IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

United States Courts
Southern District of Texas
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IN RE ENRON CORPORATION SECURITIES LITIGATION	
This Document Relates To:	
MARK NEWBY, et al., Individually and On Behalf of All Others Similarly Situated, Plaintiffs, v. ENRON CORP., et al., Defendants.	Consolidated Civil Action Case No.: H-01-CV-3624 (Jury)
THE REGENTS OF THE UNIVERSITY OF CALIFORNIA, et al., Individually and On Behalf of All Others Similarly Situated, Plaintiffs, v. KENNETH L. LAY, et al., Defendants.	

DEFENDANTS J.P. MORGAN CHASE & CO., J.P. MORGAN SECURITIES INC., AND JPMORGAN CHASE BANK'S REPLY BRIEF IN FURTHER SUPPORT OF THEIR MOTION TO DISMISS THE FIRST AMENDED CONSOLIDATED COMPLAINT

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Defendants J.P. Morgan Chase & Co. ("JPMC"), J.P. Morgan Securities Inc. ("JPMSI") and JPMorgan Chase Bank ("JPMCB") (collectively, "JPMorgan Chase" or the "JPMorgan Chase Entities") respectfully submit this Reply Memorandum of Law in further support of their motion to dismiss Plaintiffs' First Amended Consolidated Complaint for Violation of the Securities Laws (the "Amended Complaint" or "Am. Compl.").[1]

PRELIMINARY STATEMENT

Plaintiffs' Opposition seeks to sidestep JPMorgan Chase's motion to dismiss the Amended Complaint by labeling JPMorgan Chase's challenges "technical" and "nitpicking." To be sure, we do not here, on this Rule 12(b) motion, argue the merits of the claims alleged in the Amended Complaint, nor would it be proper to do so. In no way, however, does this mean that JPMorgan Chase's defense of this case is purely technical.

Instead, if Plaintiffs' action survives this motion and later appropriate motions for summary judgment, JPMorgan Chase will adduce at trial evidence that will controvert Plaintiffs' baseless allegations. The facts will show that Plaintiffs' assertion that JPMorgan Chase knew about Enron's true financial condition is false and that – in light of the $2.6 billion in Enron obligations to which JPMorgan Chase was exposed and JPMorgan Chase's release of security in the months preceding Enron's bankruptcy – the allegation does not even make sense. The facts will show that Plaintiffs' contention that JPMorgan Chase's prepay forward transactions were improper "disguised loans" is also false. While the Enron prepays provided financing, they were not loans, in either form or substance, and, to JPMorgan Chase's knowledge and understanding, the prepay transactions were entered into for perfectly legitimate purposes and were accounted

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[1] In addition to the arguments herein, the JPMorgan Chase Entities adopt and incorporate by reference the arguments in the other bank defendants' reply memoranda to the extent applicable to the JPMorgan Chase Entities.

for in accordance with generally accepted accounting principles. The facts likewise will show that the fraud at Enron was not the use structured financing provided by, among others, JPMorgan Chase, but rather the alleged fraudulent reporting of financing and other transactions by Enron. And there, the evidence will demonstrate that JPMorgan Chase did not play any role, let alone mislead anyone: JPMorgan Chase did not provide tax, accounting or auditing services to Enron. Instead, the decisions about financial disclosures by Enron were made by Enron and its legion of accountants, auditors and other professionals who advised on, and prepared, its audited financial statements. In short, the evidence in this case will show that JPMorgan Chase was not a part of the fraud at Enron and that Plaintiffs have no claim against JPMorgan Chase.

On this motion, JPMorgan Chase has demonstrated several deficiencies in Plaintiffs' Amended Complaint, the resolution of which does not require judging facts. And Plaintiffs' rhetorical exercise in characterizing these deficiencies does not fix the fatal pleading, statute of limitations, standing and other problems with the Amended Complaint. This Reply Memorandum demonstrates that none of the arguments in the Plaintiffs' Opposition saves the Amended Complaint from dismissal.

First, the one-year time bar plainly applies to Plaintiffs' claims here. Plaintiffs' misconstruction of the Sarbanes-Oxley Act's amended limitations period is not only inconsistent with the express language of the statute, but also with this Court's prior ruling on this very issue in this case. Plaintiffs also ignore the long-established legal doctrine that "inquiry notice" is sufficient to trigger the applicable statute of limitations.

Second, Plaintiffs effectively concede their lack of standing to assert any claims against JPMSI and JPMC under Sections 12(a)(2) and 15 of the Securities Act of 1933 (the "1933 Act"), respectively. Their plea to the Court to wait, for no good reason, until it considers

Plaintiffs' motion for class certification is disingenuous. Moreover, the controlling principles set forth by the U.S. Supreme Court demonstrate that JPMSI was *not* a "seller" under Section 12(a)(2) and the securities in question were *not* distributed "by means of a prospectus."

Third, Plaintiffs' control person claims against JPMC pursuant to Section 20(a) of the Securities Exchange Act of 1934 (the "1934 Act") and Section 15 of the 1933 Act remain not only wholly conclusory, but Plaintiffs fail to state a claim for the necessary predicate violations of Sections 10(b) and 12(a)(2) against JPMSI and JPMCB.

Fourth, Plaintiffs cannot supplement the Amended Complaint's impermissible "group pleading" by adding allegations in the Opposition papers or citing non-public documents not referenced in the Amended Complaint.

The Amended Complaint should be dismissed against the JPMorgan Chase Entities.

ARGUMENT

The Amended Complaint, filed May 14, 2003, adds two former bystanders to this litigation, JPMSI and JPMCB. Against both, Plaintiffs allege causes of action under Section 10(b) of the 1934 Act (Count I) and Article 581-33(A)(2) of the Texas Securities Act ("TSA") (Count V). In addition, Plaintiffs allege a new cause of action under Section 12(a)(2) of the 1933 Act (Count IV) against JPMSI. Against the original defendant, J.P. Morgan Chase & Co., Plaintiffs add control person claims under Section 20(a) (Count I) and Section 15 (Count IV).

I. Plaintiffs' Federal Claims Against JPMSI And JPMCB, And The Control Person Claims Against JPMC, Are Time Barred

The federal claims asserted against JPMSI (Counts I and IV) and JPMCB (Count I), as well as the associated control person claims against JPMC, are time-barred.[2] The statutes of limitation applicable to the Section 10(b) and Section 12(a)(2) claims ran *one year* after Plaintiffs discovered, or should have discovered through reasonable diligence, the factual allegations underlying the claims. Plaintiffs were on notice of the allegations against JPMSI and JPMCB by the end of 2001. Thus, Plaintiffs' attempt to add JPMSI and JPMCB as defendants, nearly 18 months later, on May 14, 2003, is time-barred.

The expanded limitations period of the Sarbanes-Oxley Act, by its own terms, does not apply here. Plaintiffs' amendments also do not "relate back" to the filing date of the original Complaint. Plaintiffs' failure to sue JPMSI and JPMCB before May 14, 2003 was not a "mistake" under Federal Rule 15(c)(3). And Plaintiffs' Section 12(a)(2) claim does not arise out of the same "conduct, transaction, or occurrence" in the original Complaint under Rule 15(c)(2).

A. Plaintiffs Discovered Or Should Have Discovered The Allegations Underlying Their Amendments More Than One Year Before The Amended Complaint

For proceedings, like this action, commenced prior to July 30, 2002,[3] Section 10(b) and Rule 10b-5 claims are time-barred one year after the plaintiff discovered, or in the exercise of reasonable diligence should have discovered, the alleged facts constituting the

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2 The limitations period for Plaintiffs' Section 20(a) control person claim against JPMC is the same as the limitations period for Plaintiffs' Section 10(b) claims against JPMSI and JPMCB. *Theoharous v. Fong*, 256 F.3d 1219, 1228 n.12 (11th Cir. 2001). Likewise, Plaintiffs' Section 15 control person claim has the same limitations period as Plaintiffs' Section 12(a)(2) claim against JPMSI. *Herm v. Stafford*, 663 F.2d 669, 679 (6th Cir. 1981).

