EFiled: Feb 18 2025 12:03PM EST
Filing ID 75660306
Case Number 446,2024

IN THE SUPREME COURT OF THE STATE OF DELAWARE

RHONDA SCHERTZ, Derivatively on behalf of CARVANA CO. Plaintiff-Below/Appellant, v. ERNEST GARCIA II, Defendant-Below/Appellee, -and- CARVANA CO., a Delaware corporation, Nominal Defendant-Below/Appellee.	No. 446, 2024 On appeal from the Court of Chancery of the State of Delaware, C.A. No. 2023-0600-KSJM **PUBLIC VERSION FILED: FEBRUARY 18, 2025**

APPELLANT'S REPLY BRIEF

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Dated: February 7, 2025

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Other Authorities

Rules

PRELIMINARY STATEMENT

Appellees misapply the law, overlook key facts, and rely on defendant-friendly inferences, which are improper on a motion to dismiss. Plaintiff appeals dismissal of her *Brophy* claim against Garcia Senior under Rule 12(b)(6).[1] Demand futility is not at issue, so the Complaint is evaluated under a notice-pleading standard, not a rigorous particularity standard.

Appellees do not engage with Plaintiff's arguments for why the true state and extent of Carvana's T&R challenges constitute MNPI. Nor could they, as less than one week after Appellant's Opening Brief was filed, the U.S. District Court for the District of Arizona (the "**Federal Court**") held—based on identical facts—that Carvana's public statements concerning its T&R challenges had been materially false and misleading.

Plaintiff has alleged more than enough to support a reasonable inference that Garcia Senior had knowledge of this MNPI and was at least partially motivated to sell over $3.6 billion worth of Carvana stock before it collapsed when the market learned the truth.

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[1] Unless defined herein, capitalized terms have the same meaning as in Appellant's Opening Brief ("**OB**"). The Answering Brief of Defendant-Appellee Ernest Garcia II and Nominal Defendant-Appellee Carvana Co. is referred to as "**AB**."

The Court of Chancery's decision should be reversed, and this case remanded for further proceedings.

DEVELOPMENTS FOLLOWING APPELLANT'S OPENING BRIEF

Two relevant developments have occurred since Plaintiff filed her opening brief. ***First***, the Federal Court substantially denied defendants' motion to dismiss the federal securities fraud action against Carvana and certain officers and directors. *United Ass'n Nat'l Pension Fund v. Carvana Co.* (*In re Carvana Co. Sec. Litig.*), 2024 WL 5153343 (D. Ariz. Dec. 16, 2024). Defendants' subsequent motion for reconsideration was rejected in a strongly worded opinion. *In re Carvana Co. Sec. Litig.*, 2025 WL 371717, at *2 (D. Ariz. Feb. 3, 2025) (noting the "Court already considered and rejected the very arguments Defendants regurgitate here"). ***Second,*** Carvana settled the State of Connecticut's claims that Carvana engaged in willful deception relating to its failure to comply with Connecticut T&R laws. (AR0001-27). The Court may take judicial notice of the foregoing under D.R.E. 201(d) and 202(a)(1).

The Federal Securities Fraud Decision

The Federal Court largely denied defendants' motion to dismiss the federal securities fraud action on December 16, 2024, six days after Appellant filed her Opening Brief.

The Federal Court held that eight statements (seven of which are also at issue here) concerning Carvana's compliance with state T&R laws were materially false and misleading. The statements fall into three categories:

1. Carvana made repeated statements between February 25, 2021, and May 10, 2022, that "we are subject to a wide range of evolving federal, state, and local laws and regulations" and that "failure to comply" or "even an allegation that we violated these laws… could result" in penalties. These were materially false and misleading because "Carvana's risk disclosures framed the violation of title and registration laws and regulations as a mere 'possibility,' when, unbeknown to investors, these violations and resulting penalties were 'existing issues[]'" that had already manifested. *See* A0144-47, ¶¶202, 204, 206; OB at 18-20, 27-30; 2024 WL 5153343, at *7. The Federal Court rejected defendants' assertions that these were forward-looking statements, opinions, and tempered by cautionary language. 2024 WL 5153343, at *9-10.

