there is not a single e-mail, letter or other document which would suggest otherwise. Accordingly, there is no evidence from which a rational juror could infer beyond a reasonable doubt that Mr. Reyes had the specific intent to cheat or deceive investors, and that he appreciated that his actions were "wrongful." Mr. Reyes's motion for judgment of acquittal must be granted.

B. The Prosecution Has Failed to Address the Concerns Raised by the Court at the July 6 Hearing or To Prove That Reyes Violated the Securities Laws

As set forth previously, at the July 6 hearing, the Court directed the prosecution to identify all of the evidence demonstrating that Mr. Reyes: (1) understood the accounting principles underlying APB 25; and was aware that (2) Brocade's stock option granting practices required the expensing of stock options under APB 25 and that (3) the company's financial statements and disclosures were inaccurate because they did not include those non-cash stock option compensation expenses. **In response, the prosecution has identified no new evidence, but has instead relied on the same evidence proffered at the July 6 hearing**. None of the proffered evidence would lead a rational juror to find beyond a reasonable doubt that Mr. Reyes understood the accounting principles underlying

APB 25, realized that Brocade's stock option practices required an accounting charge under APB 25, and knew that Brocade's stock options were not being properly recorded in the Company's financial statements. All of the purported evidence remains as unpersuasive today as it was on July 6th.

1. The Morrison & Foerster Interview Does Not Support an Inference That Mr. Reyes Knew That Look-Backs Were Wrongful

The prosecution contends that Craig Martin's testimony, that Mr. Reyes said in a January 2005 interview that he did not use look-backs to price option grants, was a false exculpatory statement that can now be used to demonstrate that Mr. Reyes knew in 2001 and 2002 that the use of look-backs to price stock options was wrongful. Nothing could be further from the truth. Even if the Court believes that there is sufficient evidence of Mr. Reyes's purported awareness of the look-back pricing to render the purported statements inaccurate, the statements shed no light on the relevant question — Mr. Reyes's knowledge and state of mind in 2001–2002. This is because Mr. Reyes's purported statements to Mr. Martin were made in January 2005 — ***three years after the relevant time period***. Whether Mr. Reyes thought look-backs were wrongful in January 2005 is not probative of whether he thought they were wrongful three years earlier, when he is alleged to have committed the charged fraud. As the Court correctly observed at the July 6 hearing: "The question is: Did he have that state of mind . . . in 2000, 2002?" (7/6/02 RT at 2257:15–17.) The prosecution has no evidence which answers that straightforward question.

The Ninth Circuit and other circuits have rejected attempts, such as the one now tried by the prosecution, to prove knowledge of wrongfulness with after-the-fact, allegedly false exculpatory statements because such evidence "is as consistent with innocence as with guilt." *See United States v. Cassese*, 428 F.3d 92, 101 (2d Cir. 2005) ("To the extent Cassese sought to cancel the trade because he realized that the stock purchase was unlawful, it is equally possible that he realized this on the day he sought to cancel the trade as on the day of the purchase."); *United States v. Rahseparian*, 231 F.3d 1257, 1262–64 (10th Cir. 2000) (reversing conviction for mail fraud and conspiracy because only evidence of defendant's contemporaneous knowledge of fraudulent activities was false exculpatory statement he made a year and a half after business ceased operations); *United States v. Lorea*, 72 F.3d

136, 1995 WL 729504, *4 (9th Cir. Dec. 7, 1995) (reversing conviction for aiding and abetting on ground that defendant's nervousness and false statements to customs agents were insufficient to show intent). As the Ninth Circuit aptly stated in *Lorea*: "False exculpatory statements are weak circumstantial evidence because the innocent as well as the guilty may lie when confronted with criminal charges." *Id.*, 1995 WL 729504, at *4.