3 This action was commenced on October 22, 2001.

violation and three years after such violation.[4] *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gibertson*, 501 U.S. 350, 364 (1991); *Reed*, 875 F. Supp. at 1288.[5] Similarly, Plaintiffs' claims under Section 12(a)(2) are governed by Section 13 of the 1933 Act, which provides that "[n]o action shall be maintained to enforce any liability created under section [12(a)(2)] unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence." 15 U.S.C. § 77m.[6]

Under both of these statutes of limitation, the clock begins to run when the plaintiff is on "inquiry notice" of the claims. "Inquiry notice is the term used for knowledge of facts that would lead a reasonable person to *begin investigating* the possibility that his legal rights had been infringed." *Kauthar*, 149 F.3d at 670 (internal citations and quotations omitted)

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4 Notwithstanding Plaintiffs' assertion that actual discovery is required to start the clock running, Opp. at 14, every circuit court to consider the issue has concluded that "inquiry notice" or "constructive discovery" is sufficient. *See New England Health Care Employees Pension Fund v. Ernst & Young, LLP*, No. 01-6523, 2003 WL 21540666, at *4 (6th Cir. July 9, 2003); *LC Capital Partners v. Frontier Ins. Group,* 318 F.3d 148, 154 (2d Cir. 2003); *In re NAHC, Inc. Sec. Litig.,* 306 F.3d 1314, 1325 (3d Cir. 2002); *Young v. Lepone,* 305 F.3d 1, 8 (1st Cir. 2002); *Theoharous,* 256 F.3d at 1228; *Sterlin v. Biomune Sys.,* 154 F.3d 1191, 1201 (10th Cir. 1998); *Kauthar SDN BHD v. Sternberg,* 149 F.3d 659, 670-71 (7th Cir. 1998), *cert. denied,* 525 U.S. 1114 (1999); *Howard v. Haddad,* 962 F.2d 328, 330 (4th Cir. 1992). The Fifth Circuit likewise affirmed a dismissal of Section 10(b) claims on the basis that plaintiff was on inquiry notice over one year before the action was commenced. *Reed v. Prudential Sec., Inc.*, 87 F.3d 1311 (5th Cir. 1996) (mem.), *aff'g*, 875 F. Supp. 1285, 1289-90 (S.D. Tex. 1995).

5 Plaintiffs attempt to distinguish *Reed* on the basis that it relied on "inquiry notice" cases decided before *Lampf.* Opp. at 14 n.7. Moreover, Plaintiffs contend that *Reed* is not controlling "because it does not address *Lampf.*" *Id.* These assertions are wrong. The *Reed* court plainly states: "It is not necessary for the plaintiff to have actual knowledge of fraud for the limitations period to begin to run. *Lampf, Pleva, Lipkind, Prupis & Petigrow,* 501 U.S. at 363, 111 S. Ct. at 2782." *Reed*, 875 F. Supp. at 1288.

6 There can be no dispute that inquiry notice is sufficient with respect to Plaintiffs' Section 12(a)(2) claim because Section 13 explicitly states that the limitations period runs one year after "discovery should have been made by the exercise of reasonable diligence." 15 U.S.C. § 77m.

(emphasis added). "[I]nquiry notice is triggered by evidence of *the possibility of fraud, not by complete exposure of the alleged scam.*" *Martinez Tapia v. Chase Manhattan Bank, N.A.*, 149, F.3d 404, 410 (5th Cir. 1998) (quoting *Brumbaugh v. Princeton Partners*, 985 F.2d 157, 162 (4th Cir. 1993))(emphasis added). "[T]he clock begins to tick when a plaintiff senses 'storm warnings,' not when he hears thunder and sees lightning." *Jensen v. Snellings*, 636 F. Supp. 1305, 1309 (E.D. La. 1986) (citation omitted), *aff'd in part and rev'd in part on other grounds*, 841 F.2d 600 (5th Cir. 1988). Moreover, following such "storm warnings," a plaintiff "must proceed with a reasonable and diligent investigation, and is charged with the knowledge of all facts such an investigation would have disclosed." *Jensen*, 841 F.2d at 607.

Here, the "storm warnings" began at least by October 16, 2001 when Enron issued its first financial restatement, Am. Compl. ¶ 61, and thus Plaintiffs are charged with knowledge of all facts that a reasonable investigation would have disclosed thereafter. *Jensen*, 841 F.2d at 607. Plaintiffs argue that Enron's "initial revelations" in the Fall of 2001 did not provide notice to Plaintiffs of the bank defendants' conduct. Opp. at 15. To the contrary, as discussed below, Plaintiffs knew the identities of JPMSI and JPMCB, in connection with the matters alleged in the Amended Complaint, for more than a year before they filed the Amended Complaint.

With respect to the Mahonia prepay transactions, Plaintiffs were on notice of JPMCB's alleged conduct no later than December 22, 2001. On that date, it was publicly reported that certain defendants in the action styled *JPMorgan Chase Bank v. Liberty Mutual Insurance Co.*, No. 01 Civ. 11523 (S.D.N.Y.) (the "Surety Action"), filed a counterclaim against JPMCB alleging that "forward sales contracts were 'materially false,'" and "that the contracts were actually intended 'to provide a mechanism to obtain surety bonds to secure loans made by

Mahonia to Enron in the guise of forward supply contracts.'" Andrew Hill, *Insurer Claims Enron Contracts Were A Front*, FIN. TIMES, Dec. 22, 2001.[7] Indeed, the substance of Plaintiffs' allegations here concerning the Mahonia prepays was expressly set forth against JPMCB in the Surety Action filings in December 2001: "[T]he contracts were not intended by the parties [including JPMCB] to be fulfilled as actual supply contracts but, instead, were intended to provide a mechanism to obtain surety bonds to secure loans . . . in the guise of forward supply contracts." Appendix, Exhibit 1 (Answer, Affirmative Defenses and Counterclaim of St. Paul Fire & Marine Ins. Co. of 12/19/01, at 9);[8] *cf.* Am. Compl. ¶ 664 ("These transactions were, in reality, disguised loans from JP Morgan to Enron . . . .").

With respect to the securities issued by Marlin Water Trust II and Marlin Water Capital Corp. II (the "Marlin II Notes"), Plaintiffs were on notice of JPMSI's alleged conduct as early as October 29, 2001. On that date, it was reported that "Enron called a conference call Tuesday to clear the air, but it ended up compounding its problems by failing to answer questions posed by a Boston investor about the Marlin partnership, leaving Wall Street with the clear impression that the company faces a nearly $1 billion loss on that deal." Andrew Barry, *Bulls Look to Recovery, as Techs Lead the Surge*, BARRONS, Oct. 29, 2001. On November 5, 2001, *Barron's* further reported on Marlin, observing that "[t]here's concern in the debt market that *Marlin bondholders may suffer if Enron ends up in bankruptcy*." Andrew Barry, *Addition by Subtraction: Bond's End Boosts Stocks*, BARRONS, Nov. 5, 2001 (emphasis added).

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7 The Court is entitled to consider on this motion to dismiss "information that was publicly available to reasonable investors," including news articles. *Phillips v. LCI Int'l, Inc.*, 190 F.3d 609, 617 (4th Cir. 1999); *In re Guess?, Inc. Sec. Litig.*, 174 F. Supp. 2d 1067, 1068 (C.D. Cal. 2001).

8 The Court may take judicial notice of the counterclaim in the Surety Action because it is a public record. *Jefferson v. Lead Indus. Ass'n Inc.*, 106 F.3d 1245, 1259 n.14 (5th Cir.

