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MICHAEL W. DOBBINS
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IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF ILLINOIS

EASTERN DIVISION

LAWRENCE E. JAFFE PENSION PLAN, ON BEHALF OF ITSELF AND ALL OTHERS SIMILARLY SITUATED, Plaintiff,	Lead Case No. 02-C-5893 (Consolidated)
- against -	Judge Ronald A. Guzman Magistrate Judge Nan R. Nolan
HOUSEHOLD INTERNATIONAL, INC., ET AL., Defendants.	

APPENDIX OF UNPUBLISHED AUTHORITIES

APPENDIX OF UNPUBLISHED AUTHORITIES

1. *Davidoff* v. *Farina*, No. 04 Civ. 7617 (NRB), 2005 U.S. Dist. LEXIS 17638 (S.D.N.Y. Aug. 22, 2005)
2. *In re Initial Public Offering Securities Litigation*, MDL 1554 (SAS), No. 21 MC 92 (SAS), 04 Civ. 3757 (SAS), 2005 U.S. Dist. LEXIS 12845 (S.D.N.Y. June 28, 2005)
3. *Porter* v. *Conseco, Inc.*, No. 1:02-cv-01332-DFT-TAB, 2005 U.S. Dist. LEXIS 15466 (S.D. Ind. July 14, 2005)

TAB 1

LEXSEE 2005 US DIST LEXIS 17638

DAVIDOFF, et al., Plaintiffs,-against-FARINA, et al., Defendants.

04 Civ. 7617 (NRB)

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

2005 U.S. Dist. LEXIS 17638

August 19, 2005, Decided
August 22, 2005, Filed

DISPOSITION: [*1] Defendants' motions to dismiss granted and Complaint dismissed with prejudice.

LexisNexis(R) Headnotes

COUNSEL: For Plaintiffs: Jeffrey A. Klafter, Esq., Kurt B. Olsen, Esq., Klafter & Olsen LLP, White Plains, NY; Jonah Goldstein, Esq., Ryan Llorens, Esq., Lerach Coughlin Stoia Geller Rudman & Robbins LLP, San Diego, CA.

For the Individual Defendants: John D. Donovan, Jr., Esq., Ropes & Gray LLP, Boston, MA.

For Verizon: William H. Pratt, Esq., Kirkland & Ellis LLP, New York, NY.

For Smith Barney: Mitchell A. Lowenthal, Esq., Carmine D. Boccuzzi, Jr., Esq., Cleary Gottlieb Steen & Hamilton LLP, New York, NY.

JUDGES: NAOMI REICE BUCHWALD, UNITED STATES DISTRICT JUDGE.

OPINIONBY: NAOMI REICE BUCHWALD

OPINION:

MEMORANDUM and ORDER

NAOMI REICE BUCHWALD
UNITED STATES DISTRICT JUDGE

This putative securities class action arises out of the June 28, 2000 initial public offering of 173,913,000 shares of Class A common stock (the "IPO") of Genuity, Inc. ("Genuity"), as well as the subsequent demise and ultimate bankruptcy of that company. Plaintiffs, who purchased shares of Genuity during the putative class period (which extends from the IPO through the filing of bankruptcy), have sued Citigroup [*2] Global Markets Inc. (f/k/a Salomon Smith Barney Holdings Inc.) ("Smith Barney"), n1 Verizon Communications Inc. ("Verizon") n2 and three former Genuity officers (the "Individual Defendants"), n3 seeking damages for alleged violations of the United States securities laws. All defendants have moved to dismiss plaintiffs' complaint on the ground that it fails to state a claim for relief under Fed. R. Civ. P. 12(b)(6) and fails to plead with sufficient particularity under both Fed. R. Civ. P. 9(b) and the Private Securities Litigation Reform Act of 1995 (the "PSLRA"). For the reasons set forth herein, defendants' motions to dismiss are granted.

n1 Smith Barney was one of two lead underwriters for Genuity's IPO. Plaintiffs allege that, as part of its responsibilities in this regard, Smith Barney performed due diligence that included a review and approval of Genuity's business plan.

n2 As explained below, Verizon was created by a merger of GTE Corporation and Bell Atlantic Corporation,

the same merger that created Genuity as a spin-off company.
[*3]

n3 The Individual Defendants are Paul R. Gudonis, who was Genuity's Chairman and C.E.O., Daniel P. O'Brien, who was Genuity's Executive Vice President and C.F.O., and Joseph C. Farina, who was Genuity's President and C.O.O.

BACKGROUND n4

n4 The facts set forth below are drawn from plaintiffs' First Amended Class Action Complaint for Violation of the Securities Exchange Act of 1934, dated November 19, 2004 (the "Complaint"), and are, as is appropriate in deciding these motions, assumed to be true herein.

This lawsuit was instituted after Genuity filed for protection under Chapter 11 of the United States Bankruptcy Code on November 27, 2002. On October 2, 2003, Genuity filed with the bankruptcy court a Second Amended Disclosure Statement in support of the Consolidated Plan of Liquidation (the "Disclosure Statement"), which allegedly revealed to plaintiffs that Genuity had been significantly undercapitalized since [*4] the company went public on June 28, 2000. In their 79-page Complaint, plaintiffs allege that the June 27, 2000 Prospectus that Genuity filed with the Securities and Exchange Commission ("S.E.C.") in connection with the IPO (the "Prospectus"), as well as Genuity's spring 2000 Form S-1 Registration Statement and two subsequent amendments thereto, (collectively, the "IPO statements") were materially misleading because they failed to disclose this undercapitalization. Plaintiffs allege further that various public statements made by Genuity about its business and financial health in the period between the IPO and the company's ultimate bankruptcy filing (collectively, the "post-IPO statements") were materially misleading for a myriad of reasons. The putative class period is alleged to extend through the entire solvent life of the company, from the June 28, 2000 IPO through the November 27, 2002 bankruptcy filing. Below, we outline the IPO and subsequent relevant events before detailing plaintiffs' allegations and defendants' arguments in support of dismissal.

