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SUPERIOR COURT OF THE STATE OF CALIFORNIA

COUNTY OF SAN FRANCISCO

LENZA H. McELRATH III, individually, in his representative capacity, and on behalf of all others similarly situated, Plaintiffs, v. UBER TECHNOLOGIES, INC., a Delaware corporation, 1455 Market St., 4th Floor San Francisco, CA 94103, Defendant.	No. CGC-16-551748 **MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF UBER TECHNOLOGIES, INC.'S DEMURRER TO FIRST AMENDED COMPLAINT** **HEARING** **DATE:** SEPT. 27, 2016 **TIME:** 9:30 A.M. **DEPT.:** 302 **RESERVATION NUMBER: 08150927-15** **COMPLAINT FILED: MAY 2, 2016** **FAC FILED: JULY 13, 2016**

I. INTRODUCTION

Plaintiff's First Amended Complaint ("FAC") asserts just one cause of action: a violation of the California Private Attorneys General Act ("PAGA"). This sole cause of action is based on Defendant Uber Technologies, Inc.'s ("Uber") alleged violation of four separate California Labor Code sections. However, Plaintiff has not alleged facts that, if true, violate the California Labor Code. As such, he is not an "aggrieved employee" as required to bring a PAGA action, and thus his FAC fails to state a claim against Uber.

The gravamen of Plaintiff's FAC is that Uber promised him incentive stock options ("ISOs"), but then granted him nonqualified stock options ("NSOs"). Based on this alleged failed promise, he asserts that Uber violated California Labor Code Sections 201 (requiring immediate payment of wages upon discharge or layoff), 202 (requiring immediate payment of wages upon resignation), 204 (requiring semimonthly payments of wages) and 970 (prohibiting an employer from making false representations to induce employees to move to, from or within California to work for the employer).

The problem with Plaintiff's claim is that the facts alleged, even if true, do not violate the California Labor Code. Plaintiff cannot state a claim under Sections 201, 202 and 204 because Uber's alleged violations concern *stock options*, and California law is clear that stock options are not wages covered by California Labor Code Sections 201, 202 and 204.

Nor can Plaintiff state a claim under California Labor Code Section 970. The alleged promise of ISOs was expressly and undisputedly subject to approval by Uber's Board of Directors. As such, it was a conditional promise, subject to non-performance or different performance. Such a promise cannot, as a matter of law, form the basis of a misrepresentation claim.

For these reasons, Plaintiff cannot establish that Uber violated the Labor Code. Plaintiff is therefore not an aggrieved employee and cannot state a PAGA claim upon which relief may be granted. Accordingly, Uber respectfully requests that the Court sustain this demurrer and dismiss Plaintiff's FAC in its entirety, with prejudice.

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II. FACTUAL BACKGROUND AND PROCEDURAL HISTORY

A. Plaintiff's Employment Agreement Promised ISOs "to the Maximum Extent Allowed by the Tax Code," Subject to Board Approval.

Plaintiff is a regular, full-time Uber employee. (FAC ¶ 1.) He started his employment in September 2014. (*Id.*)

Plaintiff's Employment Agreement with Uber stated that "[s]ubject to the approval of the Company's Board of Directors," he would receive "a stock option covering 20,000 shares" of Uber's common stock (the "Option"). (Ex. 1, Employment Agreement ¶ 2(c).)[1] The Employment Agreement also prescribed that the Option would be "an *incentive stock option* to the *maximum extent allowed by the tax code.*" (*Id.* (emphases added).) In addition, the Employment Agreement advised Plaintiff "to consult with [his] own tax advisor concerning the tax risks associated with accepting an option to purchase the Company's Common Stock" and expressly stated that the Option would be "subject to the other terms and conditions set forth in the Company's 2013 Stock Plan ... and in the Company's standard form of Stock Option Agreement." (*Id.*) Plaintiff acknowledged and agreed to these terms and advisements by executing the Employment Agreement. (*Id.* at 6.)

B. Plaintiff's Stock Option Grant Awarded Plaintiff Exactly What Was Promised – ISOs to the Extent Permitted Under the Tax Code.