These courts have uniformly held that an after-the-fact false exculpatory statement is legally insufficient proof of guilt absent strong independent evidence of guilt, which simply does not exist here. *See, e.g., United States v. Abraham*, 617 F.2d 187, 191 (9th Cir. 1980) ("[F]light and false exculpatory statements standing alone will not lead to a conviction absent other independent evidence."); *United States v. Morrison*, 220 Fed. Appx. 389, 397 (6th Cir. 2007) ("[B]ecause the Government, not Morrison, carries the burden of proof throughout the entire trial, Morrison's unbelievable narrative cannot be used as a sword against him where the Government has not otherwise proffered sufficient evidence of his guilt."). "[A]lthough evidence of after-the-fact consciousness of guilt may have independent probative force, and may strengthen inferences supplied by other pieces of evidence, such evidence is 'insufficient proof on which to convict where other evidence of guilt is weak and the evidence before the court is as hospitable to an interpretation consistent with the defendant's innocence as it is to the Government's theory of guilt.'" *Cassese*, 428 F.3d at 101 (quoting *United States v. Johnson*, 513 F.2d 819, 824 (2d Cir. 1975)). Because the prosecution has no competent evidence of guilt, its reliance on the Martin testimony is legally insufficient.

The cases cited by the government in support of its position are inapposite. The opinions in *United States v. Perkins*, 937 F.2d 1397 (9th Cir. 1990) and *United States v. Wood*, 550 F.2d 435 (9th Cir. 1976), merely concerned the propriety of jury instructions relating to false exculpatory statements. As the Court has already explained, "[W]e are not talking about what the appropriate instructions are. ***We are talking about whether, given the state of the evidence, there is enough to go to a jury***." (7/6/07 RT at 2238:17–21 (emphasis added).) The other cases cited by the government are also distinguishable because, unlike here, the prosecutors in those cases had presented strong independent, contemporaneous evidence of knowledge or intent. *See United States v. Newman*, 6 F.3d 623, 628 (9th

Cir. 1993); *United States v. Ruggiero*, 56 F.3d 647, 655–56 (5th Cir. 1995); *SEC v. Musella*, 748 F. Supp. 1028, 1038–40 (S.D.N.Y. 1989). Accordingly, a rational juror could not find beyond a reasonable doubt based on Martin's testimony that Mr. Reyes believed that the look-back pricing was wrongful during the relevant time period.

2. The Management Representation Letters to KPMG Do Not Prove Reyes's Knowledge of Stock Option Accounting

The prosecution next argues that the November 18, 2002, management representation letter to KPMG (Ex. 44) constitutes evidence that Mr. Reyes "knew the accounting implications of his fraud." (Resp. at 12). The prosecution is wrong.

As set forth in the motion for judgment of acquittal, the management representation letter was signed by Tony Canova, the then-CFO, *and* Mr. Reyes. (Ex. 44). It was eight pages long and contains 32 paragraphs of representations, most of which are accounting and legal representations about which Mr. Reyes would have had no knowledge. Even prosecution witness Neil Miotto ("Miotto"), the KPMG partner who oversaw the Brocade audits, testified that the representations in a management representation letter pertain to accounting and legal matters and he did not expect "the CEO to go dig up that information." (6/27/07 RT 1415:19–1417:16). Accordingly, Mr. Reyes's need to rely on the Finance Department in connection with the representations set forth in the management representation letters was a fact fully anticipated and embraced by KPMG.

The representation letters were also prepared as part of a lengthy process in which the Finance Department negotiated the language of the letter which was drafted by KPMG. (Miotto: 6/27/07 RT 1411:21–23; 1412:11–19). Mr. Reyes had no involvement in that process, however. (*Id.*, 1411:10–1412:19). There is no evidence that Mr. Reyes reviewed or understood each paragraph of the representation letter when he signed it. No witness has testified that he or she even explained or discussed the letter with Mr. Reyes, or observed Mr. Reyes read or review it.

Moreover, paragraph 31 (Ex. 44), which deals with the Company's accounting for stock options, merely reflects that "[s]tock-related awards to employees have been accounted for in accordance with the provisions of APB Opinion 25 . . . ." Nowhere does the letter describe the

provisions of APB 25, and no witness has testified that he or she explained the accounting principles underlying APB 25 to Mr. Reyes. Mr. Miotto testified that he never gave any guidance to Mr. Reyes regarding APB 25. (*Id.*, 1418:4–13). This paragraph speaks to an accounting treatment employed by the Finance Department. The prosecution has presented no evidence suggesting that Mr. Reyes was specifically aware that the Finance Department was not following that accounting treatment. Accordingly, no rational juror could find beyond a reasonable doubt that the management representation letters informed Mr. Reyes regarding the accounting principles underlying APB 25 or that the company was not following those accounting principles.