I. Events Leading Up To the IPO

Genuity was a "Tier 1" Internet backbone provider n5 that offered customers suites of [*5] managed Internet infrastructure services such as dedicated and broadband access, web hosting and content delivery and value-added services such as Voice over IP and managed Internet security services. Genuity's origins can be traced to BBN Corporation, a Massachusetts telecommunications company that was acquired in 1997 by GTE Internetworking Inc. ("GTE Internetworking"), a holding company subsidiary of GTE Corporation ("GTE").

n5 The Complaint defines Tier 1 Internet backbone providers as "having the network scale and on-network traffic to offer their customers connectivity to virtually all addresses on the Internet, either directly through their Internet backbone or through cost-free, high speed private connections to other Tier 1 Internet backbones." Compl. P2.

In July 1998, GTE and Bell Atlantic Corporation ("Bell Atlantic") announced a proposed merger, which would combine the two companies into what is now known as Verizon. As part of the merger, and in response to objections by the Federal Communications [*6] Commission ("F.C.C."), GTE and Bell Atlantic determined that GTE Internetworking would be spun off to create an independent company, Genuity. n6 Pursuant to the spin-off plan, Genuity would conduct an IPO that would give the public over 90.5% of the Class A voting equity stock and Verizon (the merged company) approximately 10% of the Class A stock and 95% of the Class B stock. Under the plan, once Verizon obtained requisite approvals from state telecommunications regulators, it would have the option of converting its Class B stock into 80% of the outstanding Class A stock and thereby regaining control of Genuity. Also pursuant to the plan, Verizon both retained rights of consent over various corporate actions by Genuity and was entitled to elect one member of Genuity's board of directors.

n6 Under the Telecommunications Act of 1996, the former regional Baby Bells, such as Bell Atlantic, were

prohibited from owning long distance assets without obtaining approvals, referred to as "271 Approvals," from state regulators. Because the F.C.C. classified certain Internet backbone assets of and services provided by GTE Internetworking as long distance assets, it would not approve the GTE-Bell Atlantic merger unless either those assets were divested or GTE Internetworking became independent of the merged company.

[*7]

II. The IPO

Genuity's IPO was the largest in Internet history. According to the Complaint and the Disclosure Statement, when discussions about a possible IPO began in the spring of 2000, the original target offering price was $25 per share, which would have generated approximately $4.3 billion in proceeds. As discussed more fully below, plaintiffs allege that Genuity's business plan was developed with this figure in mind. With preparations for the IPO underway, however, market conditions began to deteriorate and, as of June 24, 2000, at the recommendation of the investment bankers retained to underwrite the IPO, GTE and Bell Atlantic publicly hoped for an offering price of $12 to $15 per share. n7 By June 28, 2000, however, market conditions had deteriorated further such that the company settled upon an $11 per share offering price, which would generate approximately $1.9 billion in proceeds. Notwithstanding these changes, plaintiffs allege, Genuity neither altered its business plan nor disclosed in its Prospectus that the plan "was severely underfunded as a result of raising only $1.9 billion [through] the IPO." Compl. P6. The IPO was eventually conducted on June 28, 2000 at [*8] an offering price of $11 per share and, as expected, raised approximately $1.9 billion in proceeds.

n7 The Complaint alleges that this offering price was disclosed in the financial press on June 24, 2000.

III. Events Subsequent to the IPO

From early June 2000 through September 2000, GTE and Bell Atlantic worked with their existing bank lenders, including Smith Barney's "sister company," Citibank, N.A., to obtain a credit facility for Genuity. On September 5, 2000, a $2 billion credit facility (the "September 5, 2005 Loan") was established by a consortium of banks under an agreement that also provided that an event of default would occur at such time, if ever, as Verizon was no longer in a position to exercise its option to regain control of Genuity.

Immediately following the IPO, according to the Complaint, Genuity began to expend capital in accordance with its preexisting business plan at a rate of approximately $400 million per quarter. As part of that spending plan, Genuity launched a $20 [*9] million marketing and advertising campaign in September 2000 promoting its "Black Rocket" product, which, according to promotional materials, would bundle key Internet infrastructure into one fully integrated package for mid-to large-sized businesses. To entice potential buyers of the product, Genuity guaranteed that, once ordered, Black Rocket would be delivered within 10 business days or the buyer would be credited for all installation fees. Additionally, Genuity guaranteed that Black Rocket customers would receive credits to their accounts if their product did not have "up-times" of at least 99.9%.

In March 2001, in order to obtain more needed capital, Genuity secured a $500 million loan from defendant Verizon (the "Verizon Loan"). In September 2001, the parties to the Verizon Loan amended the loan to make up to $2 billion available to Genuity. As with the September 5, 2000 Loan, the Verizon Loan provided for cancellation if Verizon did not maintain its option to reacquire control of Genuity.

By the end of 2001, plaintiffs allege that Genuity was facing serious financial difficulties as a result of low revenues, failing sales programs, retention of obsolete equipment and continued [*10] significant capital expenditures under the business plan. On July 21, 2002, Genuity's board of directors held a Sunday night meeting at which it was decided that Genuity would draw down the remaining $850 million available to it under the September 5, 2000 Loan. n8 On July 24, 2002, Genuity announced publicly that Verizon had cancelled its option to reacquire control over Genuity and terminated the Verizon Loan. Finally, on November 27, 2002, Genuity filed for Chapter 11 bankruptcy protection. Plaintiffs allege that the bankruptcy filing was due to Genuity's "inability to recover from the drastically underfunded IPO, its continued high rate of capital expenditures, and its inability to acquire capital from either the banks [that provided the September

5, 2000 Loan] or Verizon." Compl. P16. Genuity's stock, which, according to the Complaint, had been trading as high as $70 per share in early 2001, was trading for pennies per share at the time that bankruptcy was declared.

n8 The Complaint alleges that Deutsche Bank, one of the lenders involved in the September 5, 2000 Loan, refused to forward its portion of the requested $850 million "because it believed that Genuity requested the funds only because Genuity knew that Verizon was backing out of its plan to reacquire [Genuity]." Compl. P15. On July 23, 2002, Deutsche Bank sent a letter to Genuity asking whether Genuity had any reason to believe that Verizon was no longer interested in reacquiring Genuity. Genuity did not answer Deutsche Bank's letter and instead filed a breach of contract lawsuit against Deutsche Bank.