Furthermore, on November 15, 2001, the *Houston Chronicle* reported Enron's own assessment that it "made some very bad investments" in certain businesses, including Wessex Water, the principal asset underlying the Marlin II Notes. Tom Fowler, *Enron Plans Asset Sell-Off To Slash Debt*, HOUSTON CHRON., Nov. 15, 2001, at 1. And Enron's bankruptcy filing on December 2, 2001 unquestionably put purchasers of Marlin II Notes on inquiry notice of the facts underlying their claims concerning alleged misleading statements in the Offering Memoranda, which listed JPMSI, specifically, as an initial purchaser of Marlin II Notes.[9]

With respect to the analyst reports, Plaintiffs were on notice in the Fall of 2001 of their alleged misleading nature from Enron's financial restatements, the SEC's investigation of Enron and Enron's bankruptcy filing – all independently sufficient "storm warnings" as a matter of law. Moreover, that these Chase analyst reports bore JPMSI's name put Plaintiffs on actual notice that JPMSI, and not any other JPMorgan Chase entity, issued them.

Finally, with respect to LJM2, the Amended Complaint contains no allegation that either JPMSI or JPMCB, specifically, were at all involved as investors in that partnership. *See, e.g.,* Am. Compl. ¶ 461 ("Thus, JP Morgan [and others] were early investors in LJM2").

While the foregoing demonstrates Plaintiffs had plenty of inquiry notice for more than a year before filing the Amended Complaint, Plaintiffs also had actual knowledge that JPMSI, JPMCB, or other subsidiaries or affiliates of JPMC – but not JPMC itself – were the entities involved with the Enron-related activities alleged in the Amended Complaint. On May 8, 2002, JPMC filed its motion to dismiss Plaintiffs' original Complaint, in which JPMC

1997).

9 Similarly, Plaintiffs were on inquiry notice, upon Enron's bankruptcy, of their claims arising out of alleged misstatements in the offering documents for Enron's February 1999 common stock offering and the July 2001 resale of Enron zero coupon convertible notes, Am. Compl. ¶ 662, which offering documents listed JPMSI as an underwriter.

affirmatively stated that that JPMSI is the "entity that issued the analyst research notes" and that JPMCB's predecessor, The Chase Manhattan Bank, was "the entity that engaged in almost every other Enron-related activity that the Complaint ascribes to defendant JPMorgan Chase." Motion to Dismiss of J.P. Morgan Chase & Co., of 5/8/02, at 6 n.2.[10]

In sum, Plaintiffs were on inquiry notice of their claims against JPMSI and JPMCB before the end of 2001 and actual notice, at the latest, on May 8, 2002. In either case, the applicable statutes of limitations ran before May 14, 2003 and, thus, Plaintiffs' federal claims against JPMSI and JPMCB, and the associated control person claims against JPMC, are time-barred.

B. The Sarbanes-Oxley Act Does Not Save Plaintiffs' Time-Barred Claims

Plaintiffs argue that none of their new claims is time-barred because they are governed by the two-year/five-year limitations period established by the Sarbanes-Oxley Act. Plaintiffs are incorrect for two reasons. First, the Sarbanes-Oxley Act's amended limitations period applies only to "proceedings commenced on or after July 30, 2002." Indeed, because this action was commenced on October 22, 2001, *this Court has already held that the Sarbanes-Oxley Act does not apply to this proceeding. In re Enron Corp. Sec., Derivative & ERISA Litig.*, 258 F. Supp. 2d 576, 601 n.20 (S.D. Tex. 2003). Second, the Sarbanes-Oxley Act did not repeal

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[10] The JPMorgan Chase Entities are not "estopped" from asserting a statute of limitations defense for claims brought after January 27, 2003. Opp. at 15. The suggestion that Plaintiffs' claims against JPMSI and JPMCB were tolled on January 27, 2003 presumes that their claims had not already expired. However, all Plaintiffs' federal claims against JPMSI and JPMCB were already time-barred because Plaintiffs were on *inquiry* notice of their claims by the end of 2001. Notwithstanding, Plaintiffs cannot claim any estoppel reliance on the January 27, 2003 order (which directed the bank defendants to file appropriate motions if they object to being named defendants because a subsidiary is the real party in interest) because JPMC had put Plaintiffs on *actual* notice of JPMSI's and JPMCB's involvement in the alleged actionable conduct *on May 8, 2002*, when JPMC filed its motion to dismiss the original Complaint.

Section 13 of the 1933 Act, which provides an express one-year/three-year statute of limitations for Plaintiffs' Section 12(a)(2) claims (as well as the Section 15 control person claim).

1. Plaintiffs' Amended Complaint is not a "proceeding" commenced after July 30, 2002

Plaintiffs call the Amended Complaint, filed on May 14, 2003, a new "proceeding" that was commenced after July 30, 2002, and thus subject to the amended limitations period of the Sarbanes-Oxley Act. Opp. at 8. To the contrary, a civil action is a single proceeding that is commenced when the plaintiff first files its original complaint. *See* FED. R. CIV. P. 3. "After the original filing, the suit is considered to be pending. Thus the amendment of the . . . complaint . . . does not constitute a new filing of the case." *Ameriwood Indus. Int'l Co. v. American Cas. Co.*, 840 F. Supp. 1143, 1152 (W.D. Mich. 1993) (citing Wright & Miller, *Federal Practice & Procedure* § 1052 (1992 and 1993 Supp.)); *cf. National Union Fire Ins. Co. v. Willis*, 296 F.3d 336, 342 (5th Cir. 2002) (observing that, if an amended complaint is considered to commence a proceeding, it would irreconcilably result in "one lawsuit qualifying as two different civil proceedings."). Because the Amended Complaint did not commence a "proceeding" after July 30, 2002, the Sarbanes-Oxley Act's statute of limitations does not apply to any of Plaintiffs' new claims and the new defendants named therein. *In re Mirant Corp. Sec. Litig.*, CA No. 1:02-CV-1467-BBM, slip. op. at 12 n.4 (N.D. Ga. July 14, 2003) (declining to apply the Sarbanes-Oxley Act to claims added by an amendment filed on November 25, 2002). Appendix, Exhibit 2.[11]

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[11] Plaintiffs rely on *Friedman v. Rayovac Corp.*, No. 02-C-308-C, slip op. (E.D. Wis. June 23, 2003), in which the court concluded that "serving an additional party commences a new 'proceeding,'" *Id.* at 23. That decision is contrary to the clear language of Federal Rule of Civil Procedure 3 as well as the Fifth Circuit precedent cited above.

2. The Sarbanes-Oxley Act's amended limitations period does not apply to Plaintiffs' Sections 12(a)(2) and 15 claims

Even if the Court were to apply the Sarbanes-Oxley Act's limitations period here, it nevertheless does not apply to Plaintiffs' Sections 12(a)(2) and 15 claims, which are subject to the express statute of limitations found in Section 13. *In re Merrill Lynch & Co., Inc. Research Reports Sec. Litig.*, No. 02 MDL 1483, 2003 WL 21518833, at *19 (S.D.N.Y. July 2, 2003) (in a case filed on October 1, 2002, applying the Sarbanes-Oxley Act to plaintiff's Section 10(b) claim and applying Section 13 to plaintiff's Section 12(a)(2) claim).