2. Carvana executives stated at the J.P. Morgan Auto Conference in August 2021 that North Carolina's suspension of Carvana's dealer license for its Raleigh facility was "unusual," "unprecedented," and "North Carolina specific[.]" These were materially false and misleading because, unbeknownst to the public,

Michigan had already fined and suspended Carvana for 18 months, and Ohio had already investigated Carvana, suspended it from issuing temporary tags, and placed it under increased oversight. The Federal Court held that a "reasonable investor [could] interpret" management's statements as "suggesting the North Carolina suspension was an anomaly." *See* A0101-02, A0148-49, ¶¶135, 207-08; 2024 WL 5153343, at *10; OB at 18-20, 28.

3. In response to the *Undriveable Cars* exposé published by *Barron's*, Carvana stated in June 2022 that its problems with T&R compliance were limited to "a very small percentage of instances" and that "[w]e've had productive conversations with regulators in all of those states and feel very confident about our operations going forward[.]" These were false and misleading because Carvana thereafter continued to violate the terms of its Michigan probation 127 times and had its license suspended for "[c]omitting fraud[]," "destroying title applications," and "[i]mproperly issuing temporary registrations." The Federal Court rejected defendants' assertion that the statements were puffery because the pleadings were "replete with allegations that Carvana systemically violated title and registration regulations, which resulted in customer delays and regulatory actions against Carvana," and a reasonable investor may conclude from the statements that

"Carvana's days of regulatory scrutiny were in the past." *See* A0095, A0154-55, ¶¶121, 216-17; OB at 27-28; 2024 WL 5153343, at *11.

As to Garcia Senior, the Federal Court sustained the Section 20(a) control person claims, and dismissed the Section 10(b) and Section 20A claims on the grounds that he did not personally make the false and misleading statements at issue and plaintiffs did not satisfy the heightened PSLRA pleading standard. 2024 WL 5153343, at *20, 22, 32-34. This is discussed in detail in Point D below.

The Connecticut Settlement

On January 14, 2025, it was announced that Carvana had settled an action by the State of Connecticut concerning Carvana's failure to timely comply with state T&R laws by paying a $500,000 penalty and establishing a $1 million consumer restitution fund. (AR0028-29). Announcing the settlement, the Connecticut Attorney General stated that Carvana:

> grew faster than it could manage, … made promises it simply could not keep, and its customers paid the price. We saw hundreds of complaints regarding long delays in title and registration [and other issues]. In addition to restitution and penalties, this settlement requires Carvana to come into compliance with all Connecticut laws. We're going to be watching closely to ensure they do right…going forward[.]

Id. The press release announcing the settlement continued:

> Connecticut launched its investigation into Carvana in January 2022, following hundreds of complaints to the Office of the Attorney General, Department of Consumer Protection and Better Business Bureau. Many consumer complaints related to extended delays between delivery of vehicles and receipt of Connecticut registration documents. Carvana represented that it handled the title and registration process, but in many cases the registration process took months to complete. Because of the registration delays, Carvana would sometimes provide consumers with a succession of out-of-state temporary registrations. In other instances, consumers were forced either to park their cars or risk driving unregistered vehicles.

Id. (providing excerpts from customer complaints). The Connecticut settlement shows that Carvana's inability to comply with state T&R laws was structural and belies Appellees' claim that "an issue within one state or locality does not necessarily mean Carvana would face similar issues in others[.]" AB 12.

ARGUMENT

PLAINTIFF STATES A *BROPHY* CLAIM AGAINST GARCIA SENIOR

A. Stating a *Brophy* Claim Under Rule 12(b)(6) is Not Onerous

Appellees incorrectly assert that Plaintiff was required to "allege facts ***showing***" that Garcia Senior knew Carvana's MNPI and was motivated to sell his stock because of the specific content of that information. AB 21-22. This exaggerates Plaintiff's burden. Defeating a Rule 12(b)(6) motion requires Plaintiff to allege facts ***supporting a reasonable inference*** of Garcia Senior's knowledge and scienter. *See* OB at 22-24.

Defendants' authority for the existence of a "very high" bar "for stating a [*Brophy*] claim" was not decided under the Delaware notice pleading standard that controls this appeal. *See* AB 21, quoting in *In re Camping World Holdings, Inc. S'holder Deriv. Litig.*, 2022 WL 288152, at *9 (Del. Ch. Jan. 31, 2022). In *Camping World*, the issue was whether plaintiff adequately pled demand futility under Rule 23.1, which is evaluated under a stringent particularity standard. *Id.* at *6. Here, that is not the case; the Court of Chancery dismissed the Complaint under Rule 12(b)(6) and demand futility is not at issue in this appeal.