3. Mr. Reyes's Certification on the 2002 Form 10-K Does Not Prove Reyes's Knowledge of Stock Option Accounting

The prosecution also relies on Mr. Reyes's electronic signature on the 2002 Form 10-K, along with the electronic certification submitted in connection with that filing. Without any evidence suggesting that Mr. Reyes actually read the relevant sentence about APB 25 in the 102 page document, the prosecution argues that his electronic signature is sufficient to establish knowledge (1) of the accounting principles underlying APB 25, (2) that the company's option granting practices required a compensation charge under APB 25, and (3) that the company was not in fact already reporting those charges within the 10-K. As the Court aptly noted, to accept the prosecution's argument would be akin to holding Mr. Reyes — and every other CEO in America — "strictly liable" for signing a Form 10-K that for whatever reason turned out to be incorrect. (7/6/07 RT 2244:22–2246:12). This is not the law.

At the July 6 hearing, the prosecution suggested that because Mr. Reyes certified that he had read Brocade's Form 10-K, he should be held responsible for every word stated therein. Mr. Reyes, however, never represented that he had thoroughly read or studied the 10-Ks, much less that he understood every paragraph therein. Indeed, it was not until fiscal year 2002 that the Form 10-Ks even began to include certifications.[10] In that year, Mr. Reyes signed a certification stating that he "reviewed this annual report on Form 10-K of Brocade Communications Systems, Inc." and that based

[10] There are no certifications in the Form 10-Ks for fiscal years 2000 and 2001. (*See* Exs. 17 and 22).

on his knowledge, the report does not contain any untrue statements of material fact or omit any material fact. (*See* Ex. 27 at 80). The prosecution has failed to introduce any evidence, however, describing the process by which Mr. Reyes "reviewed" the 10-K.

The prosecution also suggests that Mr. Reyes's signature and certification on Brocade's 2002 10-K should be "viewed as a statement" by Mr. Reyes "that he knew that" his signing of grant minutes with earlier grant dates "would have direct accounting consequences that would cause Brocade to under-report its compensation expenses." (Resp. at 13). This inference is simply not supported by any evidence, and would require the jury to make a huge leap of logic based on speculation, rather than evidence, which the law expressly forbids. *United States v. D'Amato*, 39 F.3d. 1249, 1256 (2d Cir. 1994) (conviction cannot stand on "speculation and surmise" alone).

First, there is no evidence that Mr. Reyes's understood the applicable accounting principles during the relevant time frame or that he realized that Brocade's option granting practices required Brocade to take compensation charges on its financial statements.

Second, even if he had known that Brocade's stock option granting practices required the company to take accounting charges on its financial statements, there is no evidence that Mr. Reyes was aware that Brocade's financial statements or 10-Ks did not include those charges. That is because each of Brocade's Form 10-K's were over 100 pages long and contained references to compensation expenses for stock options. For example, the Form 10-K for fiscal year 2002 is 102 pages long. On page 46 of the filing it states, "The Company accounts for its stock option plans and its Employee Stock Purchase Plan in accordance with the provisions of Accounting Principles Board Opinion 25, 'Accounting for Stock Issued to Employees,' (APB 25), whereby the difference between the exercise price and the fair value at the date of the grant is recognized as compensation expense." (Ex. 27 at 54). The prosecution suggests that from this single sentence, the jury could infer that Mr. Reyes allegedly learned (1) the accounting principles underlying APB 25; (2) that the company's stock option practices required the company to take accounting charges under APB 25; and (3) that the company was not recording those charges on its financial statements.