The Internal Revenue Code ("IRC") recognizes two types of employee stock options: ISOs and NSOs. *See Falkowski v. Imation Corp.*, 132 Cal. App. 4th 499, 515 n.16 (2005) (citations omitted). An ISO is not taxed upon either the grant or exercise of the option. *Id.* (citing 26 U.S.C. §§ 421(a)(1), 422(a)). However, the federal tax code does not permit employers to issue unlimited ISOs. Rather, the Internal Revenue Code imposes a $100,000 limit on the total aggregate fair value of ISOs that are exercisable by an employee within a calendar year. 26 U.S.C. § 422(d). Accordingly, to "the extent that the aggregate fair market value of stock with respect to which [ISOs] ... are exercisable for the 1st time by any individual during any calendar year ... exceeds $100,000, such options shall be treated as [NSOs]." *Id.* Put another way, under

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[1] All citations to "Ex.__" are to Exhibits attached to the Declaration of Wendy J. Brenner in Support of Uber's Demurrer to Plaintiff's FAC.

the $100,000 rule set by the Internal Revenue Code, if the value of option shares that are exercisable by an employee in any given year exceeds $100,000, the shares in excess of the $100,000 limit cannot legally be ISOs – those must be NSOs. Unlike ISOs, NSOs are taxed at the time of either grant or exercise, and are subject to capital gains tax upon the sale of the stock. *Falkowski*, 132 Cal. App. 4th at 515 n.16 (citing 26 U.S.C. § 83(a)).

Shortly after commencing employment with Uber, Plaintiff received a notice of stock option grant from Uber (the "Notice"), stating that his Option had been granted. (Ex. 2, Notice at 1.) The Notice, which Plaintiff signed on October 14, 2014, stated that the Option was "granted under and governed by the terms and conditions" of the Stock Plan and the Stock Option Agreement. (*Id.* at 1-2.)

Consistent with the Employment Agreement, the Stock Option Agreement provided Plaintiff with an Option to purchase 20,000 shares, designated as ISOs to the maximum extent permitted under the Internal Revenue Code. Specifically, Plaintiff's Stock Option Agreement provided that his Option would be "early exercisable" – that is, *all* of the shares subject to the Option (whether vested or not) could be exercised "in whole or in part" just six months after the date of the grant. (Ex. 2, Stock Option Agreement at ¶ 3; Notice at 1.) As a result, *all* of the shares were exercisable in a single year, and subject to the $100,000 limit imposed by the Internal Revenue Code. The aggregate value of such shares exceeded $100,000; as such, the $100,000 limit imposed by the Internal Revenue Code resulted in a portion of the shares being deemed ISOs (that portion with an aggregate value under $100,000) and the remaining shares deemed NSOs (that portion in excess of $100,000). The application and effect of the $100,000 limit was expressly explained in the Stock Option Agreement. (Ex. 2, Stock Option Agreement at ¶ 2.)

Notably, Plaintiff "acknowledge[d] receipt of a copy of the [Stock] Plan and represent[ed] that he ... is familiar with the terms and provisions thereof (and has had an opportunity to consult counsel regarding the Option terms)." (*Id.* at ¶ 8.) Plaintiff "accept[ed] [the] Option and agree[d] to be bound by its contractual terms as set forth [in the Stock Option Agreement] and in the [Stock] Plan." (*Id.*)

C.   **Plaintiff's PAGA Notice and FAC Allege That Uber Violated the Labor Code.**

In February 2016, Plaintiff sent a letter to the California Labor and Workforce Development Agency ("LWDA") (the "PAGA Notice") claiming that Uber violated the California Labor Code by issuing him an Option that was comprised of both ISOs and NSOs instead of the 20,000 ISOs that he alleges were promised in his Employment Agreement. (*See* Ex. 3, PAGA Notice at 4.) Plaintiff's PAGA Notice further alleged that Uber "convinced [Plaintiff] to accept employment and relocate by telling [him] he would receive ISOs, but the company never intended to provided (sic) the promised compensation." (*Id.* at 5.) While Plaintiff indeed recognized that his Employment Agreement granted him "an [ISO] to the maximum extent allowed by the tax code," Plaintiff claimed – without support – that "[t]he tax code allows the option (as promised) to be entirely an ISO." (*Id.*)

On this basis, Plaintiff maintains that Uber's alleged misconduct constituted a violation of Sections 201, 202, 204, and 970 of the Labor Code. (*Id.* at 6.) To support these allegations, Plaintiff stated in conclusory fashion that, Uber's "false representations are contained in [his] Employment Agreement" and concern: 1) the type of options that would be provided as compensation and 2) when those options would be exercisable. (*See id.*) Plaintiff went on to claim that "[b]y never providing the agreed compensation the company has failed to distribute [Plaintiff's] agreed wages in the time allowed by law, and has shown it will not provide [his] earned wages when [his] employment ends." (*Id.*)