[*11]

IV. The Alleged Misrepresentations

Plaintiffs assert two claims for relief. Claim One alleges that the Individual Defendants and Smith Barney violated § 10(b) of the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5, when the IPO statements and the post-IPO statements were issued. Claim Two alleges that the Individual Defendants and Verizon are liable for the alleged misleading statements as a result of their status as "controlling persons" within the meaning of § 20(a) of the 1934 Act, 15 U.S.C. § 78t(a). Before discussing defendants' arguments in support of dismissal, we briefly outline the statements that plaintiffs allege were misleading.

A. The IPO Statements

As mentioned above, plaintiffs contend that the Prospectus and the pre-IPO Registration Statement (and amendments thereto), were misleading because they failed to disclose to potential investors that the IPO offering price was substantially lower than had initially been anticipated and that Genuity's business plan—and particularly its planned capital expenditures—had [*12] not been modified to take into account the substantially lessened initial capital that would be available to the company at the eventual offering price. In support of this argument, plaintiffs rely primarily on the Disclosure Statement that Genuity filed with the bankruptcy court on October 2, 2003. That statement reads in relevant part as follows:

> In early 1999, GTE Internetworking developed a business plan for the expansion of the GTE/BBN Internet business. As merger planning between GTE and Bell Atlantic progressed, the parties decided that the merged company would, as part of its overall business strategy, enter into direct competition with AT&T, Sprint UUNet (a subsidiary of MCI Worldcom) and others to provide data transmission and Internet backbone services. Accordingly, the merged GTE and Bell Atlantic would require construction of a far larger telecommunications network than GTE Internetworking had originally been contemplating. The two companies developed this new, expanded business plan through the summer and fall of 1999, in order to start construction of the expanded network as soon as they consummated their merger. The companies planned to spend $11-13 billion in [*13] capital within five years to build its business and network with over 500 POPs. In early 2000 the GTE board of directors approved this business plan for the GTE Internetworking business . . . .
>
> As described above, Genuity Inc.'s business plan contemplated $11-13 billion of capital expenditures over five years. To fund this plan, Bell Atlantic and GTE began discussions with investment bankers in the spring of 2000 with a view toward raising $4.3 billion in an initial public offering of Genuity Inc. stock (the "IPO"), which was to remain with Genuity Inc. as the foundation of its capitalization. The $4.3 billion target was based on an estimated IPO price of about $25 per share.
>
> With preparations for the IPO underway, the market for equity in telecommunications and Internet-based businesses began to deteriorate. At the recommendation of their investment bankers, GTE and Bell Atlantic lowered the target IPO share price to a range of $12-15 per share. Notwithstanding the lower-than-expected IPO price and the corresponding reduction in the initial equity capitalization of Genuity Inc., GTE and Bell Atlantic did not change the terms of the Genuity IPO Spin-Out. GTE and Bell Atlantic [*14] did not cancel the IPO, because accomplishing the Genuity IPO Spin-Out was an absolute necessity and precondition to consummating the merger of GTE and Bell Atlantic. Nor did GTE and Bell Atlantic alter

the Genuity Inc. Group business plan, in part because they had sought approval of the merger from their respective shareholders based on a business plan that contemplated the Genuity Inc. Group constructing a massive telecommunications network that would be reintegrated into Verizon as soon as Verizon obtained the requisite 271 Approvals.

By June of 2000, owing to further decline of the industry and the capital markets, the investment bankers recommended a final price for the IPO of $11 per share, which would provide Genuity Inc. with only $1.9 billion of initial equity capital, or 40% of the sum anticipated when GTE and Bell Atlantic formulated the Genuity Inc. Group's business plan. Notwithstanding this further reduction in the equity capitalization of Genuity Inc., GTE and Bell Atlantic did not make any attempt to alter the Genuity Inc. Group's business plan or to defer the IPO. Nor did GTE and Bell Atlantic contribute any additional equity capital to Genuity Inc. to compensate [*15] for the shortfall in IPO proceeds and initial capitalization. On June 27, 2000, the Genuity Inc. board of directors approved the $11 per share IPO pricing, and the IPO was consummated on June 30, 2000. n9

Immediately after the IPO, the Genuity Inc. Group began its capital expenditure program in accordance with its business plan. This caused the Genuity Inc. Group to spend cash at the rate of approximately $400 million per quarter. At this rate, given its paid-in capital, the Genuity Inc. Group would have exhausted its cash in little more than 12 months. The Genuity Inc. Group's business plan, as GTE and Bell Atlantic had approved it, contemplated that Genuity Inc. would have to raise additional funds in the debt markets to supplement what was expected to be an initial equity capitalization of $4.3 billion.

Murphy Decl., Ex. F at 12-13.

n9 The other submissions in this case indicate that the IPO actually occurred on June 28, 2000.

Relying on the Disclosure Statement, plaintiffs argue that Genuity's [*16] allegedly undisclosed business plan was "predicated" and "dependent" on "initially raising $4.3 billion through the IPO." Compl. PP17, 65, 69, 189. Plaintiffs allege that the business plan "contemplated Genuity's construction of a massive telecommunications network that would be reintegrated into Verizon as soon as Verizon obtained the requisite 271 approvals from state regulators," id. P19, and thus called for Genuity to spend capital "at a rate of $400 million per quarter," id. P11. The Complaint further alleges that Genuity's business plan required an initial "foundational" capital infusion of the intended $4.3 billion from the IPO to "enable[] Genuity to pursue its Business Plan for almost three years without the necessity of having to raise additional funds during that period and limiting its need to obtain additional financing from other sources," Compl. P17. In contrast, plaintiffs argue, the $1.9 billion that the IPO actually generated would last the company approximately twelve months at the planned expenditure rate. See id. P11. As a result, plaintiffs contend, Genuity's business plan was undercapitalized from the beginning and the IPO statements were materially [*17] misleading because they failed to disclose these facts to potential investors.