The description of the principle underlying APB 25 is far from clear, however.[11] More importantly, nothing in the Form 10-K would have put Mr. Reyes on notice that the Company did not, in fact, include the appropriate non-cash stock option compensation expenses. In fact, the inclusion of such expenses are included in the Form 10-K. (*see, e.g.,* Ex. 27 (2002 Form 10-K) at 38, 40). It is not until page 53 of the 2002 Form 10-K that the document even mentions that these stock option compensation expenses relate to grants made in 1999 and not in 2002. Thus, Mr. Reyes would have had to have reviewed and understood every line on every page of the 102-page Form 10-K (and to have understood the general principles underlying APB 25) to have the knowledge that the stock option expenses were not properly recorded in Brocade's Form 10-Ks. The prosecution, however, has failed to elicit testimony from even a single witness that Mr. Reyes read, reviewed, or discussed the Form 10-K, much less that he carefully checked the income statements, or that he understood the relevant language and realized that there were no compensation expenses recorded for retroactively priced options during the relevant time periods.

The fact that Mr. Reyes "reviewed" a 10-K in some fashion that had one cryptic sentence in it about compensation expenses does not constitute evidence that he understood stock option accounting principles, knew the financial statements were incorrect, and signed them anyway, which is what would be required to find him guilty of securities fraud or any of the other counts charged in the Indictment. No rational jury could find beyond a reasonable doubt that Mr. Reyes was guilty on this meager basis. To do so would transform this into a strict liability case, which it is not.

[11] For example, one of the key concepts embedded in the sentence is "date of grant." Neil Miotto, the KPMG engagement partner for Brocade testified that the term "grant date" or "date of grant" as it is described in the 10-K, is not defined in APB 25 and that both grant date and measurement date were concepts that needed to be understood in order to calculate compensation expense under APB 25. (Miotto: 6/27/07 RT 1445:3-20; *see also*, 6/28/07 RT 1659:18-1660:11) (according to Miotto, the requirement of an expense based on the grant date is "implied" in APB 25). Nowhere in the sentence is the concept of measurement dates explained, and the prosecution has not provided any testimony establishing that "date of grant" has a definitive meaning Mr. Reyes would or should have understood and been able to apply after he read this one sentence. In fact, Mr. Miotto testified that even accounting firms such as Ernst & Young, Arthur Andersen and KPMG had differing views of how to apply APB 25. (*See* Miotto 6/27/07 RT 1446:16-1452:6.)

4. Craig Martin's Testimony That Mr. Reyes Understood the Implication of Granting "In the Money" Options As of January 2005 Does Not Prove That Reyes Understood the Relevant Accounting Opinions In 2000 or 2002

The prosecution next relies on Craig Martin's testimony about his January 2, 2005 interview of Mr. Reyes. Two and a half years after the fact, Mr. Martin was able to testify to little more than that Mr. Reyes indicated that he became aware that granting "in-the-money" options had "accounting implications" *sometime* during his tenure as CEO (Martin: 7/2/07 RT 2201:4–7). Neither Martin's notes, nor his memoranda of the interview, prepared over one year after the interview, reflect the precise question asked or the answer given on this topic.

As set forth in the Rule 29 motion, even if the Court were to credit Martin's testimony, it sheds no light on what Mr. Reyes understood about the relevant accounting principles underlying APB 25, or on when Mr. Reyes came to this understanding. Indeed, Mr. Martin testified that he had never discussed either APB 25 or FAS 123 with Mr. Reyes. (7/2/07 RT 2203:17–18, 23–24). This is not competent evidence to support a beyond a reasonable doubt finding that Mr. Reyes understood the relevant accounting principles; that he understood that Brocade's practices triggered the responsibility to take compensation expenses on Brocade's financial statements; or that, even if he did understand these "accounting implications," he understood them during the relevant time period (2001–2002). Indeed, it is equally susceptible to the possibility that Mr. Reyes came to this understanding after the period of the alleged scheme or in the course of Brocade's internal investigation which was already two months old when Mr. Martin interviewed Mr. Reyes. *See United States v. Mulheren*, 938 F.2d 364, 372 (9th Cir. 1991) (where evidence is "'at least as consistent with innocence as with guilt,'" government must offer something more to tip the balance towards guilt) (citations omitted).