Section 804(b) of the Sarbanes-Oxley Act (codified at 28 U.S.C. § 1658(b)) provides that the new statute of limitations applies to "a private right of action *that involves a claim of fraud, deceit, manipulation, or contrivance* in contravention of a regulatory requirement concerning the securities laws, as defined in section 3(a)(47) of the Securities Exchange Act of 1934." 28 U.S.C. § 1658(b) (emphasis added). Notwithstanding the language highlighted above, Plaintiffs assert that the Sarbanes-Oxley Act's statute of limitations is not limited to fraud claims because the term "securities laws" includes the 1933 Act. Opp. at 6. Plaintiffs' skewed reading ignores that the Sarbanes-Oxley Act's limitations period does not apply to *all* securities laws; rather, it applies only to securities laws "that involve[] a claim of fraud, deceit, manipulation, or contrivance."[12] Because Section 12(a)(2) does not require proof of fraud, its express statute of limitations found in Section 13 is not displaced by the Sarbanes-Oxley Act. *See Gustafson v. Alloyd Co.*, 513 U.S. 561, 580 (1995); Am. Compl. ¶ 1016.3 ("Plaintiffs assert

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[12] Moreover, Plaintiffs' reliance on *In re Gibbons*, 289 B.R. 588, 592 (Bankr. S.D.N.Y. 2003) is misplaced. *Gibbons* addresses Section 803, not Section 804, and while Section 803 states that it is applicable to "violations of any of the Federal securities laws," Section 804 applies to only "claim[s] of fraud, deceit, manipulation, or contrivance in contravention of a regulatory requirement concerning the securities laws, as defined in section 3(a)(47)."

negligence claims" in the Section 12(a)(2) cause of action).[13]

Furthermore, if Congress wanted to repeal or amend Section 13 of the 1933 Act, it certainly knew how to do it explicitly.[14] In the Sarbanes-Oxley Act, Congress amended 28 U.S.C. § 1658, which, pre-amendment, provided a general statute of limitations for all federal causes of action that are *not* subject to an express statute of limitations. Of course, prior to the Sarbanes-Oxley Act, private fraud-based claims asserted under Section 10(b) were subject only to the judicially-created statute of limitations set forth by the *Lampf* Court, not an express statute. Accordingly, seeking to establish a new express statute of limitations for such fraud-based claims, Congress revised Section 1658. It did not revise Section 13 of the 1933 Act which was, and continues to be, the applicable statute of limitations for causes of action asserted under Section 12(a)(2).

C. Plaintiffs' New Claims And Addition Of New Parties Do Not Relate Back Under Rule 15(c)

Because the Amended Complaint was filed more than a year after the limitations periods ran on Plaintiffs' federal claims against JPMSI and JPMCB (and the control person claims against JPMC), Plaintiffs contend that the Amended Complaint "relates back" to the original Complaint under Rule 15(c). Rule 15(c)(3) sets forth the requirements that a plaintiff must demonstrate before a *new party* relates back to the original pleading, including that the new

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13 Plaintiffs speak out of both sides of their mouths when they insist that scienter is not a necessary element of their Section 12(a)(2) claim and at the same time that the Sarbanes-Oxley Act, which by its terms applies only to fraud-based claims, should apply to their Section 12(a)(2) claim.

14 Despite Plaintiffs' attempted recourse to the Sarbanes-Oxley Act's legislative history, Opp. at 10-12, the Court's inquiry should end with its reading of the statute. *Connecticut Nat. Bank v. Germain*, 503 U.S. 249, 254 (1992) ("When the words of a statute are unambiguous ... judicial inquiry is complete") (internal quotations omitted); *Thompson v. Goetzmann*, No. 02-10198, 2003 WL 21523349, at *4 (5th Cir. July 7, 2003).

party "knew or should have known that, but for a mistake concerning the identity of the proper party, the action would have been brought against" that new party. FED. R. CIV P. 15(c)(3).[15] Rule 15(c)(2) provides that a *new claim* relates back to an earlier pleading only when the newly-asserted claim "arose out of the conduct, transaction, or occurrence set forth or attempted to be set forth in the original pleading." FED. R. CIV. P.15(c)(2).

1. Plaintiffs fail to meet the requirements set forth in Rule 15(c)(3)

As Rule 15(c)(3) clearly states, Plaintiffs must allege that they made a mistake as to the identity of the proper party, and that JPMSI and JPMCB knew or should have known that but for Plaintiffs' mistake, they would have been added previously.[16] FED. R. CIV. P.15(c)(3). Plaintiffs have not met either requirement.

a. Plaintiffs do not adequately allege a mistake of law

Plaintiffs do not even attempt to argue that they made a factual mistake as to the identities of JPMSI and JPMCB when filing the original Complaint.[17] Rather, Plaintiffs contend that JPMSI and JPMCB were added as Section 10(b) defendants to correct a potential mistake in

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15 The JPMorgan Chase Entities did not argue as a basis for dismissal that they lacked notice of this litigation. Accordingly, Plaintiffs' lengthy argument on this point, Opp. at 19-24, is not responsive to the JPMorgan Chase Entities' motion to dismiss.

16 Plaintiffs bear the burden of satisfying the requirements for relation back under Rule 15(c). *Hazelton v. City of Grand Prairie, Tex.*, 8 F. Supp. 2d 570, 580-81 (N.D. Tex. 1998). Thus, Plaintiffs' suggestion that the bank defendants identify a rational strategy for why Plaintiffs heretofore omitted various subsidiaries is wrong.

17 Indeed, Plaintiffs made reference in the original Complaint to both JPMSI and JPMCB. Plaintiffs explicitly identified JPMSI as an affiliate of JPMC, Original Compl. ¶ 100, and repeatedly referenced JPMSI analyst reports, *see, e.g., id.* ¶¶ 153, 190, 376, 380, which identify themselves as publications of "J.P. Morgan Securities Inc." Moreover, Plaintiffs explicitly cited a decision by Judge Rakoff in the Surety Action, which case was captioned *JPMorgan Chase Bank v. Liberty Mut. Ins. Co. Id.* ¶ 665. Accordingly, Plaintiffs' failure to name JPMSI and JPMCB as defendants in the original Complaint, or otherwise add them to the lawsuit within the applicable limitations periods, was not the product of a "mistake" as to their identities. *See Jacobsen v. Osborne*, 133 F.3d 315, 321

law "concerning corporate 'separateness.'" The 1966 Advisory Committee Notes to Rule 15(c) state that the mistake of law doctrine is meant to apply where plaintiffs would have their claims dismissed because they mistakenly named institutional rather than individual defendants.[18] Accordingly, most courts that have relied on a "mistake of law" to permit plaintiffs to change defendants have done so in the narrow situations contemplated by the Advisory Committee Notes. *See, e.g., Soto v. Brooklyn Correctional Facility*, 80 F.3d 34, 37 (2d Cir. 1996) (allowing addition of individual corrections officers as defendants where plaintiff had previously named only correctional facility); *Woods v. Indiana University—Purdue University at Indianapolis,* 996 F.2d 880, 887 (7th Cir. 1993) (finding that plaintiff made a mistake of law in pursuing "state agencies rather than individual state actors as defendants"); *Kirk v. Cronvich*, 629 F.2d 404, 408 (5th Cir. 1980) (allowing addition of individual sheriff as defendant where plaintiff had previously named Parish and sheriff's office), *overruled on other grounds by Schiavone v. Fortune*, 477 U.S. 21 (1986).[19]

(5th Cir. 1998); *Cornwell v. Robinson*, 23 F.3d 694, 705 (2d Cir. 1994).

18 The Advisory Committee Notes clearly indicate the intent of the doctrine:

> The problem has arisen most acutely in certain actions by private parties against officers or agencies of the United States. Thus an individual denied social security benefits by the Secretary of Health, Education, and Welfare may secure review of the decision by bring a civil action against that officer within sixty days. In several recent cases the claimants instituted timely action but mistakenly named as defendant the United States, the Department of HEW, the 'Federal Security Administration' (a nonexistent entity), and a Secretary who had retired from the office nineteen days before.

FED. R. CIV. P. 15 Advisory Committee Notes 1966 Amendment.