B. The Post-IPO Statements

Plaintiffs also allege that defendants made various false or misleading statements in the wake of the IPO and leading up to Genuity's bankruptcy in November 2002. The statements alleged to be false or misleading were made, for the most part, in interviews with the press, press releases and S.E.C. filings. They are also numerous, but it is unnecessary to recount each statement individually here because all of plaintiffs' post-IPO allegations essentially reduce to four claims, namely: (i) Genuity's statements about its financial condition throughout the putative class period were misleading because Genuity was improperly recognizing revenue in violation of GAAP; (ii) Genuity's statements about its financial condition in 2001 were misleading because Genuity improperly delayed taking an impairment charge on allegedly outdated networking equipment for several months; (iii) Genuity's optimistic representations regarding its Black Rocket product were misleading because they were unrealistic; and (iv) Genuity's statements about its network capabilities were misleading because Genuity's [*18] actual network capabilities were substantially less than the company publicly represented them to be.

1. Improper Revenue Recognition

Plaintiffs allege that numerous statements made by Genuity in its financial statements and in the press regarding the

company's financial health were misleading because the company was improperly recording revenue under GAAP. The alleged GAAP violations occurred in at least four distinct ways. First, plaintiffs allege that Genuity recognized revenue on sales contracts at the time the contracts were signed rather than when the products at issue were delivered, "even though the contracts could be, and often were, cancelled" by Genuity's customers. Compl. P138. Plaintiffs also allege that Genuity improperly recognized revenue on "multi-year" contracts in full at the time the contracts were signed rather than deferring revenue to later periods in which revenue would actually be realized. Plaintiffs allege that these practices "violated the basic GAAP concept that revenue must be earned and realizable in order for a company to recognize it." Compl. P138.

Second, and relatedly, plaintiffs allege that Genuity improperly recognized revenue in connection [*19] with "last minute deals" in which, in order to "bridge the gap between the company's forecasted sales and its actual sales," Genuity would enter into sales agreements with customers either (i) at the end of a quarter or (ii) at the beginning of a quarter but "backdate" the contracts to reflect a signing during the previous quarter. Compl. PP141-43. These techniques were improper, plaintiffs allege, because, although Genuity would recognize the revenue on these contracts during the period in which they purported to be signed, the revenue associated with them was not properly realizable because customers "had the ability to cancel the agreement[s] and in fact often did cancel these agreements." Id. P142. Moreover, plaintiffs allege, recognizing revenue on these contracts at the time of signing was improper because "the customer was not required to pay anything until the services were actually delivered." Id. P143.

Third, plaintiffs allege that Genuity engaged in an improper "dark fiber swap" with Qwest, another Internet service provider, in the first quarter of 2001. Compl. PP27, 144-49. The alleged transaction involved an exchange between the companies of "very large . . [*20] . fiber optical capacity assets for a period of 99 years." Id. P144. The capacity exchanged "was dark fiber and was not anticipated to be lit up for the foreseeable future." Id. P145. n10 Plaintiffs contend that, since the exchange "did not involve the culmination of an earnings process," the proper GAAP treatment of the transaction would have been for Genuity "to record the asset received at the carrying value of the asset transferred." Id. P147. Allegedly in violation of GAAP, however, Genuity treated the exchange as two separate transactions whereby the company first recognized earnings associated with the transfer of its capacity to Qwest and then recorded an asset purchase in the same dollar amount for the capacity it received from Qwest, even though no money actually changed hands. n11 Plaintiffs allege that Genuity's treatment of the transaction "wrongly inflated Genuity's revenue for this period." Id. P149. n12

n10 The Complaint does not define the terms "dark fiber" or "lit up." We assume for our purposes here that plaintiffs mean that the fiber optical capacity exchanged did not carry Internet traffic.

[*21]

n11 Plaintiffs allege that Qwest subsequently acknowledged that the proper accounting treatment of transactions such as this was to "record [them] as exchanges of similar productive assets based on the carrying value of the optical capacity assets that were provided in the exchanges." Compl. P148. Plaintiffs further allege that the S.E.C. filed civil charges against Qwest's executives "for their roles in an array of questionable deals, including deals between Qwest and Genuity," and that "Qwest's accounting further led to a criminal investigation by the Department of Justice and an investigation by the House Committee on Energy and Commerce." Id. P150.

n12 Plaintiffs also allege that, in the third quarter of 2000, Genuity engaged in a transaction with Qwest whereby Genuity acquired modems, equipment and services for $260 million and Qwest paid Genuity a "bonus" of $4 million for closing the transaction before the end of the quarter. Plaintiffs allege that Qwest's accounting treatment of its receipt of the $260 million was of a "questionable nature." It is unclear how, if at all, these allegations relate to plaintiffs' claims against Genuity.

[*22]

Finally, plaintiffs allege that revenue was improperly recognized on "fictitious" sales invoices. Plaintiffs contend that the Individual Defendants encouraged its sales staff to submit bogus invoices by instituting a policy whereby sales staff would be paid commissions in full upon submission of an invoice and then, if the order was subsequently cancelled, charged the amount of the commission from the employee's next paycheck. Moreover, according to a "former Genuity Partner Manager, . . . several sales people submitted sizeable fictitious sales orders and then resigned from Genuity before

the orders were provisioned." Id. P154-55. Plaintiffs contend that Genuity's recognition of revenue associated with such sales orders was improper because the revenue was not realizable.

2. Delayed Impairment Charge on Long-Lived Assets

Plaintiffs' second post-IPO claim is that Genuity's statements regarding its financial condition in 2001 were misleading because Genuity improperly delayed taking a $2.6 billion impairment charge on various networking equipment until the fourth quarter of 2001 that should have been taken in "late 2000/early 2001." Compl. PP157-68. Plaintiffs allege that, [*23] in late 2000, Genuity bulk purchased millions of dollars worth of routing and switching equipment to supply future orders. Plaintiffs further allege that, by early 2001, $30-$ 50 million worth of the equipment was sitting in Genuity's "data centers" unused, and it was apparent that "large amounts" of Genuity's stockpiled networking equipment had become "outdated and obsolete," Compl. P31, in part because demand was shifting away from dial-up services to DSL and cable modem services, id. P167.