At the July 6 hearing, the Court correctly noted this fundamental flaw in the prosecution's reliance on Martin's testimony. The Court stated "And at what point — [when] is [it] reasonable to infer that he had some understanding of the accounting implications during the period of time that he was granting these options? What is the evidence of that?" (7/6/07 RT 2236: 23–2237:1). The straightforward answer to the Court's question is that there is no such evidence. Accordingly, no

rational juror could find beyond a reasonable doubt that Mr. Reyes had the requisite knowledge of the accounting principles underlying APB 25 based on Mr. Martin's testimony.

5. The iQuantic PowerPoint Presentation Does Not Prove Reyes's Knowledge of the Accounting Opinions

The prosecution next refers to an attachment to a June 9, 2003 e-mail sent by Stephanie Jensen to six individuals, including Mr. Reyes. (Ex. 187). The attachment is a 45-page PowerPoint presentation from iQuantic, which on page 28 contained a cursory reference to APB 25 and FAS 123. As the e-mail indicates, the presentation attached to the e-mail was not to be made to or even in the presence of Mr. Reyes but rather to the compensation committee of the Board of Directors. There is no evidence that Mr. Reyes ever reviewed this e-mail or the attachment, let alone reviewed and understood the specific reference to APB 25 on page 28. Nor is there any evidence that Mr. Reyes ever discussed the e-mail or its attachment with anyone. Even prosecution witness June Weaver testified that she never discussed APB 25, FAS 123 or stock option accounting with Mr. Reyes. (6/20/07 RT 571:24–572:1; 575:1–7)

Moreover, the e-mail was sent to Mr. Reyes in June of 2003. As set forth previously, the prosecution has elicited testimony relating to the purported non-cash stock option compensation expenses that the prosecution believes should have been recorded in 2001 and 2002, only. This e-mail was sent after 2002, and therefore cannot serve as the factual predicate for Mr. Reyes's knowledge of the relevant accounting opinions during the relevant time period, as defined by the prosecution's case-in-chief.

At the July 6 hearing, the Court, responding to the prosecution's proffer of this e-mail to support Mr. Reyes's knowledge of the relevant accounting opinions, stated:

> The Court: Okay. So it's not to him. She is not saying, "I'm giving you the document." She is saying, "I'm going to give this document to them." Okay. Now — and that's all that's in the cover. So my question is: What evidence do you have in the record, that you can point to, that Mr. Reyes actually opened up the attachment? I mean, people get things all the time. I get things from my law clerks. Of course, I read them all. But people — people get things all the time in attachments. Some people have the habit and custom of reading all the attachments, but here in this particular attachment she is saying, "I have

> something I'm going to give to somebody else." So what evidence in the record is there that Mr. Reyes ever saw the attachment, either opened this up, or got a copy of it, or had it discussed? What is the evidence in the record?
>
> Mr. Crudo: With respect to the direct evidence that he, in fact, opened this and reviewed this very document, I don't think there is any.
>
> The Court: There is no evidence. Okay. Now, there is no direct evidence.
>
> Mr. Crudo: Correct.

(7/6/07 RT 2233:3–25).

The Court was correct in its observations.

The prosecution also argues that Mr. Reyes proactively reached out to the group of employees who were studying the new stock option accounting opinion FAS 123, thereby showing a general interest in the rules. (Resp. at 16 n.6). This purported evidence proves nothing. As the Court recognized at the July 6 hearing:

> He may be interested, but, I mean, I would think that the chief executive officer of a company is interested in any number of things, and properly so. And we know he was interested in the – in granting the stock options. He had a large role in that. No question about it. But the question is: What evidence in the record is there that he actually understood the accounting implications of the granting of an in-the-money stock option? Okay? That's what I want – that's what I want you to address. What evidence is there that he actually understood?

(7/6/07 RT 2234:11–20).

FAS 123 relates to the expensing of all stock option grants using the Black-Scholes fair value methodology. It has nothing to do with the accounting principles underlying APB 25. It has nothing to do with whether Mr. Reyes was aware that the company's stock option granting practices required an accounting charge under APB 25 or whether those charges were recorded on the company's financial statements or disclosures. Accordingly, no rational juror could find beyond a reasonable doubt that Mr. Reyes had the requisite knowledge of APB 25 based on the June 2003 e-mail or the e-mails relating to FAS 123.

