UNITED STATES DISTRICT COURT

DISTRICT OF MASSACHUSETTS

__________, Individually and on Behalf of All Others Similarly Situated, Plaintiff, vs. WAYFAIR INC., NIRAJ SHAH, STEVEN K. CONINE and MICHAEL D. FLEISHER, Defendants.	))))))))))))	No. <u>CLASS ACTION</u> COMPLAINT FOR VIOLATION OF THE FEDERAL SECURITIES LAWS <u>DEMAND FOR JURY TRIAL</u>

Plaintiff _______ ("plaintiff") alleges the following based upon the investigation of her counsel, which included a review of U.S. Securities and Exchange Commission ("SEC") filings by Wayfair Inc. ("Wayfair" or the "Company"), as well as regulatory filings and reports, securities analysts' reports and advisories about the Company, press releases and other public statements issued by the Company, and media reports about the Company. Plaintiff believes that substantial additional evidentiary support will exist for the allegations set forth herein after a reasonable opportunity for discovery.

NATURE OF THE ACTION

1. This is a securities class action on behalf of all purchasers of Wayfair Class A common stock between August 2, 2018 and October 31, 2018, inclusive (the "Class Period"). The claims are brought under the Securities Exchange Act of 1934 ("1934 Act").

JURISDICTION AND VENUE

2. The claims asserted herein arise under and pursuant to §§10(b) and 20(a) of the 1934 Act [15 U.S.C. §§78j(b) and 78t(a)] and SEC Rule 10b-5 [17 C.F.R. §240.10b-5]. This Court has jurisdiction over the subject matter of this action pursuant to 28 U.S.C. §1331 and §27 of the 1934 Act.

3. Venue is proper in this District pursuant to 28 U.S.C. §1391(b), because Wayfair is headquartered in this District and many of the acts and practices complained of herein occurred in substantial part in this District.

4. In connection with the acts and conduct alleged in this complaint, defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, including, but not limited to, the mails and interstate wire and telephone communications.

PARTIES

5. Plaintiff ________ acquired Wayfair common stock, as set forth in the accompanying certification, and has been damaged thereby.

6. Defendant Wayfair is an online purveyor of household retail goods. Wayfair is headquartered at 4 Copley Place, 7th Floor, Boston, Massachusetts. As of October 24, 2018, Wayfair had more than 61.8 million shares of its Class A common stock issued and outstanding and more than 28.5 million shares of its Class B common stock issued and outstanding. The rights of the holders of Class A common stock and Class B common stock are identical, except with respect to voting and conversion rights. Each share of Class A common stock is entitled to one vote per share and each share of Class B common stock is entitled to ten votes per share. Each share of Class B common stock may be converted into one share of Class A common stock at the option of its holder and will be automatically converted into one share of Class A common stock upon transfer thereof, subject to certain exceptions. Wayfair Class A common stock was listed and traded in an efficient market on the New York Stock Exchange ("NYSE") throughout the Class Period under the ticker symbol "W."

7. Defendant Niraj Shah ("Shah") is a co-founder of Wayfair and is and was, at all relevant times, its President, Chief Executive Officer and Co-Chairman of its Board of Directors.

8. Defendant Steven K. Conine ("Conine") is a co-founder of Wayfair and is and was, at all relevant times, Co-Chairman of its Board of Directors.

9. Defendant Michael D. Fleisher ("Fleisher") is and was, at all relevant times, Chief Financial Officer of Wayfair.

10. Defendants Shah, Conine and Fleisher are referred to herein as the "Individual Defendants." Wayfair and the Individual Defendants are referred to herein, collectively, as "Defendants."

11. Defendants are liable for: (i) making false statements; or (ii) failing to disclose adverse facts known to them about Wayfair. Defendants' fraudulent scheme and course of business that operated as a fraud or deceit on purchasers of Wayfair common stock was a success, as it: (i) deceived the investing public regarding Wayfair's prospects and business; (ii) artificially inflated the price of Wayfair common stock; (iii) allowed certain of Wayfair executives and insiders to cash out, selling millions of dollars' worth of their personally held shares of Wayfair common stock at fraud-inflated prices, including the Individual Defendants named herein, who collectively sold approximately $67 million worth of their personally held shares during the Class Period; and (iv) caused plaintiff and other members of the Class to purchase Wayfair common stock at inflated prices.

SUBSTANTIVE ALLEGATIONS

12. Defendant Wayfair is engaged in the e-commerce business in the United States, Europe, and internationally. The Company offers approximately 10 million products for the home sector under various brands. It offers a selection of furniture, décor, decorative accents, housewares, seasonal décor, and other home goods through its sites, such as Wayfair, Joss & Main, AllModern, DwellStudio, Perigold, and Birch Lane.