Similarly, *In re Oracle Corp. Deriv. Litig*., 867 A.2d 904, *aff'd,* 872 A.2d 960 (Del. 2005), was decided on *summary judgment* based on a "massive record" that was "close to an all-evidence dump of discovery." 867 A.2d at 906, 908. Motions for summary judgment address the merits under a standard more stringent than pre-discovery motions to dismiss. *See also Kahn v. Kolberg Kravis Roberts & Co., L.P.*, 23 A.3d 831, 838 (Del. 2011) ("***KKR***") (noting that, in *Oracle*, the Court affirmed "the elements essential for a plaintiff to prevail"—on the merits—"on a *Brophy* claim.").

This appeal addresses the sufficiency of the pleadings when demand futility is not at issue. As in *Pfeiffer v. Toll,* "[t]he Complaint is not subject to any heightened pleading standard…. [a]lthough a plaintiff must plead with particularity when attempting to establish demand futility [*e.g.,* as in *Camping World*], that is not the issue here." 989 A.2d 683, 692-693 (Del. Ch. 2010), *abrog. in part on other grounds* in *KKR*, 23 A.3d 831.

Plaintiff's allegations are thus evaluated here "under the plaintiff-friendly Rule 12(b)(6) standard, [and] not a particularity standard." *Pfeiffer*, 989 A.2d at 692, citing *In re Am. Int'l Group, Inc*., 965 A.2d 763, 800-01, 811 (Del. Ch. Feb. 10, 2009) (evaluating pleadings under a Rule 12(b)(6) standard when Rule 23.1 is not at issue).

Appellees' effort to impose burdensome pleading requirements fails. In dismissing this claim, the Court of Chancery misapprehended the facts, which colored the resulting inferences. OB 29-31. Applying the proper standard to the facts alleged, the Court of Chancery's dismissal of Plaintiff's *Brophy* claim against Garcia Senior should be reversed.

B. Appellees Concede that Garcia Senior is Carvana's Fiduciary

Appellees acknowledge that Garcia Senior owes fiduciary duties to the Company and its stockholders because he owns a "majority ownership interest in Carvana's voting stock". AB 21. They do not dispute that Garcia Senior controls Carvana. *See* OB 25; AB 1 (referring to Garcia Senior as "the controlling stockholder of Carvana").

Nor could they, as Carvana's SEC filings emphasize that "the Garcia Parties"—Garcia Senior, Garcia Junior, and their affiliated companies— "have the ability to … control our policies and operations" through their supermajority voting power under the Company's two-tier capital structure. (A0057, A0063, ¶¶47, 59). *See also In re Carvana Co. Sec. Litig.*, 2024 WL 5153343, at *33 (sustaining Section 20(a) controller liability claim against Garcia Senior based on four of the same

statements alleged here, and noting that "in every form where the 'Garcia Parties' are identified, Garcia Senior is included.").

As noted by the Federal Court, Carvana's SEC filings "suffice to allege that Garcia Senior was more than just a majority shareholder—he exercised 'actual control' over Carvana, its officers, and directors[,]" and that "[c]ourts have upheld Section 20(a) claims against shareholders under circumstances far less indicative of control." *Id.*

C. Carvana's Systemic Failure to Follow State T&R Laws was MNPI

Appellant's Opening Brief shows how the Court of Chancery misapprehended the facts and timeline in ruling that Carvana's T&R compliance challenges did not constitute MNPI because Carvana promptly and fully disclosed them to the market. *See* OB 27-32. Six days after Plaintiff filed her Opening Brief, the Federal Court held that Carvana's statements concerning its T&R difficulties were materially false and misleading for the same reasons argued by Plaintiff here and below. *In re Carvana Co. Sec. Litig.*, 2024 WL 5153343, at *19. *See* "Developments Following Appellant's Opening Brief" above.