On May 2, 2016, Plaintiff filed his initial Complaint, which alleged four causes of action based on the allegations set forth in the PAGA Notice: (1) breach of contract, (2) PAGA violation, (3) fraud by intentional or negligent misrepresentation, and (4) fraud by concealment. (Compl. ¶¶ 12-34.) On July 13, 2016, Plaintiff filed the FAC. In doing so, Plaintiff removed all causes of action, except the one alleging a PAGA violation. (*Compare* Compl. *with* FAC.) Plaintiff did not add any new allegations to support his claim, and seeks, among other relief, civil penalties for Uber's PAGA violation. (*See* FAC at 2-3.)

III.   **LEGAL STANDARD**

A demurrer tests the legal sufficiency of a complaint or a particular cause of action.

Award Metals, Inc. v. Superior Court, 228 Cal. App. 3d 1128, 1131 (1991) (citation omitted). A court must sustain a demurrer where the complaint fails to set forth well-pled facts establishing a right to relief. *Longshore v. Cnty. of Ventura*, 25 Cal. 3d 14, 22 (1979); Cal. Code Civ. Proc. ("CCP") § 430.10(e). A demurrer is "treat[ed] [] as admitting all material facts properly pleaded, but not contentions, deductions or conclusions of fact or law." *Berryman v. Merit Prop. Mgmt., Inc.*, 152 Cal. App. 4th 1544, 1550 (2007) (quotation and citation omitted). Matters which may be judicially noticed are also considered, which include documents that are incorporated by reference in the complaint. *See Pac. Emp'rs Ins. Co. v. California*, 3 Cal. 3d 573, 575 n.1 (1970); *Ascherman v. Gen. Reinsurance Corp.*, 183 Cal. App. 3d 307, 311 (1986) (taking judicial notice of a document referenced in, but not attached to, plaintiff's complaint because "courts may consider [such] evidence . . . when ruling on the propriety of the demurrer"). The Court may disregard facts if they are contradicted by facts of which the Court may take judicial notice. *See Embarcadero Mun. Improvement Dist. v. Cnty. of Santa Barbara*, 88 Cal. App. 4th 781, 786 (2001) (citation omitted).

A demurrer should be sustained without leave to amend where "the nature of the plaintiff's claim is clear and under the applicable substantive law it is plain that there can be no liability," *Award Metals*, 228 Cal. App. 3d at 1132, or where there is no "reasonable possibility that the defect can be cured by amendment." *Blank v. Kirwan*, 39 Cal. 3d 311, 318 (1985).

IV. THE FAC DOES NOT STATE A CLAIM FOR A VIOLATION OF PAGA.

Uber's demurrer should be sustained without leave to amend because the FAC fails to state a PAGA violation upon which relief may be granted. PAGA permits individuals to bring private actions against an employer for civil penalties for violations of certain sections of the Labor Code. Cal. Lab. Code § 2698 *et seq*. To bring a PAGA claim, Plaintiff must show that he is an "aggrieved employee." Cal. Lab. Code § 2699(g)(1) (only an "aggrieved employee" may maintain a civil action to recover civil penalties for California Labor Code violations "on behalf of himself or herself and other current or former employees against whom one or more of the alleged violations was committed"). An "aggrieved employee" is "any person who was employed by the alleged violator and against whom one or more of the alleged violations was

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committed." *Id.* at § 2699(c). Accordingly, to establish that he is an "aggrieved employee," Plaintiff must show that Uber violated one of the specified Labor Code provisions.

Here, Plaintiff seeks civil penalties for Uber's alleged violations of four Labor Code Sections covered by PAGA – Sections 201, 202, 204, and 970. (FAC ¶ 15); Cal. Lab. Code § 2699.5. Yet the FAC (including the incorporated PAGA Notice) pleads no facts to establish that Uber violated any of these sections. Because Plaintiff fails to state a claim for any Labor Code violation by Uber, Plaintiff cannot show that he is an aggrieved employee and, thus, cannot state a PAGA claim.

A.   Plaintiff Fails to State a Claim for Violations of California Labor Code Sections 201, 202 and 204 Because Stock Options Do Not Constitute Wages.

The FAC does not plead a violation under Sections 201, 202 and 204 because Plaintiff fails to allege that Uber's alleged misconduct concerns wages, an essential element to prove violations under these wage-related Labor Code sections.