13. The Class Period starts on August 2, 2018. On that day, before the opening of the market, Wayfair issued a press release announcing its second quarter 2018 ("2Q18") financial results for the period ended July 30, 2018. The release emphasized Wayfair's "Q2 Direct Retail Net Revenue Growth of 49% Year over Year to $1.6 billion" and that it had "12.8 million Active Customers, ***up 34% Year over Year***." Stating that the Company had spent $177.6 million on advertising during 2Q18, the release quoted defendant Shah, who highlighted the Company's purportedly stellar ongoing customer growth, sales and profitability trends, stating in pertinent part as follows:

> "We are pleased to report a record second quarter and our largest yet year-over-year dollar growth in Direct Retail net revenue. This recent quarter included our biggest revenue day in the history of the company as we introduced Way Day, the first-ever retail holiday for home . . . . ***Our long-term investments in further developing our logistics networks, international business, and in scaling headcount to improve our product and service offerings are resonating strongly with new and returning customers. By focusing on bringing customers the best possible experience in shopping for the home, from the home, we are leading the way in our category. We are delighted with the progress that we are making and the way in which we are positioned to keep taking market share as dollars shift online***."

14. Also on August 2, 2018, Wayfair conducted a conference call with investors and stock analysts during which the three Individual Defendants provided additional positive statements about the Company's then present business metrics and financial prospects. During his prepared remarks, defendant Fleisher provided the following guidance for Wayfair's third quarter of 2018 ("3Q18"), ending September 30, 2018, stating in pertinent part as follows:

> For Q3 quarter-to-date, our growth in Direct Retail gross revenue is back to running at a more normalized level of approximately 40%. Setting guidance is always a difficult task given our rate of growth, and predicting the exact timing of the payoff from various initiatives adds an additional layer of complexity. ***The guidance we're giving for Q3 reflects that and our desire to be prudent when forecasting our mass-market consumer business where the customer has to show up every day***.
>
> For Q3 2018, we forecast Direct Retail net revenue of $1.61 billion to $1.645 billion, a growth rate of approximately 36% to 39% year-over-year and representing year-over-year Direct Retail dollar growth of approximately $450 million. Within that, we expect U.S. Direct Retail year-over-year growth in the range of 34% to 36% and international Direct Retail year-over-year growth in the range of 50% to 60%. We forecast other revenue to be between $13 million to $17 million, for total net revenue of $1.623 billion to $1.662 billion for the third quarter.
>
> ***For consolidated adjusted EBITDA, we forecast margins of negative 3.7% to negative 4% for Q3 2018***. We expect international adjusted EBITDA to be negative $45 million to negative $50 million in Q3 as we continue to add resources and ad spend in Canada, the U.K. and Germany. In the U.S. business, we expect to deliver adjusted EBITDA margin of approximately negative 1% as we invest primarily in headcount to build continued scale in our primary market.
>
> As I highlighted earlier, we expect the rate of hiring to continue at elevated levels in Q3, and this will weigh on Q3 profitability, before an expected sequential reduction in the rate of hiring in Q4 as we both slow the pace of hiring substantially

and start to see the leverage of the larger employee base faced off on our many growth initiatives.

We remain incredibly bullish about our business, both in the near term and long term. The investments we have been making to bring our customers the best possible offering are clearly working with strength across our customer KPIs and our market share growing, as a result. We plan to continue investing in these strategic priorities and are excited by the scale of the opportunity that we see in front of us and our ability to keep winning as we go after it.

15. Specifically addressing advertising spending during the conference call, defendant Fleisher reassured investors that the spending was all targeted, directed and highly profitable, stating in pertinent part as follows:

Q2 advertising spend of $178 million or 10.7% of net revenue represents year-over-year leverage of over 30 basis points, ***as we invest in engaging both new and repeat customers and benefit from a growing base of repeat customers who require a lower level of ad spend per dollar of revenue***.

16. During the Q&A session of the conference call, defendant Shah engaged in the following discussion with an analyst from BofA Merrill Lynch, again reassuring investors that the Company's advertising spending was highly targeted, direct and profitable, ***because Wayfair was handling it in-house under its own control***. The following exchange took place:

[Akshay Bhatia – BofA Merrill Lynch:] One thing that is becoming more prevalent in the e-commerce space is advertising within the marketplace. So wanted to ask you what Wayfair is doing on the advertising front? Maybe what opportunity you see there? And what tailwind do you think this could be the margins longer term?