Specifically, Carvana's disclosures falsely characterized the risks of failing to comply with state T&R laws as purely hypothetical when they had already come to

pass. OB 28; 2024 WL 5153343, at *7. Management falsely characterized North Carolina's suspension of Carvana's dealer license as an anomaly even though Carvana had already been sanctioned by Michigan and Ohio. OB 18-20; 2024 WL 5153343, at *10. Carvana falsely asserted that its T&R compliance problems were miniscule, that it had "productive conversations with regulators," and that it was confident in compliance going forward, when its problems were only beginning to come to light. *See* 2024 WL 5153343, at *11. Rather than address Plaintiff's factual arguments and the Federal Court's correct decision that Carvana's public statements were materially false and misleading based on the same facts, Appellees only repeat the Court of Chancery's mistaken conclusion to the contrary. AB 2, 10, 19, 22.

Appellees' assertion that Plaintiff is "retrospectively rewriting" Carvana's internal documents to create MNPI is divorced from reality. AB 30. The Federal Court validated Plaintiff's interpretation of Carvana's books and records, namely that they reflect a Company-wide failure of a critical corporate function that Carvana concealed from the public. Since Carvana's statements concerning T&R compliance were demonstrably both false and misleading, it follows that internal knowledge about the *true* state of the Company's T&R failures was MNPI because the public had not been told those facts. (A0144, A0155, ¶¶202, 218).

Accepting Appellees' argument to the contrary requires the Court to draw inferences in their favor. Apart from being impermissible when resolving the pleadings, it is unreasonable given the Federal Court's ruling—based on the same facts alleged here—that Carvana's statements concerning T&R compliance were misleading under the heightened standard for pleading securities fraud. *VLIW Tech., LLC v. Hewlett-Packard Co*., 840 A.2d 606 (Del. 2003) ("On appeal [from dismissal of a complaint for failure to state a claim], facts alleged in the complaint must be taken as true and all inferences therefrom are viewed in a light most favorable to the plaintiff" under Rule 12(b)(6)).

Plaintiff alleged more than enough to support the inference that Carvana's T&R failures were material, widespread, growing, and withheld from the public. Internal documents and testimony from confidential witnesses establish that Carvana's management had detailed, contemporaneous knowledge of the company's widespread T&R failures, yet chose not to disclose the full extent of these issues to investors. (A0089, A0138, A0141, A0144, A0146-47, A0153, A0162-63, ¶¶107, 191, 195, 202, 205, 207, 214, 232).

Appellees rely on the Court of Chancery's mistaken conclusion that Carvana repeatedly disclosed T&R issues to investors "throughout the relevant period." AB

28, Ruling 31. Their reliance is misplaced because the Chancery Court erred in reaching that conclusion. As discussed above, in Appellant's Opening Brief, and by the Federal Court, there is an irreconcilable difference between framing things as hypothetical concerns or long-gone—as Carvana did—when, in reality, they are pervasive, widespread, ongoing, and growing actual problems. During the time period at issue, the concerns were neither hypothetical nor long-gone. They were real and Carvana did not disclose them to investors.

In sum, Appellees try to wrongly equate vague, boilerplate risk disclosures that have been found to be false and misleading with actual, undisclosed knowledge of Carvana's systemic noncompliance with state T&R laws. The reality was far worse than investors were led to believe—which is why the stock price fell after the truth came out. Accordingly, the Court of Chancery erred in ruling that the state and extent of Carvana's T&R failures was not MNPI.

D. It is Reasonable to Infer Garcia Senior's Knowledge of this MNPI

There is no requirement to plead knowledge with particularity. "Under Rule 9(b), a plaintiff can plead knowledge generally." *Elec. Last Mile Solutions, Inc. S'holder Litig.*, 2024 WL 223195, at *3 (Del. Ch. Jan. 22, 2024). "Accordingly, 'for purposes of a motion to dismiss under Rule 12(b)(6), a complaint need only plead

facts supporting a reasonable inference of knowledge.'" *Id.*; *Wells Fargo & Co. v. First Interstate Bancorp*, 1996 WL 32169, at *11 (Del. Ch. Jan 18. 1996) (for "pleading knowledge, Rule 12(b)(6) and 9(b) are very sympathetic to plaintiffs."). Courts recognize that *Brophy* claims must "by necessity" be pled "on circumstantial facts[.]" *In re TrueCar, Inc. S'holder Deriv. Litig.*, 2020 WL 5816761, at *24 (Del. Ch. Sept. 30, 2020). Facts are circumstantial when they may reasonably be inferred from the existence of other facts. *See, e.g., Lemons v. State*, 32 A.3d 358, 362 n.9 (Del. 2011), citing 29 Am.Jur.2d Evidence § 1361 [now § 1314].