19 Plaintiffs rely on two unpublished decisions in asserting that the mistake of law doctrine applies here. *Simpson v. Borg-Warner Automotive, Inc.*, No. 97 C 1911, 1997 US Dist. LEXIS 19502 (N.D. Ill. Dec. 4, 1997) addressed a situation where a plaintiff sought to

Plaintiffs here, having made no such error, are not entitled to rely on the "mistake of law" doctrine to add JPMSI and JPMC as Section 10(b) defendants. *Dalicandro v. Legalgard, Inc.*, No. CIV.A. 99-3778, 2003 WL 182942, at *7 (E.D. Pa. Jan. 23, 2003) (refusing to allow relation back where "no error of law comparable to those mentioned in the Advisory Committee Notes occurred"); *In re Brand Name Prescription Drugs Antitrust Litig.*, No. 94 C 987, MDL 997, 1998 WL 474146, at *5 (N.D. Ill. Aug. 6, 1998) (holding that mistake of law doctrine is limited to "plaintiffs misconception as whether to sue an individual or institutional government defendant," and does not apply to a "miscalculation [plaintiffs] may have made" with regard to the applicability of precedent to their claims). The Eleventh Circuit's decision in *Powers v. Graff*, 148 F.3d 1223 (11th Cir. 1998) is also instructive. There, plaintiffs sought to amend their Section 10(b) claim by adding the control persons of the brokerage company originally named as a defendant. The court declined to allow the amendment, finding the mistake of law doctrine inapplicable:

> Not only did Plaintiffs know the identity of Defendants before expiration of the limitations period ... Plaintiffs also should have known that Defendants would be proper parties to the suit, that is, persons arguably liable for the alleged wrongdoing. To know that Defendants may be have been liable for the wrongdoing, Plaintiffs need only have known that Defendants were, in fact, control persons of [the original Defendant].

Id. at 1227. Similarly, Plaintiffs here knew that JPMSI and JPMCB are subsidiaries of JPMC that engaged in transactions with Enron. As such, Plaintiffs' failure to add them previously precludes the application of the relation back doctrine.

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substitute one defendant for another, not add additional defendants as here. *Id.* at *4-*5. And *Gaspard v. Highlands Ins. Co., et al.*, No. 89-3385, 1991 U.S. Dist. LEXIS 3010 (E.D. La. Mar. 12, 1991) is inapposite as that court allowed an additional defendant to be added in the event that the court was in error about the proper parties to be sued. *Id.* at *4.

b. JPMSI and JPMCB had no reason to believe their omission from the original Complaint was a "mistake"

Even if the Court were to find that Plaintiffs failed to name JPMSI and JPMCB due to a mistake, Plaintiffs must also demonstrate that JPMSI and JPMCB "knew or should have known that," but for the mistake they would have been named earlier. FED. R. CIV. P. 15(c)(3). When, as here, a plaintiff does not substitute an originally named party for the new parties, but rather considers both the original and the new parties as proper, the new parties could not have known they were previously omitted due to a mistake. *Kemp Indus. v. Safety Light Corp.*, No. Civ. A. 92-95, 1994 WL 532130, at *13 (D.N.J. Jan. 25, 1994) ("If the party originally named in the complaint was not mistakenly named, and was in fact a proper party, the unnamed defendant will have reason to believe it was not omitted by mistake, but by strategy."). Because Plaintiffs have retained JPMC as a party to this action, JPMSI and JPMCB had no reason believe that their omission until now was a mistake. *See Cornwell*, 23 F.3d at 705 ("The requirement that a new defendant 'knew' he was not named due to a mistake concerning identity presupposes that in fact the reason for his not being named was a mistake in identity").

2. Plaintiffs fail to meet the requirements of Rule 15(c)(2)

Rule 15(c)(2) provides a single requirement for the relation back of new claims: it must be based on the same transaction or occurrence as set forth in the original complaint. FED. R. CIV. P.15(c)(3). However, Plaintiffs' Section 12(a)(2) claim against JPMSI alleges misstatements not asserted in the original Complaint.

a. Plaintiffs' Section 12(a)(2) claim against JPMSI is not based on the same transaction or occurrence alleged in the original Complaint

Plaintiffs' only new legal theory against any of the JPMorgan Chase Entities is a Section 12(a)(2) claim brought against JPMSI, alleging misstatements made in connection with

the Marlin II Notes.[20] Plaintiffs knew about and referenced the Marlin II Notes offering in the original Complaint, Compl. ¶ 49, but chose not to allege *any missatements* with respect to such offering until May 14, 2003. These later-alleged misstatements do not arise out of the same "conduct, transaction, or occurrence" alleged in the original Complaint, and thus, do not relate back to the original filing date. *In re Bausch & Lomb, Inc. Sec. Litig.*, 941 F. Supp. 1352, 1366 (W.D.N.Y. 1996) (because each alleged misstatement is a separate cause of action, pleadings asserting newly added misstatements do not relate back, even when the "prior pleadings did put defendants on notice that plaintiffs' claims against them arose out of the same general scheme to defraud"); *see also Hunt v. Am. Bank & Trust Co.*, 783 F.2d 1011, 1013-14 (11th Cir. 1986) (holding that new claims do not relate back when they "concern a separate incident of fraud").

II. Plaintiffs' Section 12 Claim Against JPMSI Fails

In the Amended Complaint, Plaintiffs have added a new cause of action (Count IV) directed at JPMSI pursuant to Section 12(a)(2) of the 1933 Act. Am. Compl. ¶¶ 1016.1-1016.9. The Section 12(a)(2) claim arises out of JPMSI's alleged participation in the offering of the Marlin II Notes, one of the so-called "Foreign Debt Securities" described in the Amended Complaint. *Id.* ¶ 1016.4. This claim (and, necessarily, the Section 15 control person claim against JPMC) must be dismissed because no named Plaintiff purchased any Marlin II Notes. Plaintiffs simply do not have standing to bring the Section 12(a)(2) claim against JPMSI. Plaintiffs also fail to allege several key elements of a Section 12(a)(2) claim; namely, that JPMSI was a "seller" of the Marlin II Notes to Plaintiffs within the meaning of Section 12(a)(2) and that Plaintiffs purchased the Marlin II Notes in an initial public offering.

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[20] In connection with this new claim, Plaintiffs also add a control person claim against JPMC pursuant to Section 15, which claim must necessarily be dismissed upon failure to state a claim against JPMSI under Section 12(a)(2).

A. Plaintiffs Admit They Lack Standing To Pursue Their Section 12(a)(2) Claim

In their Opposition, Plaintiffs are forced to admit that there is no factual basis for the Amended Complaint's allegation that "plaintiffs sustained substantial damages in connection with their purchases of the [Marlin II Notes]." *Id.* ¶ 1016.9. Plaintiffs concede that no named Plaintiff, in fact, purchased any of the Marlin II Notes, Opp. at 47, and, thus, no Plaintiff suffered any damages as a result of such non-existent purchases. Plaintiffs, having suffered no injury-in-fact, lack standing to assert a Section 12(a)(2) claim relating to the Marlin II Notes.[21] *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560 (1992) (plurality opinion). Since no named Plaintiff purchased any Marlin II Notes, Plaintiffs likewise fail meet the additional requirements that the plaintiff purchase the security directly from the defendant in an initial public offering. *Gustafson*, 513 U.S. at 571; *Rosenzweig v. Azurix Corp.*, 335 F.3d 854, 871-72 (5th Cir. 2003); *see also* Point II.B, *infra*.

Plaintiffs do not dispute their lack of standing. Opp. at 47. Rather, they improperly suggest that the Court defer ruling on the issue until it considers Plaintiffs' pending motion for class certification. *Id.* That would just delay the inevitable, however, because Plaintiffs cannot, as a matter of law, represent a class in which they do not belong. *Lewis v. Casey*, 518 U.S. 343, 357 (1996) (explaining that "even named plaintiffs who represent a class must allege and show that they personally have been injured, not that injury has been suffered by other, unidentified members of the class to which they belong and which they purport to represent") (internal quotations omitted); *In re Taxable Mun. Bond Sec. Litig.*, 51 F.3d 518, 522

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[21] Plaintiffs also assert, Opp. at 46 n.38, that they may represent a class of purchasers of Foreign Debt Securities for purposes of pursuing Section 10(b) and Rule 10b-5 claims. But the cases they cite do not apply where, as here, plaintiffs seek to represent purchasers of securities of a *different issuer*. Whether purchasers of one type of security may in some circumstances represent a class including purchasers of the other securities of the

(5th Cir. 1995) ("It is well-established that to have standing to sue as a class representative it is essential that a plaintiff must be part of that class . . . .") (internal quotations and alterations omitted); *see also Franze v. Equitable Assurance*, 296 F.3d 1250, 1254 (11th Cir. 2002) (holding that a plaintiff lacking standing cannot satisfy the prerequisites for class representation under Rule 23(a)).[22] Moreover, Plaintiffs' amended motion for class certification does not include any purchasers of Marlin II Notes. Opp. at 47 n.39. And, contrary to Plaintiffs' suggestion, it "makes logical sense" to decide this motion to dismiss for lack of standing before the class certification motion, which will be rendered moot upon a determination that Plaintiffs lack standing. *King v. Douglass*, 973 F. Supp. 707, 712 (S.D. Tex. 1996).