[Shah:] Yes. We think advertising is an area of very high potential benefit. To be fair, on one hand, . . . we're very excited about it. When we talk about hiring people for these teams and the investment we're making in headcount, this is a great example of an area that, over the last couple of quarters, we've really staffed that up with a great team that I'm very excited about. A lot of the early work they're doing, but then, to be fair, it's early work. So in terms of when it's real impact on the P&L, it's still a little ways out.

For us, we think advertising is going to be a little more nuance than what some other folks can do where they can just kind of plaster it on the top, because that doesn't affect the customer experience negatively because, for example, if

you're selling batteries, whether you let Duracell or Energizer dominate the page, it doesn't matter as long you have both on Page 1 and Page 2.

We need to be thoughtful in terms of making sure that we use the diversity of product, the right styles for the consumer to continue to engage them. But then there's things we can do, for example, to let suppliers help launch their new products and get them ramped more quickly and help fund that. So we're actually very excited about some advertising products that we have underway. But in terms of the P&L impact, I'd both say I'm excited about how big it can be, but I'd also say that that's a ways out.

[Bhatia:] Got it. And maybe as a follow-up, can you talk about what you're doing differently on the marketing side that you can still drive leverage while adding nearly 1 million customers? Anything to call out there? Or is it really just the repeat rate growing?

[Shah:] ***I think the key thing to keep in mind on what we do on our paid advertising, and this is a very unique thing for us when you compare us to other folks, is we built all our advertising technology in-house. And so when you think about building your own ad tech, being able to then take your first part of data and really, nuance clickstream data, your own algorithms are at honed to your categories and your customer kind of life cycle and then take those and integrate them into the advertising products out there, that's a huge benefit***.

We then kind of further fuel that. Pinterest, Facebook, Google have all publicly named us as a partner with whom they codevelop ad units, who's their early alpha and beta partner in things. Google mentioned us PLAs and trusted stores. Facebook mentioned us on their earnings call about a year ago. ***And so what we found is that by being an innovator and understanding every bit of the nuances on how these platforms work on the new products and then building our own ad tech for integration, for bidding and for our own algorithms, you can always sort of further progress what you can do***.

And obviously you have the trends – we have trends on data that we use. So there's no reason why – if you think about – when we think about 12.8 million customers, that's less than 10% of the potential customers. We think that about 70 million households in the United States, 70 million households in Europe and Canada, 140 million – 12.8 million is still not that many. So there's a lot of new customers to get. And then, obviously, the share of wallet is a huge opportunity. But to your point, repeat is, obviously, a big opportunity, too. ***So I think building our own ad tech has been a huge advantage***, but there's also a lot more customers to get, so that's why we keep adding.

17. That same day, Wayfair filed its quarterly report on Form 10-Q with the SEC, which was signed and certified pursuant to the Sarbanes Oxley Act of 2002 by Individual Defendants Shah

and Fleisher. The Form 10-Q provided the same 2Q18 financial results disclosed above, and stated the following concerning the Company's advertising spending then underway:

> **Advertising**
>
> Advertising consists of direct response performance marketing costs, such as display advertising, paid search advertising, social media advertising, search engine optimization, comparison shopping engine advertising, television advertising, direct mail, catalog and print advertising. We expect advertising expense to continue to increase ***but decrease as a percentage of net revenue over time due to our increasing base of repeat customers***.

18. On these positive statements, the price of Wayfair Class A common stock skyrocketed, increasing from $107 per share on August 1, 2018 to a Class Period high of more than $150 per share by September 14, 2018. Wayfair's senior executives and directors cashed in, selling tens of thousands of their personally held shares for tens of millions of dollars in proceeds. Defendant Shah sold 245,071 shares for $32.377 million in proceeds; defendant Conine sold 245,066 shares for $32.378 million in proceeds; and defendant Fleisher sold 20,565 shares for $2.576 million in proceeds. Collectively, the Individual Defendants and other Wayfair insiders sold more than $87.75 million worth of their personally held Wayfair shares during the Class Period.

19. The statements referenced above in ¶¶13-17 were materially false and misleading because they failed to disclose the following material adverse facts which were known to Defendants or recklessly disregarded by them:

(a) that Wayfair had been experiencing significantly diminished demand for its online product offerings and had significantly increased advertising spending to grow sales;

(b) that Wayfair, which was already more than one-third of the way into its 3Q18 when its announced its 2Q18 results on August 2, 2018, had already dramatically increased advertising spending for its 3Q18; and

(c) as a result, Defendants' statements about Wayfair's business, operations and prospects were materially false and misleading and/or lacked a reasonable basis at all relevant times.