The Wall Street Journal describes Carvana as the Garcias' "family business." (A0052-54, A0058, A0062-63, ¶¶39, 41, 48, 56, 58) (Wharton professor observes that Carvana's ownership structure allows the Garcia family to "run this $60 billion public company as if it's a family firm and for the family's benefit…"). The Court of Chancery previously found that Garcia Senior and his son "collectively control Carvana[.]" *In re Carvana Co. Stockholders Litig.*, 2022 WL 2352457, at *1 (Del. Ch. June 30, 2022). As discussed in Section B above, the Federal Court affirmed Garcia Senior's control over Carvana for purposes of liability under Section 20(a), underscoring how his influence extends far beyond simple majority stockholder status.

These are the facts: Garcia Senior is the Company's founder and personally controls 84% of the Company's stock. (A0056, ¶45). At least half the Board, which he installed, is beholden to him. (A0195-211, ¶¶291-316).[2] He appointed his son, who lives next door to him, as the Company's President. (A0045, A0054, ¶¶19, 43). Carvana acknowledges that Garcia Senior and his son control the Company. *See* Point B above. Carvana relies heavily on the Garcia family's privately held companies—co-owned by Garcia Senior and his son and described by a law professor as "a convoluted tangle of interrelated companies and related party transactions [that are] very difficult to understand or pull apart"—for inventory, financing, operations, real estate, and collections. (A0048, A0054, A0058-62, ¶¶42, 48, 49, 50-56). It would be difficult to find a major area of Carvana's business that is not connected with the Garcias' private companies.

Indeed, commissions from peddling extended warranties issued by another one of the Garcia family companies account for 12% of Carvana's profits. (A0059-60, ¶50). Every year, Garcia Senior benefits from hundreds of millions of dollars in

[2] *See also In re Carvana Co. S'holders Litig.,* 2022 WL 2352457, at *13-14 (finding that Defendants Below, directors Platt and Sullivan, lack independence from Garcia Senior based on the same facts alleged here).

related party transactions between his companies and Carvana, which Carvana acknowledges are "not negotiated at arm's length." (A0057, A0062, ¶¶47, 56-57). *The Wall Street Journal* reports that Garcia Senior and his son "coordinated" a private offering to increase their stake in the Company at below-market prices. (A0157-58, ¶223). The Court of Chancery found that Garcia Senior "participated behind the scenes in the planning and execution" of another private offering where they further increased their stake in the Company (*Id.*; A0063-64, ¶60, quoting *In re Carvana Co. S'holders Litig.,* 2022 WL 2352457, at *4). Finally, the Court of Chancery found that Garcia Senior and his son communicate about the Company and its business. *Id.*; *see also In re Carvana Co. Sec. Litig.*, 2024 WL 5153343, at *28 (noting the Garcias "employed a hands-on management style," and "'it would be absurd to suggest' that Garcia Junior… did not know of Carvana's title and registration issues[.]"). It is thus entirely reasonable to infer that Garcia Senior was routinely kept informed about Carvana's persistent difficulty in executing its central compliance function, which bears on the Company's core operations.

Appellees incorrectly suggest that drawing this inference runs counter to Delaware's presumption that directors act in good faith. AB 25. Not so; the breach of fiduciary duty is Garcia Senior acting on MNPI. It is perfectly natural for father

and son to talk about a company they control, particularly given the unusually close relationship and extensive business ties between Garcia Senior and his son. *See generally*, J. Travis Laster and J.M. Zeberkiewicz, *The Rights and Duties of Blockholder Directors*, 70 Bus. Law 33, 55 (2015) (acknowledging the "practical reality" that directors appointed by large blockholders routinely report to their principals). The issue is not the communications themselves, but Garcia Senior's subsequent trading on the basis of the MNPI shared during those communications.

The depth and breadth of facts supporting the inference of Garcia Senior's knowledge contrasts starkly to the unsupported and wholly conclusory allegations in Appellees' authority. In *Tilden v. Cunningham*, 2018 WL 5307706, *19 & n.200 (Del. Ch. Oct. 26, 2018), the court declined to infer that defendants "must have obtained some additional material, non-public information" when the allegations were "wholly conclusory" and the specific MNPI was not alleged. But that is not the case here. *See* Point C above. Similarly bare allegations were made in *Pfeffer v. Redstone*, where plaintiff pled no facts supporting an inference of knowledge beyond "conclusorily asserting that [defendants] would (or must) have been told[.]" 965 A.2d 676, 687 (Del. Ch. Jan. 23, 2009). Likewise in *In re Vaxart Stockholder Litig.,* where plaintiff alleged that defendants "must have been told" with no factual basis

beyond defendants' positions. 2022 WL 1837452, at *19 n.183 (Del. Ch. June 3, 2022). In contrast to those cases, Garcia Senior and his private companies were thoroughly involved in Carvana's business.