6. The Bidzos E-mail Does Not Establish That Reyes Had Knowledge About APB 25 or Intent To Deceive

The prosecution again raises the October 2004 e-mail exchange between Jim Bidzos and Reyes (Ex. 648), and suggests that it is evidence of Mr. Reyes's knowledge that the look-back pricing conducted at Brocade was wrongful. The prosecution misreads and misinterprets this e-mail exchange. First, the e-mail was dated October 8, 2004. The prosecution, however, has only elicited testimony relating to non-cash stock option expenses associated with grants from 2001 through 2002. Because the e-mail exchange falls outside the scope of the relevant time period by two years, it cannot be relied upon by the prosecution to demonstrate Mr. Reyes's knowledge in the relevant time period. (7/6/07 RT 2257:13–17) (framing the relevant question as whether Mr. Reyes had the requisite criminal state of mind in 2000 to 2002).

Moreover, the e-mail exchange specifically relates to grants for §16(b) officers. Due to the passage of the Sarbanes Oxley Act, starting on August 29, 2002, notification of such grants made to senior officers had to be made to the SEC within two business days of the grant. Public Accounting Reform and Investor Protection Act, 15 U.S.C. §78p (2002). This is clearly the rule to which Mr. Reyes was referring when he stated to Mr. Bidzos (Exhibit 648) that "under the current law" it was illegal to backdate. Because the e-mail refers expressly to options granted to §16(b) officers, the retroactive pricing proposed by Verisign's CFO could not be lawfully done. Under Sarbanes Oxley, Mr. Reyes's response makes perfect sense. The e-mail clearly does not speak to Brocade's stock option granting program or to the grants made to new hires and other Brocade rank and file employees. Accordingly, no rational juror could find beyond a reasonable doubt that Mr. Reyes had the requisite knowledge of APB 25 based on the Bidzos e-mail.

Most critically, as the Court has recognized, a generalized statement that backdating was illegal is incorrect — it is and was not illegal to backdate. Thus, any understanding Mr. Reyes had to that effect would have been unfounded. As such, the evidence cannot support a finding that he engaged in knowingly wrongful conduct — since the conduct, as the prosecution must concede, was *not* wrongful.

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7. Ms. Weaver's Testimony About Mr. Reyes's Purported Statement About "Illegality" Is "Untethered" to Anything and Is Therefore Not Probative

The prosecution also relies again on the testimony of June Weaver, and in particular, on her comment that Mr. Reyes told her that "it's not illegal if you don't get caught." (Weaver: 6/20/07 RT 567:1–4). Ms. Weaver, however, has no recollection of whether this comment was made in connection with the stock option granting process. In fact, she has no recollection of the context in which the statement was made at all. The Court put it best at the July 6 hearing, noting that Weaver's testimony "was pretty untethered and only slightly tethered to the witness's recollection" *and* that Weaver had "no recollection whatsoever, that the statement was tied to stock option compensation." (7/6/07 RT 2227:9–14). The law, however, does not permit a juror to convict based on speculation or conjecture. *United States v. D'Amato*, 39 F.3d 1249, 1256 (2d Cir. 1994). Indeed, courts have granted Rule 29 in the face of similar facially inculpatory statements, even when they are directly tied to the alleged crime. *See Cassese*, 428 F.3d at 101 (granting Rule 29 despite fact that defendant told banker two months after the purchase that he had "made a stupid mistake"). For this, and many other reasons, a rational juror could not rely on Ms. Weaver's testimony to find beyond a reasonable doubt that Mr. Reyes believed that the look-back pricing of stock options was wrongful.

8. The Prosecution's Argument That Reyes Had No Reason to Falsify The Grant Lists Except to Hide Expenses is Speculative

The prosecution finally asserts that the only reason that the grant minutes were backdated was to hide the look-backs from Brocade's finance department in order to avoid compensation expenses. First, there is absolutely no evidence in the record to support that proposition – zero. Second, the prosecution's argument directly contradicts the record, which plainly demonstrates that the HR Department's practice of "looking back" to select grant dates was visible to members of the finance department. Rather than conceal their look-backs, HR employees memorialized their pricing practices in writing. (*See, e.g.,* Ex. 944 (Colleen Devine's "New Pricing Memo"). Moreover, these documents were retained as part of Brocade's books and records and were openly stored on Brocade's computer system in a file folder "owned by finance or stock administration." (Weaver: 6/25/07 RT at 783:3–16; Kada: 6/25/07 RT at 847:10–16.)