20. On November 1, 2018, before the open of trading, Wayfair issued a press release announcing its 3Q18 financial results. Though its Direct Retail net revenue grew 43.3% year over year, the Company reported a massive $151.7 million net loss for the quarter under Generally Accepted Accounting Principles ("GAAP"), or $(1.69) per share, compared with a GAAP loss of $76.4 million, or $(0.88) per share, for 3Q17. In reality, advertising expenses had skyrocketed in 3Q18 to more than $202.5 million, an increase of 43%, meaning that total operating expenses rose 52% to $538 million and costs rose by more than 50% for expenses, including technology and operations as well as customer service and merchant fees, significantly increasing the Company's reported GAAP losses. Rather than the 3Q18 "consolidated adjusted EBITDA . . . margins of negative 3.7% to negative 4%" Defendants had stated the Company was on track to achieve on August 2, 2018, Wayfair reported a negative adjusted EBITDA of "$(76.4) million ***or (4.5)% of total net revenue***."

21. As a result, Wayfair's U.S. business was not profitable in 3Q18, and on a conference call conducted with investors that morning, Defendants disclosed that the segment would also post a loss in the fourth quarter of 2018 ("4Q18"), ending December 31, 2018 – the quarter that included the key holiday shopping season. Conversely, the U.S. segment had been profitable in 3Q17 and 2Q18.

22. On this news, the price of Wayfair common stock declined precipitously, closing down more than $14 per share, or nearly 13%, to close at $96.16 per share on November 1, 2018, on unusually high volume of more than 9.9 million shares traded, almost seven times the average daily trading volume.

23. Stock analyst Tom Forte, managing director for D.A. Davidson & Co., was quoted by *The Wall Street Journal* as stating: "'The basic story of Wayfair has been we're going to invest for growth today and our growth will be so significant that in the future when we scale our investment spending, our profitability . . . will be so much greater . . . .'" Adding, "[b]ut the Company needs to spend more [on advertising] to keep growing sales at the current rate."

24. And as reported by *CNBC*:

> Over the past year, the online home furnishing store added 3.6 million new active customers, about 35 percent more over 2017, but it's spending a lot to attract them, according to Neil Saunders [managing director of GlobalData Retail] . . . .
>
> "Over the same period, spend on advertising was around $707 million. ***This works out at $196 per new customer. When customers only spend $443 a year, this seems like a rather excessive, and completely unprofitable, acquisition cost*** . . . ."

ADDITIONAL SCIENTER ALLEGATIONS

25. As alleged herein, Wayfair and the Individual Defendants acted with scienter in that they knew that the public documents and statements issued or disseminated in the name of the Company were materially false and misleading; knew that such statements or documents would be issued or disseminated to the investing public; and knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements or documents as primary violations of the federal securities laws. As set forth elsewhere herein in detail, these Defendants, by virtue of their receipt of information reflecting the true facts regarding Wayfair, their control over, and/or receipt and/or modification of Wayfair's allegedly materially misleading statements and/or their associations with the Company, which made them privy to confidential proprietary information concerning Wayfair, participated in the fraudulent scheme alleged herein.

LOSS CAUSATION/ECONOMIC LOSS

26. During the Class Period, as detailed herein, the Defendants made false and misleading statements and engaged in a scheme to deceive the market and a course of conduct that artificially inflated the price of Wayfair stock and operated as a fraud or deceit on Class Period purchasers of Wayfair stock by misrepresenting the Company's business and prospects. Later, when the Defendants' prior misrepresentations and fraudulent conduct became apparent to the market, the price of Wayfair stock fell precipitously, as the prior artificial inflation came out of the price over time. As a result of their purchases of Wayfair Cass A stock during the Class Period, plaintiff and other members of the Class suffered economic loss, *i.e*., damages, under the federal securities laws.

NO SAFE HARBOR

27. Wayfair's verbal "Safe Harbor" warnings accompanying its oral forward-looking statements ("FLS") issued during the Class Period were ineffective to shield those statements from liability.

28. The Defendants are also liable for any false or misleading FLS pleaded because, at the time each FLS was made, the speaker knew the FLS was false or misleading and the FLS was authorized and/or approved by an executive officer of Wayfair who knew that the FLS was false. None of the historic or present tense statements made by Defendants were assumptions underlying or relating to any plan, projection or statement of future economic performance, as they were not stated to be such assumptions underlying or relating to any projection or statement of future economic performance when made, nor were any of the projections or forecasts made by Defendants expressly related to or stated to be dependent on those historic or present tense statements when made.