Similarly, plaintiffs in *Camping World* "ask[ed] the court to assume that the information provided to the directors must have been materially adverse." 2022 WL 288152, at *11. Here, that is not the case. *See* Point C. *Camping World* is further distinguishable as it was decided under the rigorous particularity pleading standard because plaintiffs alleged that a majority of directors faced a substantial likelihood of liability, thus excusing demand. *Id.* at *7. Such was also the case in *Zimmer Biomet Hldgs, Inc. Deriv. Litig.*, where the court declined to credit "entirely conclusory" allegations under the rigorous particularly pleading standard. 2021 WL 3779155, at *20 (Del. Ch. Aug. 25, 2021).

Appellees point to the fact that plaintiffs in the federal securities action did not succeed in pleading a claim against Garcia Senior for insider trading. *See* AB 24-25, citing *In re Carvana Co. Sec. Litig.*, 2024 WL 5153343. That has zero bearing on whether Plaintiff adequately pled facts from which the Court may infer Garcia Senior's knowledge here. First, in the federal securities action it was "unclear on the face of the [complaint] whether [the plaintiffs] independently assert[ed] an insider

trading claim against Garcia Senior under Section 10(b), despite [their] statements to the contrary" relegated to a single footnote. *Id.* at *20. Here, Plaintiff indisputably brings a *Brophy* claim against Garcia Senior in Count IV of the Complaint. (A0217, ¶¶340-43).

Next, the federal plaintiffs failed to plead that Garcia Senior himself made any false and misleading statements or personally committed a deceptive or manipulative act sufficient for liability under Section 10(b). *In re Carvana Co. Sec. Litig.*, 2024 WL 5153343, at *5, *20-21. Delaware law, however, does not require a predicate violation of federal securities laws to plead a *Brophy* claim. It only requires a fiduciary to knowingly trade on MNPI. *See, e.g.*, *Guttman v. Huang*, 823 A.2d 492, 505 (Del. Ch. 2003).

Finally, pleading knowledge for purposes of an insider trading claim under Section 10(b) and the PSLRA in the Ninth Circuit requires alleging with particularity "what information [defendant] obtained, when and from whom he obtained it, and how he used it for his own advantage." *Id.* at *21 (citing authority). Section 10(b) treats insider trading as a species of fraud, which must be pled with particularity under Rule 9(b) of the Federal Rules of Civil Procedure. *Id*. at *35. "The only conceivable allegation that Garcia Senior possessed MNPI" in the federal securities

case "is in a passing footnote[.]" *Id.* at *21 n.13. Given the paucity of allegations, the Federal Court observed that "[t]o the extent [the federal plaintiffs] allege Garcia Senior possessed MNPI based solely on his status as a controlling shareholder and the CEO's father," that is insufficient to satisfy the exceedingly high standard for pleading fraud under Rule 9(b) and the PSLRA. *Id.* at *21.

The Court of Chancery held Plaintiffs to a similarly high standard in noting that Garcia Senior's knowledge is "unexplained." Ruling at 27. Perhaps that might be required under a rigorous particularity standard. *See Rattner v. Bizdos*, 2003 WL 22284323, at *5, 10 (Del. Ch. Sept. 30, 2003) (particularized pleading of someone's knowledge "by virtue of their positions" requires alleging "the precise roles that [the person] played at the Company and the information that would have come to their attention in those roles"). That, however, is not the case under Rule 12(b)(6) for a *Brophy* claim under our law.

As discussed in Point A above, the applicable standard here is far more lenient. Plaintiff need only plead sufficient facts for the Court to infer Garcia's knowledge and scienter. She has done so. Even if the Court believes that Garcia Senior likely lacked knowledge of MNPI, the Court must resolve all inferences in Plaintiff's favor. *See Inter-Mktg. Grp. USA, Inc. v Armstrong*, 2020 WL 756965, at *14 (Del. Ch. Jan.