To sufficiently plead a claim under Sections 201 and 202, a plaintiff must allege that his employer did not pay the plaintiff his earned *wages* immediately upon his discharge or resignation. Cal. Lab. Code §§ 201(a), 202(a). Similarly, to establish a claim under Section 204, a plaintiff must allege that the employer did not make timely payment of *wages* as required under the statute. Cal. Lab. Code § 204(a) (requiring payment of wages "twice during each calendar month, on days designated in advance by the employer as the regular paydays.").

In this case, Plaintiff contends that Uber's failure to compensate him with the *stock options* promised in his Employment Agreement constitutes violations of these wage-related sections of the Labor Code. But it is well-established that under California law, stock options do not constitute wages. *See Schachter v. Citigroup, Inc.*, 47 Cal. 4th 610, 623 (2009); *IBM v. Bajorek*, 191 F. 3d 1033, 1039 (9th Cir. 1999). Plaintiff has not asserted any additional facts to support these claims. Where, as here, the FAC contains no allegations related to *wages*, Plaintiff cannot state a claim for a violation of these sections. *See, e.g., Schachter*, 47 Cal. 4th at 623 (employer's forfeiture of employee's restricted stock options upon resignation without compensation to the employee did not violate Sections 201 or 202 because stock options are not

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wages owed to the employee).[2]

B. Plaintiff Fails to State a Claim for Violation of Section 970.

Similarly, the FAC lacks sufficient allegations to state a claim for violation of Labor Code Section 970. Section 970 prohibits employers from inducing employees to move to, from, or within California based on misrepresentations concerning the terms and conditions of employment. Cal. Lab. Code § 970. Plaintiff has alleged no facts showing that Uber made any such false representations to him.

To plead misrepresentation under this section, a plaintiff must allege that the employer made a promise "without any intention to perform it." *Tyco Indus., Inc. v. Superior Court*, 164 Cal. App. 3d 148, 156 (1985) (citation omitted). Here, Plaintiff claims that the "false representations" contained in his Employment Agreement concern Uber's promises regarding: 1) the type of options he would receive and 2) when those options would be exercisable. (*See* Ex. 3, PAGA Notice at 6.) Similarly, Plaintiff contends that Uber promised to grant him ISOs, but that Uber "never intended to provide[] the promised compensation." (*Id.* at 5.)

Plaintiff's claim fails, however, because the Employment Agreement does not contain any enforceable promise with respect to equity compensation. Plaintiff's Employment Agreement explicitly stated that the Option was to be granted "[s]ubject to the approval of the Company's Board of Directors." (Ex. 1, Employment Agreement at ¶ 2(c).) It was therefore clearly stated to Plaintiff that the terms of his Option were contingent on the approval of Uber's Board of Directors (the "Board"), including the time for exercise. (*Id.*)

Because the promise in the Employment Agreement was contingent upon Board approval, Uber's Board retained the discretion to grant the Option on such terms as it deemed appropriate

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[2] Even if Sections 201, 202 and 204 did apply to stock options (which they do not), the FAC still fails to state a claim under those sections for two additional reasons. First, Sections 201 and 202 govern the payment of final wages upon termination or separation from employment. Here, however, Plaintiff has been, and remains, employed by Uber. (FAC ¶ 1.) As such, Sections 201 and 202 have not been triggered. Second, with respect to Section 204, Plaintiff does not allege (nor can he) that Uber failed to pay his wages on a timely semimonthly basis. *See See's Candy Shops, Inc. v. Superior Court*, 210 Cal. App. 4th 889, 905 (2012) (citation omitted) (recognizing Section 204 provides an employee's right to the "timely payment of wages"). Thus, Plaintiff cannot meet the "semimonthly" element necessary to state a claim for a violation of Section 204.

or even not to grant the Option at all. Under Delaware law, Board approval is required for the

issuance of options. *See* Del. Code tit. 8, § 157 (granting exclusive authority to a company's

board of directors to issue stock options and determine their terms, and requiring a written

instrument to create rights respecting those stock options).[3] As such, there can be no binding and

enforceable promise until the option is approved and granted by the Board. *See Patriot Sci.*

Corp., 504 F. Supp. 2d at 958-60 (applying Delaware law and dismissing plaintiff's breach of

contract claim based on defendant's alleged failure to grant plaintiff his allegedly promised stock

options where defendant's board of directors did not approve of the issuance of those stock

options in a written instrument); *Randolph v. CAS Med. Sys., Inc.*, No. CV085020807S, 2011 WL

3276813 (Conn. Super. Ct. July 1, 2011) (applying Delaware law and entering judgment in favor

of defendant on breach of contract claim where defendant's failure to grant stock options

allegedly promised in plaintiff's employment agreement was not approved by the defendant's

board).