Plaintiffs' indication that they may have found a purchaser of Marlin II Notes to intervene cannot save their Section 12(a)(2) claim. Opp. at 47. Standing, like other bases for jurisdiction, must be present at the inception of the lawsuit. *Lujan*, 504 U.S. at 570 n.5 ("[S]tanding is to be determined as of the commencement of suit."); *Goldin v. Bartholow*, 166 F.3d 710, 717 (5th Cir. 1999) (explaining that "standing" is the "requisite personal interest that must exist at the commencement of the litigation.") (internal quotations omitted). In addition to the foregoing, Plaintiffs' suggestion that non-party Imperial County Board of Retirement ("Imperial") may seek to intervene is an unverified statement of counsel that has no bearing on this motion to dismiss. Opp. at 47. There is no submission in record from Imperial; the

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same issuer is irrelevant.

22 *Longden v. Sunderman*, 123 F.R.D. 547 (N.D. Tex. 1988), *superseded by Castano v. American Tobacco Co.*, 84 F.3d 734 (5th Cir. 1996), is not to the contrary. The *Longden* court specifically limited its ruling to class certification. *Longden,* 123 F.R.D. at 551 (stating that the court's inquiry "does not extend to whether plaintiff class representatives have successfully stated a cause of action or will prevail on the merits"). Moreover, unlike the named plaintiffs in *Longden*, who had invested in at least some of the limited partnerships at issue, *Longden*, 123 F.R.D. at 550, Plaintiffs have conceded that no named Plaintiff purchased any Marlin II Notes. Opp. at 47.

Amended Complaint contains no allegations that Imperial bought Marlin II Notes, much less that it bought Marlin II Notes from JPMSI. Indeed, there is no suggestion in the Amended Complaint or Plaintiffs' Opposition that Imperial had any dealings whatsoever with JPMSI. Consequently, Plaintiffs' proposed *ex post facto* intervenor scheme cannot create standing here. Plaintiffs' Section 12(a)(2) claim must be dismissed against JPMSI.[23]

B. Plaintiffs Cannot Allege That JPMSI Was A "Seller" Under Section 12

Although Plaintiffs concede that JPMSI did not, in fact, sell them any Marlin II Notes, the Amended Complaint nevertheless alleges that the bank defendants "sold" the Foreign Debt Securities, including Marlin II Notes, to Plaintiffs or class members and that Plaintiffs or class members "purchased" the Foreign Debt Securities from the bank defendants. Am. Compl. ¶¶ 1016.4-1016.5; Opp. at 39. Plaintiffs argue that this allegation constructively "charges" JPMSI with having "passed title" of Marlin II Notes to Plaintiffs or class members. Opp. at 39.[24] However, the Amended Complaint does not contain any allegation that JPMSI "passed title" of

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[23] Because Plaintiffs did not, in fact, purchase any Marlin II Notes from JPMSI, the Amended Complaint's vague, conclusory allegations on that subject cannot prevent dismissal of the Section 12(a)(2) claim. *Associated Builders, Inc. v. Alabama Power Co.*, 505 F.2d 97, 99 (5th Cir. 1974) ("A (complaint) may be dismissed on motion if clearly without any merit; and this want of merit may consist . . . in the disclosure of some fact which will necessarily defeat the claim.") (internal quotations and citations omitted); *James v. Alcoa, Inc.*, No. 02-50097, 2003 WL 21692685, at *2 & nn.4-5 (5th Cir. July 21, 2003) (a court should reject "conclusory allegations concerning the legal effect of the events plaintiff has set out if these allegations do not reasonably follow from his description of what happened") (citation omitted). Plaintiffs also cannot rely on purported sales of Marlin II Notes to absent proposed class members since Plaintiffs themselves did not purchase the Marlin II Notes. *See Lewis*, 518 U.S. at 357. *Dicta* in *Moskowitz v. Mitcham Indus.*, No. H-98-1244, 2000 U.S. Dist. LEXIS 22424 (S.D. Tex. Oct. 2, 2000), suggesting otherwise is contrary to established Fifth Circuit law. *See In re Taxable Mun. Bond Sec. Litig.*, 51 F.3d at 522.

[24] Plaintiffs concede that that JPMSI is not alleged to be a seller under Section 12(a)(2) by virtue of having "solicited" a purchase of Marlin II Notes from Plaintiffs or class members. Opp. at 39; *see Cyrak v. Lemon*, 919 F.2d 320, 324-25 (5th Cir. 1990).

Marlin II Notes to Plaintiffs. *See Griffin v. PaineWebber, Inc.*, 84 F. Supp. 2d 508, 515 (S.D.N.Y. 2000) ("Unfortunately for Plaintiff, several of these allegations do not appear in the Complaint. That they appear in Plaintiff's memorandum of law in opposition to these motions to dismiss does not cure the defect.").[25] More importantly, Plaintiffs' wholly conclusory allegation that JPMSI "sold" Marlin II Notes is insufficient, as a matter of law, to plead that JPMSI passed title to those securities. *Pinter v. Dahl*, 486 U.S. 622, 642-43 (1988) ("In common parlance, a person may offer or sell property without necessarily being the person who transfers title to, or other interest in, that property.")[26]

C. Plaintiffs Admit That They Did Not Purchase Marlin II Notes "By Means Of A Prospectus"

Plaintiffs do not dispute that Section 12(a)(2) requires that a defendant sell securities to a plaintiff "by means of a prospectus," and agree that a security is sold "by means of a prospectus" only when it is sold in an initial public offering. Opp. at 40, 44; *Gustafson,* 513 U.S. at 571; *Lewis v. Fresne*, 252 F.3d 352, 357 (5th Cir. 2001). Accordingly, Plaintiffs concede that their Section 12(a)(2) claim can be sustained only if they purchased the Marlin II Notes in an

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25 Plaintiffs contend that their failure to allege any such sales is "'trivial' nitpicking." Opp. at 39. To the contrary, Plaintiffs' omission constitutes a fundamental failure to establish standing and to state a claim pursuant to Section 12(a)(2).

26 The Texas Securities Act claim asserted by Plaintiff Washington State Investment Board ("Washington Board") similary fails to adequately allege that any JPMorgan Chase Entity was a "seller" as required by the statute. Despite extraordinarily vague allegations of privity between unidentified parties, *see* Opp. at 100 ("all of the plaintiffs in the sub-class are in privity with *either* Lehman Brothers *or* J.P. Morgan"), the Washington Board does not allege any facts demonstrating that the JPMorgan Chase Entities were "sellers," nor do they dispute the well-established principle that underwriters are not "sellers" unless they actively participate in negotiations with the plaintiff/purchaser. *See Pinter,* 486 U.S. at 642; *Dartley v. ErgoBilt Inc.*, No. Civ. A. 398CV1442M, 2001 WL 313964, *2 (N.D. Tex. Mar. 29, 2001). The JPMorgan Chase Entities cannot be deemed "sellers" because the Washington Board has not alleged "direct contact between defendants and plaintiff-purchasers." *In re Azurix Corp. Sec. Litig.*, 198 F. Supp. 2d 862, 892 (S.D. Tex. 2002), *aff'd sub nom.*, *Rosenzweig v. Azurix Corp.*, 332 F.3d 854 (5th Cir. 2003).

initial public offering, which they did not do.