31, 2020) (crediting plaintiff-friendly inference even where defendants' characterization of the facts was "perhaps even the most reasonable"); *La. Mun. Police Emps. Rey. Sys. v. Pyott,* 46 A.3d 313, 358 (Del. Ch. 2012), *rev'd on other grounds,* 74 A.3d 612 (Del. 2013) ("It may be that the directors in fact acted in good faith… but at the pleadings stage I do not believe that I can adopt a defendant-friendly interpretation of the plaintiffs' allegations."). Therefore, the Court of Chancery's dismissal, premised on a more demanding standard, must be reversed.

E. It is Reasonable to Infer Garcia Senior's Scienter

Plaintiff is "not required to uncover and plead the 'smoking scienter gun' in order to state a *Brophy* claim." *In re FitBit, Inc. S'holder Deriv. Litig.*, 2018 WL 6587159, at *15 (Del. Ch. Dec. 14, 2018). Plaintiff need only "plead[] facts that support a rational inference of bad faith[.]" *Kahn v. Stern*, 183 A.3d 715 (Del. 2018). Because demand futility is not at issue on this appeal, Plaintiff need not plead scienter with particularity. *See* Point A above.

Appellees principally argue that Garcia Senior's scienter should not be inferred because he sold his stock (except for $478 million worth on December 2, 2020) pursuant to Rule 10b5-1 trading plans ("**Trading Plans**"). AB 3, 31-36. Their arguments fail from the start because the Trading Plans were not included in the

books and records produced to Plaintiff; their terms were not relied upon in the Complaint and therefore not incorporated by reference; they were not provided to the Court of Chancery on Defendants' motion to dismiss; and they were not included in the Appendices submitted to this Court. Appellees must live with the consequences of their decision not to provide the Trading Plans earlier in this litigation.

Defendants therefore cannot use Garcia Senior's Trading Plans to mitigate an inference of scienter. *In re Upstart Holdings, Inc.*, *Sec. Litig.*, 2023 WL 6379810, at *21 (S.D. Ohio, Sept. 29, 2023) (doing so "would be hasty at this juncture… where this Court has not been presented with the [plan] and has not had an opportunity to review [its] contents."); *Sinnathurai v. Novavax*, *Inc.*, 645 F. Supp.3d 495, 529 (D. Md. 2022) (a 10b5-1 plan does not negate the inference of scienter where the terms of the plan are outside the record); *Azar v. Yelp, Inc.*, 2018 WL 6182756, at *19 (N.D. Cal. Nov. 27, 2018) ("Without reviewing [the] actual trading plan, the Court… cannot conclude that the plan negates any inference of scienter.").

Moreover, a trading plan affords a defense only if it was entered into in good faith. 17 C.F.R. § 240.10b5–l(c)(l)(ii). "Not only can this Court not make such factual findings when considering a motion to dismiss, but this Court must also draw

all inferences in favor of the non-moving party." *In re Able Labs. Sec. Litig.*, 2008 WL 1967509, at *27 n.40 (D.N.J. Mar. 24, 2008). The same applies here. *Cf. Indiana Pub. Ret. Sys. v. Pluralsight, Inc.*, 45 F.4th 1236, 1266 (10th Cir. 2022) ("the text and history of Rule 10b5–1 shows that such plans can be manipulated easily for personal financial gain[.]").

Appellees assert that Garcia Senior's original Trading Plan was entered into on June 15, 2020, and he began trading on October 30, 2020. *See* AB at 33. Appellees' claim that this delay mitigates scienter has no factual basis. What are the circumstances under which the Trading Plan was adopted? Does the Trading Plan allow Garcia Senior discretion about when trading would start? Does it comply with Carvana's insider trading policy? We don't know because the Trading Plan wasn't disclosed. Between when Garcia Senior entered his initial Trading Plan and when he started trading, the Board was told at two separate meetings that "Registration Delays" are a "key driver[]" of growing customer dissatisfaction. (A0129-30, A0134, ¶¶177, 184). At the pleading stage, the Court cannot infer from the bare record that Garcia Senior's Trading Plan negates the inference of scienter.