Citing the Financial Accounting Standards Board's ("FASB") Statement of Financial Accounting Standard ("SFAS") No. 121, plaintiffs argue that Genuity was required to record an impairment charge "whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable." Plaintiffs contend that, as a result of Genuity's networking equipment becoming "outdated and obsolete," demand for Genuity's services declined rapidly and it became apparent in early 2001 that Genuity would not recover the carrying amounts of a significant portion of its stockpiled equipment. Nevertheless, plaintiffs contend, Genuity improperly waited to record the $2.6 billion charge [*24] until the fourth quarter of 2001. n13

> n13 The Complaint states that the reason Genuity waited to record the impairment charge was that the company was seeking $2.3 billion in financing from Verizon and various banks in 2001 and that "Genuity would not have been able to obtain this additional $2.3 billion of financing in 3Q01 if it had properly accounted for its impaired assets." Id. P166.

3. Statements Concerning Black Rocket

The third class of alleged misrepresentations concern Genuity's Black Rocket product. As noted earlier, Black Rocket was a packaged bundle of Internet services aimed to serve mid-to large-sized business. As also mentioned above, Genuity guaranteed to its customers that it would either deliver Black Rocket within 10 days of a customer's order or credit all of the customer's installation fees. According to the Complaint, the product had an "average price tag of $100,000 to $1 million." Compl. P12.

The Complaint alleges that, for several reasons, Genuity's public statements [*25] about Black Rocket were misleading. First, plaintiffs allege that Genuity's optimistic statements about Black Rocket's market potential were misleading because the networking technology on which Black Rocket was based was quickly becoming obsolete at the time Black Rocket was being ramped up. Second, plaintiffs contend that statements touting Genuity's 10-day delivery guarantee were misleadingly unrealistic because of the time-consuming complexity and amount of work involved in designing, building, installing, testing and delivering each customized Black Rocket product to each individual customer. Third, plaintiffs allege, while Genuity represented to the public that Black Rocket sales were "extremely profitable," the company actually "was unable to determine the costs of each Black Rocket installation due to the high level of customization required, which caused the costs associated with each Black Rocket project to vary greatly." Compl. P36. Fourth, plaintiffs allege that Genuity's representations regarding demand for and customer acceptance of Black Rocket were misleading because "the Black Rocket service offering was neither competitive nor successful due to lack of customer demand, [*26] the unrealistic installation guarantees, and the fact that Genuity had over-purchased huge stockpiles of equipment in anticipation of demand that failed to materialize and which quickly became outdated." Id. P37.

4. Statements Concerning Genuity's Network Capabilities

The last category of alleged misrepresentations is Genuity's public statements about its fiber network capacity. According to the complaint, Genuity made public statements about "the substantial progress of its network build-out." Compl. P38. Plaintiffs allege that these statements were false because "on multiple occasions Genuity built temporary, non-functional structures." Id. Moreover, plaintiffs contend, "after the phony sites were erected and announcements about their completion were made, Genuity tore them down." Id. Plaintiffs allege that, as of mid-2001, only 10% of Genuity's fiber network was "actually lit" and that "the majority of Genuity's fiber network was incapable of carrying network

traffic." Id. P39.

V. Defendants' Motions to Dismiss

All defendants have moved to dismiss on the ground that plaintiffs have neither stated a claim for relief under Fed. R. Civ. P. 12(b)(6) [*27] nor pleaded with adequate particularity under Fed. R. Civ. P. 9(b) and the PSLRA. All defendants argue that the IPO statements were not misleading as a matter of law both because the securities laws did not require Genuity to disclose prior targeted offering prices that it had chosen not to pursue in the actual IPO and because the Prospectus adequately warned plaintiffs of the risks and facts that plaintiffs now contend materialized and caused them harm. With respect to the post-IPO statements, defendants argue that plaintiffs have failed to plead with sufficient particularity and that, even if plaintiffs' allegations were sufficiently particularized, defendants' statements are protected under the PSLRA's safe harbor provision for forward-looking statements, see 15 U.S.C. § 78u-5(c). Defendants argue further that plaintiffs have failed adequately to plead scienter or "loss causation," both of which are required under the PSLRA. Finally, Verizon argues that the claims against it should be dismissed both because Verizon did not "control" Genuity within the meaning of § 20(a) of the 1934 Act and because Verizon is [*28] not alleged to have been a "culpable participant" in any wrongdoing. On July 28, 2005, the Court heard oral argument.

For the reasons discussed below, we dismiss plaintiffs' complaint in its entirety on the ground that, with respect to each alleged misrepresentation, plaintiffs have failed adequately to plead falsity, scienter and/or "loss causation."

DISCUSSION

In considering defendants' motions to dismiss, the Court may consider the Complaint as well as documents on which plaintiffs clearly relied in drafting the Complaint, such as the Prospectus and the Disclosure Statement. See, e.g., Chambers v. Time Warner, Inc., 282 F.3d 147, 153 (2d Cir. 2002). We must accept as true all material factual allegations in the Complaint. Levy ex rel. Immunogen Inc. v. Southbrook Int'l Invs., Ltd., 263 F.3d 10, 14 (2d Cir. 2001). A motion to dismiss may be granted only where "it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." Still v. DeBuono, 101 F.3d 888, 891 (2d Cir. 1996) (quoting Conley v. Gibson, 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957)). In evaluating [*29] the Complaint under this standard, we first address plaintiffs' IPO claims.

I. The IPO Statements

Defendants argue that the IPO statements were not misleading because they did not omit any fact required to be disclosed under the securities laws. Defendants argue further that the "bespeaks caution" doctrine precludes liability because the Prospectus adequately informed plaintiffs of the risks of which they now complain. We agree that, under either of these rationales, plaintiffs' IPO claims must fail.