Plaintiffs' allegation that the Marlin II Notes were listed on the Luxembourg stock exchange does not help them. Am. Compl. ¶¶ 1016.4-1016.5; Opp. at 44. First, Plaintiffs concede that neither they nor any class members actually purchased Marlin II Notes on the Luxembourg exchange. Opp. at 44. Second, even if they had, such purchases would be secondary transactions not covered by Section 12(a)(2). *Gustafson*, 513 U.S. at 571; *Rosenzweig*, 332 F.3d at 871-72 (explaining that Section 12 does not reach secondary transactions). To the contrary, Plaintiffs assert that they purchased Marlin II Notes in the initial offering. Opp. at 44. By their own terms, however, the Marlin II Offering Memoranda state that the Notes are to be distributed by means of an unregistered, private offering to qualified institutional buyers – not to the public at large. *See* JPMC Opening Br. at 16. Because the Marlin II Notes private placement offering was not registered, neither Offering Memorandum is a "prospectus" within the meaning of Section 12(a)(2), as a matter of law. *Gustafson*, 513 U.S. at 569 ("[W]hatever else 'prospectus' may mean, the term is confined to a document that, absent an overriding exemption, must include the 'information contained in the registration statement.'").[27]

What Plaintiffs are trying to do is to allege that notwithstanding the fact that the Marlin II Notes were sold in an initial *private* offering, the offering should be considered public because the Notes were later traded on the Luxembourg exchange. The argument Plaintiffs make here was repudiated in *Laser Mortgage Management Inc. v. Asset Securitization Corp.*,

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[27] "[O]verriding exemption[s]" are found in Section 3 of the 1933 Act, not Rule 144A or Regulation S, upon which the Marlin II Notes offering relied. *See Gustafson*, 513 U.S. at 569 ("Save for the explicit and well-defined exemptions for securities listed under § 3 . . . its mandate is unqualified: '[A] prospectus ... shall contain the information contained in the registration statement.'").

No. 00 Civ. 8100, 2001 WL 1029407, at *8-*9 (S.D.N.Y. Sept. 6, 2001). In *Laser Mortgage*, defendants simultaneously offered two classes of certificates: one class was offered to the public by means of a prospectus and prospectus supplement, while the other class was offered privately pursuant to a Private Placement Memorandum ("PPM"), which incorporated by reference the prospectus and prospectus supplement. *Id.* at *1. Plaintiff only purchased the private certificates. *Id.* at *2. However, plaintiff argued its purchases were covered by Section 12(a)(2) because the PPM incorporated the publicly filed prospectus. The court rejected plaintiff's contention because plaintiff bought its certificates "by means of" the PPM, not "by means of the prospectus." *Id.* at *8. As a private transaction "by means of" the PPM, plaintiff's purchase was not subject to Section 12(a)(2). Likewise, regardless of whether the Marlin II Notes were later traded publicly on the Luxembourg exchange, the Amended Complaint alleges that the Marlin II Notes were initially sold "by means of" the *private* Marlin II Offering Memoranda. Their Section 12(a)(2) claim consequently must be dismissed.[28]

III. Plaintiffs Have Not Sufficiently Alleged Control Person Liability Against JPMC

A. Plaintiffs Fail To Allege A Predicate Violation

As an initial matter, Plaintiffs' control person claims against JPMC must be dismissed because the Amended Complaint fails to state primary violations against JPMSI and JPMCB. *See* Points I, II, *supra*. Despite Plaintiffs' assertions to the contrary, it is well established that Plaintiffs' failure to plead primary violations requires dismissal of the derivative control person claims. *In re Enron Corp. Sec., Derivatives & ERISA Litig.*, 235 F. Supp. 2d 549,

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[28] *Sloane Overseas Funds v. Sapiens Int'l Corp.*, 941 F. Supp. 1369 (S.D.N.Y. 1996) is inapposite because defendants did not contend, as here, "that the Note offering was private." *Id.* at 1376 n.11. In any event, the *Sloane* court's conclusion that Section 12(a)(2) reaches an offering made *without* a prospectus is inconsistent with the express language of the statute and *Gustafson*. *See* 15 U.S.C. § 77l(a)(2) (reaching sales of

596 (S.D. Tex. 2002) ("[C]ontrol person liability is derivative; a failure to plead a primary, independent violation by the controlled person § 10(b) and Rule 10b-5 precludes such a claim for secondary liability against the controlling person under § 20 of the Exchange Act, or, a violation of §§ 11 or 12 for control person liability under section 15 of the Securities Act of 1933."). According to the Fifth Circuit, control person "liability is predicated on the existence of an independent violation of the securities laws." *ABC Arbitrage Plaintiffs Group v. Tchuruket*, 291 F.3d 336, 348 n.57 (5th Cir. 2002) (citations omitted); *Lone Star Ladies Inv. Club v. Schlotzsky's, Inc.*, 238 F.3d 363, 370 n.33 (5th Cir. 2001); *Lovelace v. Software Spectrum, Inc.*, 78 F.3d 1015, 1017 n.8 (5th Cir. 1996).

B. Plaintiffs' Control Person Allegations Are Inadequate

The control person claims against JPMC should also be dismissed because Plaintiffs' control person allegations consist almost entirely of conclusory statements alleging control person liability against the bank defendants collectively.[29] *See, e.g.*, Am. Compl. ¶¶ 99.1, 995.1, 1016.2. Plaintiffs' only allegations of control individually directed at JPMC are identical to those generic allegations directed *seriatim* at the other bank defendants. Plaintiffs' description of the JPMorgan Chase Entities is the same as its description of the other bank defendants:

> Defendant J.P. Morgan Chase & Co. is an integrated financial services institution that through known and unknown subsidiaries, divisions and/or affiliates acting as the agent of an controlled by J.P. Morgan Chase & Co., such as JP Morgan Securities Inc. and JP Morgan Chase Bank provides ... In addition to J.P. Morgan

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securities that are "by means of a prospectus"); *Gustafson*, 513 U.S. at 571.

29 Plaintiffs fervently argue that their control person claims are not subject to heightened pleading standards of Rule 9(b). Opp. at 55. There is significant disagreement among the courts over the appropriate pleading standard. *In re Enron Corp. Sec., Derivative & ERISA Litig.*, No. Civ. A. H-01-3624, MDL No. 1446, 2003 WL 230688, at *11 (S.D. Tex. Jan. 28, 2003). And while this Court has suggested that Rule 8's notice pleading standard would better effect the remedial legislative history behind Sections 15 and 20(a), the Fifth Circuit has not directly addressed the question. *Id.*

> Chase & Co., the following subsidiaries, divisions and/or affiliates, acting at the direction of and under the control or J.P. Morgan Chase & Co . . . .

Am. Compl. ¶ 100(a). *Compare* Am. Compl. ¶ 100(a) *with* ¶¶ 101(a), 102(a), 103(a), 105(a), 106(a), 107(a), 108(a).

As Plaintiffs' allegations are limited to such conclusory language, no "facts" of control at all are alleged specifically against JPMC. And while, Plaintiffs assert, control person liability is usually a question of fact, "dismissal is appropriate where the plaintiff fails to plead any facts from which it can reasonably be inferred that the particular defendant was a control person." *Collmer v. U.S. Liquids, Inc.*, No. 99-2785, 2001 U.S. Dist. LEXIS 23518, at *10 (S.D. Tex. Jan. 23, 2001). Plaintiffs have only stated unsupported legal conclusions of control, which the Court should not accept. *See Tuchman v. DSC Communications Corp.,* 14 F.3d 1061, 1067 (5th Cir. 1994). Moreover, conclusory statements demonstrate nothing more than the corporate parent-subsidiary relationship of JPMC to JPMSI and JPMCB. As a matter of law, this corporate status does not demonstrate control. *See Novak v. Kasaks*, 997 F. Supp. 425, 435 (S.D.N.Y. 1998), *rev'd on other grounds*, 216 F.3d 300 (2d Cir. 2000). Accordingly, the Section 20(a) and Section 15 claims against JPMC should be dismissed.