CLASS ACTION ALLEGATIONS

29. Plaintiff brings this action as a class action pursuant to Federal Rule of Civil Procedure 23(a) and (b)(3) on behalf of a class consisting of all purchasers of Wayfair Class A

common stock during the Class Period who were damaged thereby (the "Class"). Excluded from the Class are Defendants and their families, the officers and directors of the Company, at all relevant times, members of their immediate families and their legal representatives, heirs, successors or assigns and any entity in which Defendants have or had a controlling interest.

30. The members of the Class are so numerous that joinder of all members is impracticable. Wayfair Class A common stock was actively traded. While the exact number of Class members is unknown to plaintiff at this time and can only be ascertained through appropriate discovery, plaintiff believes that there are hundreds or thousands of members in the proposed Class. Record owners and other members of the Class may be identified from records maintained by Wayfair or its transfer agent and may be notified of the pendency of this action by mail, using the form of notice similar to that customarily used in securities class actions.

31. Plaintiff's claims are typical of the claims of the members of the Class as all members of the Class are similarly affected by Defendants' wrongful conduct in violation of federal law that is complained of herein.

32. Plaintiff will fairly and adequately protect the interests of the members of the Class and has retained counsel competent and experienced in class and securities litigation.

33. Common questions of law and fact exist as to all members of the Class and predominate over any questions solely affecting individual members of the Class. Among the questions of law and fact common to the Class are:

(a) whether the 1934 Act was violated by Defendants' acts as alleged herein;

(b) whether statements made by Defendants to the investing public during the Class Period misrepresented material facts about the business, operations and prospects of Wayfair; and

(c) to what extent the members of the Class have sustained damages and the proper measure of damages.

34. A class action is superior to all other available methods for the fair and efficient adjudication of this controversy since joinder of all members is impracticable. Furthermore, as the damages suffered by individual Class members may be relatively small, the expense and burden of individual litigation make it impossible for members of the Class to individually redress the wrongs done to them. There will be no difficulty in the management of this action as a class action.

COUNT I

For Violation of §10(b) of the 1934 Act and Rule 10b-5 Against All Defendants

35. Plaintiff incorporates ¶¶1-34 by reference.

36. During the Class Period, Defendants disseminated or approved the false statements specified above, which they knew or deliberately disregarded were misleading in that they contained misrepresentations and failed to disclose material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

37. Defendants violated §10(b) of the 1934 Act and Rule 10b-5 in that they:

(a) employed devices, schemes and artifices to defraud;

(b) made untrue statements of material fact or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or

(c) engaged in acts, practices and a course of business that operated as a fraud or deceit upon plaintiff and others similarly situated in connection with their purchases of Wayfair Class A common stock during the Class Period.

38. Plaintiff and the Class have suffered damages in that, in reliance on the integrity of the market, they paid artificially inflated prices for Wayfair Class A common stock. Plaintiff and the Class would not have purchased Wayfair Class A common stock at the prices they paid, or at all, if they had been aware that the market prices had been artificially and falsely inflated by Defendants' misleading statements.

COUNT II

Violations of §20(a) of the 1934 Act
Against All Defendants

39. Plaintiff incorporates ¶¶1-38 by reference.

40. The Individual Defendants acted as controlling persons of Wayfair within the meaning of §20(a) of the 1934 Act. By reason of their positions with the Company, and their ownership of Wayfair stock, the Individual Defendants had the power and authority to cause Wayfair to engage in the wrongful conduct complained of herein. Wayfair controlled the Individual Defendants and all of its employees. By reason of such conduct, Defendants are liable pursuant to §20(a) of the 1934 Act.

PRAYER FOR RELIEF

WHEREFORE, plaintiff prays for relief and judgment, as follows:

A. Determining that this action is a proper class action, designating plaintiff as Lead Plaintiff and certifying plaintiff as a Class representative under Rule 23 of the Federal Rules of Civil Procedure and plaintiff's counsel as Lead Counsel;

B. Awarding compensatory damages in favor of plaintiff and the other Class members against all Defendants, jointly and severally, for all damages sustained as a result of Defendants' wrongdoing, in an amount to be proven at trial, including interest thereon;

C. Awarding plaintiff and the Class their reasonable costs and expenses incurred in this action, including counsel fees and expert fees; and

D. Such equitable/injunctive or other relief as may be deemed appropriate by the Court.

JURY DEMAND

Plaintiff hereby demands a trial by jury