The securities laws affirmatively require the disclosure of information that may "render[] prior public statements materially misleading." San Leandro Emergency Medical Group Profit Sharing Plan v. Philip Morris Cos., Inc., 75 F.3d 801, 810 (2d Cir. 1996) (quoting In re Time Warner Inc. Securities Litigation, 9 F.3d 259, 268 (2d Cir. 1993)). Under the facts alleged in the present case, the relevant inquiry is essentially the same as that required under the "bespeaks caution" doctrine, which holds that misstatements in the context of a stock offering are immaterial as a matter of law when "it cannot be said that any reasonable investor could [*30] consider them important in light of adequate cautionary language set out in the same offering." Halperin v. eBanker USA.com, Inc., 295 F.3d 352, 357 (2d Cir. 2002); see also P. Stolz Family Partnership L.P. v. Daum, 355 F.3d 92, 96 (2d Cir. 2004) ("A defendant may not be liable . . . for misrepresentations in a prospectus if the alleged misrepresentations were sufficiently balanced by cautionary language within the same prospectus such that no reasonable investor would be misled about the nature and risk of the offered security.").

The required analysis comprises two steps: first, we must identify the risk that plaintiffs allege was not disclosed in the IPO statements; second, we examine the IPO statements "to determine if a reasonable investor could have been misled into thinking that the risk that materialized and resulted in [the] loss did not actually exist." Halperin, 295 F.3d at 359.

The allegedly undisclosed risk in this case was that the IPO would not provide Genuity with sufficient capital to proceed with its business plan. Even a cursory examination of the Prospectus, however, reveals that this risk and the facts underlying [*31] it were fully disclosed to potential investors. First, it was disclosed exactly how much cash the business plan required Genuity to spend and at what rate:

. "Our capital expenditures program, as currently contemplated, will require between $11 billion and $13 billion during the five-year period ending December 31, 2004, the majority of which will be for the expansion of our network infrastructure." Pratt Decl., Ex. B at 9. n14

. "We currently intend to spend $11 billion to $13 billion over the five-year period ending December 31, 2004, of which approximately $1.8 billion to $2.0 billion is expected to be spent during 2000, on the continued expansion of our network infrastructure and other capital expenditures." Id. at 10.

Second, it was disclosed exactly how much capital the IPO would raise:

. "We estimate that the net proceeds from our sale of the 173,913,000 shares of Class A common stock we are offering at the initial public offering price of $11.00 per share will be approximately $1.8 billion." Id. at 21.

Third, it was disclosed at what rate the IPO proceeds would be spent and that, at the intended spending rate, the proceeds [*32] would be completely depleted in a matter of months:

. "Of the net proceeds of this offering, we intend to use approximately $1.5 billion for capital expenditures, including approximately $1.2 billion in connection with the expansion of our fiber network and approximately $300 million for expansion of our product lines for delivery of advanced data services to our customers." Id. at 21.

. "In the near term, we believe that the proceeds from this offering . . . should be sufficient to meet our cash needs through the first quarter of 2001." Id. at 34.

Fourth, it was emphasized that significant capital in addition to the IPO proceeds would be needed and that, if additional funding was not obtained, Genuity's business would suffer:

. "We will need significant additional capital to fund our business plan and achieve profitability." Id. at 10.

. "We may be unsuccessful in raising sufficient capital on terms that we consider acceptable, when needed or at all. If this happens, we would have to delay or abandon our development and expansion plans, which would adversely affect our competitive position." Id.

n14 In fact, the estimated $11 billion to $13 billion, evenly spread over the five-year period ending December 31, 2004, would require an expenditure rate of between $550 million and $650 million per quarter, a sum that substantially exceeds the $400 million per quarter that plaintiffs allege was actually spent.

[*33]

In light of these disclosures, it is hard to imagine what could have further been said to complete the picture of Genuity's financial situation. It had to have been perfectly clear to anyone who read the Prospectus that the initial capital infusion from the IPO would soon be gone and that Genuity would have to rely on the capital markets to obtain the additional financing that its business plan required. n15

n15 Plaintiffs make much of the fact that, in connection with a motion filed on behalf of Genuity in the bankruptcy court to have a settlement of claims against Verizon approved, the Individual Defendants' attorneys, Ropes & Gray LLP, stated that they believed Genuity had a "potentially viable" breach of fiduciary duty claim against Verizon based on Genuity's inadequate initial capitalization. Pl. Opp'n at 13-14. Plaintiffs attach inordinate significance to this statement, however. For one thing, a claim for breach of fiduciary duty against Verizon, even if viable, would not imply that Genuity had made false statements in its IPO documents. For another, in the brief on which plaintiffs base their argument, Ropes & Gray ultimately concluded that:

The shareholders of Genuity likely would have an extremely difficult time stating a claim for breach of fiduciary duty due to undercapitalization, because the registration statement filed with the SEC, and

> the prospectus distributed to investors, at the time of the Genuity IPO contained extensive disclosure of the risk factors concerning Genuity's business plan and capitalization and the shareholders purchased their shares anyway. Any breach of fiduciary duty claim would, therefore, have to be brought on behalf of Genuity's creditors.

Olsen Decl., Ex B at 28.

[*34]

Plaintiffs maintain, however, that the Prospectus failed to disclose that Genuity's business plan was "undercapitalized" in the sense that it was "predicated" on raising $4.3 billion (the amount resulting from an IPO at $25 per share) in an IPO n16 and that skilled investors knowing all of the relevant facts about the business plan would have concluded that the company was doomed to failure from the start. n17 This argument simply is not tenable given that all of the operative facts—the business plan's overall capital requirement of $11 billion to $13 billion with capital expenditures in excess of $400 million per quarter, the $1.9 billion that the IPO would generate, the scheduled depletion of those proceeds in short order and the necessity to immediately seek additional debt financing to cover the gap between the capital generated through the IPO and that required under the business plan—were fully disclosed. Moreover, plaintiffs acknowledge that several of the alleged "insiders" in this case—the Individual Defendants, Verizon and Smith Barney's parent, Citigroup—themselves acquired significant portions of Genuity's public stock. n18 Verizon, Citigroup and a consortium [*35] of other sophisticated banks further loaned Genuity billions of dollars shortly after the IPO and throughout the duration of the company's solvency. And, up until shortly before Genuity's initial bankruptcy filing, Verizon is alleged to have intended to reacquire control of the company. These circumstances suggest in the strongest of terms that sophisticated investors with the most intimate knowledge of Genuity's business plan and capitalization had confidence in the company's future and certainly did not think that the company was "undercapitalized" as plaintiffs use that term. n19

n16 Plaintiffs conceded at oral argument that the previous target of $25 per share, which undoubtedly was a moving one in the months preceding the IPO, was not required to be disclosed in the Prospectus. Plaintiffs further conceded that any sophisticated investor would have known that market conditions in the months preceding the IPO would have allowed a higher offering price for Genuity shares than the $11 that was ultimately obtained.