Moreover, just four days after starting to sell under his initial Trading Plan, on November 4, 2020, Garcia Senior amended it to *increase* the number of shares he

could sell daily from 30,000 to 50,000. (A0158, A0160, ¶¶224, 227). Between December 2020 and May 17, 2022, Ohio suspended Carvana from issuing temporary tags and placed the Company under increased monitoring; the Board was told that "Registration Delays" continued to drive poor customer satisfaction; Michigan began to investigate the Company then fined and put it on probation for 18 months; and the Company made materially false and misleading statements in its Form 10-K. (A0094, A0108-09, A0127, A0129-32, A0152-53, ¶¶120, 144, 174, 177, 180, 213). On May 20, 2021, Garcia Senior modified his Trading Plan *again* to increase his daily sales limit to 60,000 shares. (A0158, A0160, ¶¶224, 227; OB at 71-72).

The fact that Garcia Senior amended his Trading Plan—twice—as the Company's stock climbed to record heights while problems increasingly mounted behind the scenes supports the inference of scienter. (A0160, ¶227; A0711; A0785-86), *In re Countrywide Fin. Corp. Deriv. Litig.*, 554 F. Supp.2d 1044, 1069 (C.D. Cal. 2008) (amending Trading Plans "at the height of the market" is probative of scienter); *Empls. Ret. Sys. of the Gov. of the Virgin Islands v. Blanford*, 794 F.3d 297, 309 (2d Cir. 2015) (trading plans provide no defense when their purpose is to take advantage of an inflated stock price).

Indeed, Garcia Senior would have realized how important complying with state T&R laws was to Carvana's business, and the damage that would follow when this was inevitably disclosed. *See Freudenberg v. E*Trade Fin. Corp.*, 712 F. Supp. 2d 171, 200 (S.D.N.Y. 2010) ("a clever insider might 'maximize' their gain from knowledge of an impending price drop over an extended amount of time, and seek to disguise their conduct with a 10b5-1 plan."). As noted by the head of the Wharton School of Business' Forensic Analytics Lab, "I've studied 20,000 10b5-1 plans. [] I can't recall another of this size where there are modifications every six months." (A0161, ¶228). At the pleading stage, Garcia Senior's highly suspicious modifications to his Trading Plans strongly support the inference of scienter, not to mention that Garcia Senior sold $478 million worth of stock *outside* his Trading Plan on December 2, 2020. (A0159, ¶226).

Appellees' grab bag of remaining arguments is easily dispensed with. The length of the trading window is a function of the length of time between when the Board first learned of Carvana's difficulties with T&R compliance and when this was finally disclosed to the public. The fact that it was kept secret for so long—through false and misleading statements, no less—is why Garcia Senior was able to make so many trades. The fact that Garcia Senior still retained a supermajority stake

in the Company is not as important as him selling a fraction of his stake for an astonishing $3.67 billion. *Nursing Home Pension Fund, Loc. 144 v. Oracle Corp.*, 380 F.3d 1226, 1232 (9th Cir. 2004) ("where, as here, stock sales result in a truly astronomical figure [there, $900 million], less weight should be given to the fact that they may represent a small portion of the defendant's holdings.").

Finally, Appellees stand mute in response to Plaintiff's well pleaded allegations that substantially all of Garcia Senior's sales took place *before* Carvana's systematic T&R compliance problems were publicly disclosed, AB 35-36; that Garcia Senior's most recent sale prior to his first sale under the Trading Plan was over 15 months earlier, *id.,* (A0158-159 ¶225); and that Garcia Senior bought 555,556 shares of Carvana stock at below-market prices before unloading them as the stock price reached record heights shortly thereafter, *id*.

The court considers all these factors in their totality. *See Fitbit*, 2018 WL 6587159, at *15 & n.179. Taken together and considered under the appropriate Rule 12(b)(6) notice pleading standard, they can only support the inference that Garcia Senior acted with scienter.

* * *

Brophy claims further "the public policy of preventing unjust enrichment based on the misuse of confidential corporate information." *KKR*, 23 A.3d 831, 840 (Del. 2011). The pleading standard under Rule 12(b)(6) is modest. Plaintiff has alleged more than enough to "support a reasonable inference of [Garcia Senior's] knowledge, and resulting scienter[.]" *Fitbit*, 2018 WL 6587159, at *15.

CONCLUSION

The Court of Chancery's ruling dismissing Plaintiff's *Brophy* claim against Garcia Senior should be reversed for the reasons above and in Appellant's Opening Brief.

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Dated: February 7, 2025
Public Version: February 18, 2025