IV. Plaintiffs' Failure To Satisfy The PSLRA And Rule 9(b) Mandates Dismissal

A. Plaintiffs' Failure To Plead Scienter Is Not A Technicality

The PSLRA's scienter requirement demands that a plaintiff must, at minimum, show "severe recklessness." Severe recklessness is *not* merely an extreme form of negligence, *see In re Baker Hughes Sec. Litig.,* 136 F. Supp. 2d 630, 647-48 (S.D. Tex. 2000), but is "limited to those highly unreasonable omissions or misrepresentations that involve not merely simple or inexcusable negligence, but an extreme departure from the standard of ordinary care, and that present a danger of misleading buyers or sellers which is either known to the defendant or is so

obvious that the defendant must have been aware of it." *Nathenson v. Zonagen Inc.*, 267 F.3d 400, 408 (5th Cir. 2001)(quoting *Broad v. Rockwell,* 642 F.2d 929, 961 (5th Cir. 1981)); *see Goldstein v. MCI WorldCom*, No. 02-60322, 2003 WL 31738963, at *11 (5th Cir. July 28, 2003) ("Bare conclusory allegations . . . will not suffice under the PSLRA").

Plaintiffs focus primarily on the Mahonia prepay transactions in their Opposition, but the Amended Complaint does not contain any specific factual allegations that each JPMorgan Chase Entity separately knew that Enron and Arthur Andersen were accounting for these transactions improperly.[30] Instead, the Amended Complaint makes general allegations as to the involvement of "top executives" in a handful of Enron transactions, and from such broad allegations, speculates that each JPMorgan Entity must have had knowledge of Enron's fraud.[31] Such generalized and conclusory allegations do not meet the PSLRA's "strong inference" of scienter standard.[32] *Melder v. Morris,* 27 F.3d 1097, 1103 (5th Cir. 1994); *see also City of*

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30 Plaintiffs' failure to distinguish among the JPMorgan Chase Entities further demonstrates their inability to meet the particularity requirements of Rule 9(b) and the PSLRA. Under the PSLRA and Rule 9(b), Plaintiffs simply may not "group plead" the JPMorgan Chase Entities. *In re Enron Corp. Sec., Derivative & ERISA Litig.,* 2003 WL 230688, at *6; *Kunzweiler v. Zero.net, In.,* No. 3:00-CV-2553-P, 2002 U.S. Dist. LEXIS 12080, at *49 n.17 (N.D. Tex. July 3, 2002). The PSLRA's pleading requirements do not distinguish between individual and corporate defendants as Plaintiffs suggest. Opp. at 94. *Double Alpha, Inc. v. Mako Partners L.P.,* No. 99 Civ. 11541, 2000 U.S. Dist. LEXIS 10454, at *7 (S.D.N.Y. July 27, 2000) (dismissing plaintiff's 10(b) claim as to nine defendant investment funds because plaintiff's group pleading was insufficient to meet the requirements of Rule 9(b)).

31 Plaintiffs' claims of a "growing mountain of evidence against the J.P. Morgan Defendants" in their Opposition papers is not a substitute for proper allegations that cannot be found in Plaintiffs' Amended Complaint.

32 JPMC's identification in its Answer of subsidiaries that engaged in transactions with Enron does not excuse Plaintiffs from meeting the PSLRA's pleading requirements. *See McNamara v. Bre-X Minerals Ltd.*, 197 F. Supp. 2d 622, 631-32 (E.D. Tex. 2001) (noting that the court must dismiss a case where the complaint does not meet the pleading requirements of the PSLRA).

Philadelphia v. Fleming Cos., 264 F.3d 1245, 1263-64 (10th Cir. 2001); *In re Advanta Corp. Sec. Litig.*, 180 F.3d 525, 539 (3d Cir. 1999).

B. Documents Not Incorporated In The Amended Complaint Should Not Be Considered On A Motion To Dismiss

In their Opposition, Plaintiffs attempt to use documents not referenced in the Amended Complaint to bolster their inadequate allegations against the JPMorgan Chase Entities. It is axiomatic, however, that "in deciding a motion to dismiss for failure to state a claim, courts must limit their inquiry to the facts stated in the complaint and in the documents either attached to or incorporated in the complaint." *Lovelace*, 78 F.3d at 1017; *U.S. ex rel. Willard v. Humana Health Plan of Texas Inc.*, 2003 WL 21467963, at *2 (5th Cir. 2003) (same). Plaintiffs have violated this rule, attaching an appendix of assorted documents to the Opposition. *See* Opp. 95-96, Ex. 40-42. Plaintiffs may not properly use them to attempt to salvage their defective Amended Complaint, which must be tested by its original allegations. The Court should therefore strike, or at the very least disregard, Plaintiffs' appendix.

The appendix includes an excerpt from an Enron post mortem prepared by the Enron Bankruptcy Examiner that references several e-mails written by Donald Layton and which Plaintiffs now assert are "illustrative of J.P. Morgan's knowledge that the Mahonia prepays were disguised loans intended to deceive public investors." Opp. at 95. The e-mails, however, do not support Plaintiffs' accusation at all. It is clear from the documents themselves that the term "disguised loan" used by Mr. Layton in the e-mails was a generic reference to all prepaid forward transactions and, indeed, all derivative transactions that, like prepaid forwards, involve an up-front payment. Nothing in these e-mails suggests Mr. Layton was referring to the Mahonia prepay structure or that he was even aware of the structure. Moreover, there is nothing sinister about the phrase "disguised loan." It is used in the financial community to describe

synthetic leases, security leases, and prepaid financial instruments.[33] As these e-mails indicate, they were written in connection with an internal review of derivatives to ensure that internal systems properly identified and reflected the general components of derivative transactions, *i.e.*, that the credit exposure resulting from this type of transaction was properly captured, recorded and monitored. And as the e-mails further indicate, the phrase had nothing to do with "disguising" the nature any transactions, but rather, a concern that a failure to adequately monitor the transactions internally might lead to an inaccurate understanding of credit exposures to derivatives customers.

In addition to these e-mails, the appendix also contains some other documents, including excerpts from a Senate Permanent Subcommittee on Investigations Report (Ex. 42), materials provided to that subcommittee (Ex. 37), and a J.P. Morgan Securities Inc. Credit Update on Enron (Ex. 38). While this reply brief is neither the time nor the place to refute the substance of Plaintiffs' accusations drawn from these additional materials, when they are rinsed clean of Plaintiffs' rhetoric, they add no factual support to Plaintiffs' fraud claims against the JPMorgan Chase Entities.

CONCLUSION

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33 *See, e.g.*, Canadian Finance and Leasing Association, *Personal Property Security Act ("PPSA") Leasing Glossary, located* at, http://www.cfla-acfl.ca/ppsaglossary.cfm (last updated Sept. 2001) ("Also referred to as 'financing lease' or '*disguised sale' or 'disguise loan.*' [sic] In essence, involves a situation where a sale of goods is structured as a lease to avoid certain legal consequences, including the requirement to register a PPSA financing statement in some jurisdictions . . . . ") (emphasis added); "IRS Issues Final Regulations on Taxation of Derivatives," *Bloomberg News* (Oct. 11, 1993) ("Finally, the IRS disclosed that its staff is working on a project that deals more generally with off-market and prepaid financial instruments. Tax lawyers interpret this to mean that the IRS is looking at options that are deep "in the money" and other instruments that have *disguised loan features, such as prepaid forward contracts.*") (emphasis added).

For the foregoing reasons and for the reasons set forth in the opening brief in support of their motion to dismiss, JPMC, JPMSI and JPMCB respectfully request that this Court dismiss the Amended Complaint in its entirety and with prejudice.

Dated: Houston, Texas
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Respectfully submitted,

/s/ Richard Warren Mithoff

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CERTIFICATE OF SERVICE

The undersigned certifies that a copy of the foregoing instrument was served on the attorneys of record for all parties to the above cause through esl3624.com in accordance with the Court's order regarding website service on the 31st day of July, 2003.

/s/ Richard Warren Mithoff
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