n17 In this vein, plaintiffs referred the Court during oral argument to the Fifth Circuit's decision in Matter of Mobile Steel Company, which defined "undercapitalization" as a condition that exists "if, in the opinion of a skilled financial analyst, [existing capital] would definitely be insufficient to support a business of the size and nature of the [company at issue] in light of the circumstances existing at the time the [company] was capitalized." 563 F.2d 692, 703 (5th Cir. 1977). Plaintiffs argue that the "bespeaks caution" doctrine does not apply in the present case because the gravamen of their IPO claim is the alleged failure of the Prospectus to disclose the "present fact" that the company's business plan was "undercapitalized" under Matter of Mobile Steel Company's definition, not that the Prospectus failed to disclose the "future risk" that Genuity would fail due to insufficient capital. See Pl. Opp'n at 7-10 (citing P. Stolz Family Partnership L.P., 355 F.3d at 97 (holding that "bespeaks caution" doctrine applies to warnings about risks of future contingencies, not to representations of "historical or present fact")). Apart from the obvious question of whether there is a meaningful distinction between these concepts under the facts alleged here, there is, for the reasons discussed above, little support in the Complaint or in plaintiffs' other submissions for the notion that, at the time of the IPO, "skilled financial analysts" thought that Genuity's capitalization would preclude viability.

[*36]

n18 Indeed, Citigroup and Verizon together acquired approximately 21.5% of the publicly traded shares.

n19 These facts also compel the conclusion that defendants did not act with the scienter that is required under the securities laws. See Part II.C, infra. Indeed, it would have made no economic sense for defendants to invest literally billions of dollars in a venture that they knew would fail.

Finally, and perhaps most tellingly, plaintiffs' fundamental premise that Genuity had an undisclosed "business plan" that was "predicated" on a "foundational" infusion of $4.3 billion in IPO proceeds is a misreading of the Disclosure

Statement. According to that statement, upon which plaintiffs stated at oral argument their premise is entirely based, Genuity's "new, expanded business plan" was "developed . . . through the summer and fall of 1999." Murphy Decl., Ex. F at 11. The Disclosure Statement also states, however, that the original $4.3 billion IPO figure was not even contemplated until months later, when "Bell Atlantic and GTE began discussions with investment bankers in the spring [*37] of 2000" about a possible IPO. Id. at 12. The Disclosure Statement clarifies, moreover, that "the $4.3 billion target was based on an estimated IPO price of about $25 per share" and thus was not some predetermined figure that Genuity's analysts determined was necessary to fund the business plan. Id. As defendants pointed out during oral argument, the "business plan" was thus a spending plan and appears not to have contemplated sources of capital, "foundational" or otherwise.

Faced with the numerous financial disclosures in the IPO statements and acknowledging that there is no disclosure requirement for earlier hoped for IPO share prices, plaintiffs have devised a contorted claim of failure to disclose a so-called business plan, which is simply unsupported by the documents on which they rely. For the reasons stated above, plaintiffs' claim that the IPO statements were fraudulent is dismissed for failure adequately to allege any material misrepresentation. n20 We now turn to the post-IPO statements.

n20 Plaintiffs clarified at oral argument that their claim against defendant Smith Barney is based solely on the IPO statements, not on the post-IPO statements. Accordingly, Smith Barney must be dismissed as a defendant for the reasons stated above, and the discussion that follows applies only to the allegations against the Individual Defendants and Verizon.

[*38]

II. The Post-IPO Statements

Defendants seek to dismiss all of plaintiffs' post-IPO claims on numerous grounds, including that the Complaint fails to plead fraud with adequate particularity, that scienter is not sufficiently pleaded and that the PSLRA's "loss causation" requirement is not satisfied. n21

n21 Before evaluating these arguments, however, it is worth noting that the Complaint makes clear that the IPO claim, which we have just dismissed, is the lynchpin of plaintiffs' case in terms of the defined class, which includes "all purchasers of the publicly traded securities of Genuity . . . during the period from June 28, 2000 through November 27, 2002." Compl. P1. There is no delineation in the Complaint of any subclass related to any of the post-IPO statements. Yet the majority of the post-IPO allegations, even if sufficiently pleaded, would be applicable to only discrete and very narrow classes, if any.

A. Particularity

Defendants' principal objection to the post-IPO claims is that [*39] plaintiffs fail to plead the existence of fraudulent misrepresentations with the particularity required by Fed. R. Civ. P. 9(b) and the PSLRA. We agree that the majority of plaintiffs' allegations lack the requisite particularity and therefore must be dismissed.

1. The Legal Standard

Where a complaint alleges fraud, Fed. R. Civ. P. 9(b) requires that "the circumstances constituting fraud . . . shall be stated with particularity." Where a complaint alleges securities fraud as a result of misleading public statements, the PSLRA requires that the complaint "specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed." 15 U.S.C. § 78u-4(b)(1).