In short, Plaintiff has not alleged sufficient facts showing any misrepresentation made by

Uber. Here, the Employment Agreement explicitly warned Plaintiff that his Option terms were

subject to the Board's approval. Accordingly, Plaintiff's allegations concerning Uber's alleged

false statements regarding his Option are contradicted by the Employment Agreement and those

allegations should thus be disregarded. *See Scott v. JPMorgan Chase Bank, N.A.*, 214 Cal. App.

4th 743, 751 (2013) ("[A] demurrer may be sustained where judicially noticeable facts render the

pleading defective . . . and allegations in the pleading may be disregarded if they are contrary to

facts judicially noticed." (citations omitted)); *see also Embarcadero Mun. Improvement Dist.*, 88

Cal. App. 4th at 786. Absent those allegations, Plaintiff fails to state a claim under Labor Code

Section 970. *See* Cal. Lab. Code § 970(b); *Tyco Indus., Inc.*, 164 Cal. App. 3d at 156.

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[3] Uber is incorporated in Delaware. (FAC ¶ 2.) Thus, under California's "internal affairs doctrine," Delaware law governs matters involving regulation of Uber's corporate governance, such as the issuance of Uber's stock. *See Patriot Sci. Corp. v. Korodi*, 504 F. Supp. 2d 952, 956 (S.D. Cal. 2007); *see also* Del. Code tit. 8, § 121(b).

1   Because Plaintiff cannot state a claim under Labor Code Sections 201, 202, 204, or 970,

2   Plaintiff cannot meet the "aggrieved employee" requirement to assert a PAGA claim. Thus,

3   Plaintiff's PAGA claim cannot survive a demurrer and should be dismissed.

C.   **Plaintiff Is Not Entitled Leave to Amend.**

5   Any request by Plaintiff for leave should be denied because amendment would be futile.

6   *Jager v. Cnty. of Alameda*, 8 Cal. App. 4th 294, 297 (1992). Amendment is futile if "the nature

7   of the claim is clear, but there is no liability under substantive law." *Wilhelm v. Pray, Price,*

8   *Williams & Russell*, 186 Cal. App. 3d 1324, 1330 (1986) (citation omitted); *see Crosby v. Wells*

9   *Fargo Banks, N.A.*, 42 F. Supp. 3d 1343, 1346 (C.D. Cal. 2014) (dismissing PAGA claim with

10   prejudice where "any further amendment would be futile"). Here, for the reasons discussed

11   above, Plaintiff has not (and cannot) plead any facts to support his PAGA claim. Accordingly,

12   the FAC should be dismissed with prejudice.

V.   **CONCLUSION**

14   For all of the reasons stated herein, the Court should sustain Uber's demurrer to Plaintiff's

15   FAC in its entirety without leave to amend.

16   Dated: August 16, 2016   COOLEY LLP

18   By: *Patrick Gibbs* uys

19   Patrick E. Gibbs

20   Attorneys for Defendant,
                                                     UBER TECHNOLOGIES, INC.

COOLEY LLP
ATTORNEYS AT LAW
PALO ALTO

PROOF OF SERVICE

I am a citizen of the United States and a resident of the State of California. I am employed in Santa Clara County, State of California, in the office of a member of the bar of this Court, at whose direction the service was made. I am over the age of 18 years, and not a party to the within action. My business address is Cooley LLP, 3175 Hanover Street, Palo Alto, California 94304-1130. My e-mail address is bgiovannoni@cooley.com. On August 16, 2016, I served the following documents on the parties listed below in the manner(s) indicated:

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF UBER TECHNOLOGIES, INC.'S DEMURRER TO FIRST AMENDED COMPLAINT

☒   (BY ELECTRONIC MAIL – CCP § 1010.6(a)(6)) Based on a court order or an agreement of the parties to accept service by e-mail or electronic transmission, I caused such documents described herein to be sent to the persons at the e-mail addresses listed below at approximately _____. I did not receive, within a reasonable time after the transmission, any electronic message or other indication that the transmission was unsuccessful.

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I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Executed on August 16, 2016, at Palo Alto, California.

_____
Brandie Giovannoni

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