HR employees also openly discussed their pricing practices with employees from the Finance Department on numerous occasions. For example, in April 2003, Ms. Weaver sought the advice of Brocade's controller, Bob Bossi, regarding whether to price new hire grants before or after the close of the quarter. (Ex. 167.) Copying Gary Blucher of the finance department and Brocade's General Counsel Ron Epstein in his response, Mr. Bossi replied: "New hire grants can happen whenever you want. Just bear in mind that after this week you can't go back and use a date pre 4/25." (Ex. 168.)

Similarly, in February 2002, prosecution witness Stephen Beyer notified Blucher and Bossi in an e-mail that he had just obtained final signature approval for stock grants dated October 30, 2001 — more than three months earlier.[12] (Exs. 134 & 135; Beyer: 6/19/07 RT at 299:12–302:16.) Thus, contrary to the government's assertion, the grant minutes at issue cannot be "consistent only with an intentional and systematic effort to mislead those who rely on them" because there was an intentional and systematic effort to ***disclose*** to Brocade's finance department the true pricing practices that the HR employees used to price grants.

C. Courts Have Granted Rule 29 Motions in Cases Where The Prosecution's Evidence is Far Stronger Than It Is Here

Courts have granted Rule 29 motions in cases where the prosecution presents far more evidence of guilt than the government has tried to present here. In *United States v. Cassese*, 290 F. Supp. 2d 443 (S.D.N.Y. 2003), the district court granted a Rule 29 motion. The defendant, the chairman and president of a computer company, was prosecuted under Section 14(e) of the Exchange Act, for purchasing stock based on inside information of an impending tender offer. There was nothing illegal about buying the stock unless the defendant *knew* the company was about to go through a tender offer. Absent evidence that the defendant had that knowledge when he bought the company's shares, there would be no crime, because there would be no *mens rea*. In other words, without knowledge that there

[12] Significantly, the prosecution cited this e-mail in their own brief (Resp. at 9), but conveniently neglected to mention that it was sent to two of the senior employees in the Finance Department.

would be a tender offer, the defendant could not have acted willfully and with a realization of wrongful conduct. *Cassese*, 290 F. Supp. 2d at 450.[13]

In response to the Rule 29 motion, the prosecution presented circumstantial evidence in an effort to create an aggregate impression that the defendant knew about the tender offer. The government argued that it was suspicious that the defendant used two brokerage accounts to buy the shares, instead of one; that the timing of the purchase was suspicious — one day after the defendant spoke to the CEO of the company that would make the tender offer; that the defendant's desire to cancel the trades soon after they were made showed a consciousness of guilt; and that over two months after the trades, Cassese told a banker who worked on the tender offer, in words or substance, that he had made "'a stupid mistake.'" *Cassese*, 290 F. Supp. 2d at 453–54. Additionally, the government introduced a Letter of Intent and a Proposed Confidentiality Agreement; the former alerted Cassese that any acquisition would likely be by tender offer (*id.* at 445) and the latter specifically warned him that trading on information received pursuant to merger negotiations might violate the federal securities laws. *United States v. Cassese*, 428 F.3d 92, 99 (2d Cir. 2005). Finally, the government argued that the defendant's experience as a CEO created a presumption that he understood securities laws. The evidence established that Cassese was familiar with certain aspects of securities laws, but there was no evidence that he had exposure to the tender offer rules. *Cassese*, 290 F. Supp. 2d at 456.

Considered in its totality, and viewed in the light most favorable to the prosecution, the district court determined that the evidence gave "'equal or nearly equal circumstantial support to a theory of guilt or a theory of innocence'" and that therefore, "'a reasonable jury must necessarily entertain a reasonable doubt.'" *Cassese*, 290 F. Supp. 2d at 456 (citations omitted). The district court's decision was upheld by the Second Circuit, which characterized the government's evidence as "modest evidentiary showings, equivocal or attenuated evidence of guilt, or a combination of the three." *Cassese* 428 F.3d at 103.

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[13] Similarly here, absent knowledge that the financial statements and books and records were inaccurate because of improper stock option accounting, Mr. Reyes's conduct is simply not criminal, even if he did know about the backdating. Without knowledge of the inaccurate accounting, he could not have possibly acted willfully and with a realization of wrongful conduct.

The same can be said for the prosecution's evidence here. It is equivocal and attenuated. It fails to show that Mr. Reyes understood the relevant accounting opinions; understood that Brocade should have taken compensation expenses; or knew that Brocade's financial statements, 10-Ks, and management representation letters were inaccurate in any way. In short, the evidence marshaled by the prosecution here is significantly weaker than the evidence introduced in *Cassese*, and the outcome should be the same. Only, the court should grant Rule 29 before this case ever goes to a jury.

D. The Court Should Grant Mr. Reyes's Motion for Judgment of Acquittal Because the Prosecution Has Not Met Its Burden, No Rational Juror Could Find Guilt Beyond a Reasonable Doubt on this Record, and There is a Danger That Anti-CEO Bias Could Unfairly Influence the Verdict if This Case Is Allowed to Go To the Jury

After 14 prosecution witnesses and approximately 2 weeks of testimony, the prosecution has, for purposes of Rule 29, elicited evidence that Brocade used short look-backs to price certain stock options, and that the option paperwork was signed by Mr. Reyes. None of that was disputed by the defense in the opening statement or in the cross-examination of the witnesses. But that is not sufficient to convict Mr. Reyes of securities fraud or any of the other criminal charges alleged here — the prosecution needs much, much more. And the prosecution has not proven it.

The Court has asked the parties to focus this briefing on the following questions: (1) What is the evidence that Mr. Reyes understood the accounting principles underlying APB 25? (2) What is the evidence that Mr. Reyes realized that Brocade's stock option practices required accounting charges under APB 25? and (3) What is the evidence that Mr. Reyes was aware that the company did not properly account for or disclose those compensation charges in its 2001 and 2002 financial statements and public disclosures? In response to those questions, the prosecution has identified a few crumbs of information. None of those crumbs drive any of the Court's questions even close to the ground, however. All of those crumbs, considered collectively, require the jury to use speculation and conjecture to bridge the gap between innocence and guilt.

The speculation and conjecture will not, however, be supported by tangible evidence or even fair inference. Rather, we fear it will be fueled by the anti-corporate officer sentiment expressed openly and repeatedly during jury selection, and it will be inflamed by the prosecutors' repeated

reference to the wealth of the defendant and certain defense witnesses, and references to concepts such as the "buck stops here" and the fiduciary responsibilities of a CEO.

The prosecutors know full well what they are doing. They know full well the potential prejudicial impact of their comments to the jury. They do not need to prove up an accounting and disclosure fraud the old fashioned way, by proving that someone told Mr. Reyes about the accounting and disclosure deficiencies and, with an intent to deceive and cheat shareholders and investors, Mr. Reyes ignored that information. They have the crumbs, they have the anti-corporate officer sentiment and they know that the speculation and conjecture of the jury will be sure to follow. That is precisely where we are in this case.

Rule 29 was enacted to dispose of cases just like this. Your Honor's role in the justice system is no more critical than at this moment. This is the moment when the government is seeking to deprive Mr. Reyes of his liberty, not based on admissible evidence demonstrating his guilt beyond a reasonable doubt, but on the misconceptions and biases held by some. There is no evidence upon which a rational juror could determine beyond a reasonable doubt that: (1) Mr. Reyes understood the accounting principles underlying APB 25; (2) Mr. Reyes realized that the stock option granting practices at Brocade required an accounting charge under APB 25; and (3) Mr. Reyes was aware that the company's financial statements and disclosures did not include those compensation charges. Accordingly, we respectfully ask the Court to grant Mr. Reyes's motion for judgment of acquittal.

III. CONCLUSION

For all of the reasons set forth above, and in Mr. Reyes's initial motion, Mr. Reyes respectfully requests that the Court grant this motion and enter a judgment of acquittal on Counts 1, 2, and 5 through 12 of the Indictment.

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