What these rules mean in the context of a fraudulent misrepresentation claim under Rule 10b-5 is that plaintiffs must "(1) specify the statements that [they] contend[] were fraudulent, (2) identify the speaker, [*40] (3) state where and when the statements were made, and (4) explain why the statements were fraudulent." Novak v. Kasaks, 216 F.3d 300, 306 (2d Cir. 2000) (internal citation omitted). While the particularity mandates of Fed. R. Civ. P. 9(b) and the PSLRA do not require plaintiffs to plead "every single fact upon which their beliefs concerning false or misleading statements are based," Novak, 216 F.3d at 313, they do require plaintiffs to plead facts "sufficient to support a reasonable belief as to the misleading nature of the statement[s] or omission[s]," id. at 314 n.1. Where improper accounting under GAAP is alleged,

moreover, plaintiffs "must provide at the very least some level of detail about the improper accounting alleged to underlie misleading statements, and their materiality, in order to survive the motion to dismiss phase." Gavish v. Revlon, Inc., 2004 U.S. Dist. LEXIS 19771, No. 00 Civ. 7291, 2004 WL 2210269, *13 (S.D.N.Y. Sept. 30, 2004); see also Rombach v. Chang, 355 F.3d 164, 174 (2d Cir. 2004) ("Plaintiffs must do more than say that the statements in the press releases [*41] were false and misleading; they must demonstrate with specificity how that is so."); San Leandro Emergency Medical Group Profit Sharing Plan, 75 F.3d at 812 (stating that, "in order to satisfy the requirements of Rule 9(b), plaintiffs must allege in what respects the statements at issue were false"). On the other hand, these particularity requirements are not meant to bar potentially meritorious securities claims where missing facts can only be obtained through discovery. See, e.g., In re AOL Time Warner, Inc. Sec. and "ERISA" Litig., 2004 U.S. Dist. LEXIS 7917, No. 02 Civ. 5575, 2004 WL 992991, *12 (S.D.N.Y. May 5, 2004).

Under these standards, most of plaintiffs' claims relating to the post-IPO statements cannot survive scrutiny under the particularity requirement. We now evaluate those claims seriatim.

2. Improper Revenue Recognition

Despite the Complaint's purported reliance on former Genuity employees and corporate insiders, plaintiffs' allegations regarding improper revenue recognition are exceedingly general and do not explain with any specificity what effect the alleged conduct had on the company's statements regarding its financial health. For example:

. [*42] Plaintiffs allege that recognizing revenue at the time Genuity's contracts were signed was improper under GAAP because "most customers" had "cancellation rights" that were "often" exercised, Compl. P21, but plaintiffs do not allege which customers cancelled, what kinds of "cancellation rights" were retained, by whom they were retained or how much revenue was improperly recognized as a result.

. Plaintiffs allege that "in many instances, . . . last minute agreements were cancelled in the following quarter," id. P142, but plaintiffs do not explain which agreements were cancelled or how much revenue was recognized as a result.

. Plaintiffs allege that "Genuity would recognize revenue from multi-year contracts in full upon the signing of the contract," id. P140, but they do not explain how often this was done, by whom or how much revenue was improperly recognized.

. Plaintiffs allege that Genuity's sales team "created fictitious sales orders," id. PP28, 154-56, but plaintiffs do not indicate when, by whom or what size "fictitious" orders were generated. n22

More generally, it is impossible to tell from the Complaint whether this conduct could have materially [*43] affected Genuity's financial statements so as to render them misleading to such an extent as to create liability under the securities laws.

n22 Nor do plaintiffs explain why, if there were truly an effort on Genuity's part to create "fictitious" sales orders, the company would have paid its sales people commissions to do so. The more logical and cheaper approach would have been simply to create the allegedly fake orders without involving the sales staff at all.

Nor do plaintiffs allege with any particularity a concerted scheme by any defendant or defendants to misrepresent Genuity's financial condition for any particular purpose. n23 It is impossible, therefore, to infer that the alleged improper accounting activity infected Genuity's practices to such an extent as to have any material impact on the company's financial statements. Accordingly, with two exceptions, which we explain shortly, we must dismiss plaintiffs' allegations of improper revenue recognition as insufficiently particularized under Fed. R. Civ. P. 9(b) [*44] and the PSLRA.

n23 Plaintiffs allege simply that, "in order to overstate its earnings and assets in 2000-2002, Genuity violated GAAP and SEC rules by improperly recognizing revenue and by failing to timely record a charge to write-down its impaired assets to reflect impairment of its long-lived assets." Compl. P133.

In opposing this result, plaintiffs rely heavily on In re Computer Associates Class Action Securities Litigation, 75 F. Supp. 2d 68 (E.D.N.Y. 1999). However, the court in that case found that plaintiffs had alleged a "widespread" and "pervasive fraudulent scheme." Id. at 73-74. If we could say the same here, we would have less hesitation to assume, as the court in that case did, that materiality existed as a "huge net effect in error as to the company's overall figures," id. at 73, and thus to overlook plaintiffs' failure to point to specific instances of improperly backdated or "multi-year" contracts, "last minute deals" or "phony sales orders." [*45] As it is, however, plaintiffs have simply failed to plead such an effect. Accordingly, in the absence of allegations of a pervasive fraudulent scheme and in the absence of specifics about particular transactions, we cannot determine to what extent the allegedly wrongful conduct would affect Genuity's financial and press statements and render those statements materially misleading.

The two exceptions, which are adequately pleaded, are plaintiffs' allegations that: (i) according to a Genuity Project Manager named Rick Goodwin, Genuity's Texas office backdated a "sizeable" n24 contract with AOL in the second quarter of 2000, id. PP25, 143; and (ii) that Genuity improperly recognized revenue in connection with its "dark fiber swap" with Qwest in the first quarter of 2001, id. PP27, 144-49. We find that these allegations are sufficiently specific under the Federal Rules and the PSLRA, and we therefore decline to dismiss them on particularity grounds. n25

n24 Giving plaintiffs the benefit of the doubt on these motions to dismiss, we assume that "sizeable" would equate to materiality.

n25 Plaintiffs also allege that, "in December 2002, per a former Genuity Account Representative, Genuity backdated a multi-million dollar contract with Verizon that was scheduled to close in 1Q03 and recognized the revenue associated with this contract in 4Q02," Compl. P143; see also id. P25. We do think that this allegation is sufficiently specific to survive dismissal on grounds of particularity. However, the conduct alleged falls outside the putative class period, which, according to the Complaint, ends on November 27, 2002. Accordingly, this allegation is not relevant to the issue before us.

[*46]

3. Delayed Impairment Charge

With respect to the claims that Genuity improperly delayed taking an impairment charge on $30-$ 50 million worth of outdated networking equipment in 2001, while plaintiffs' allegations could be more precisely drafted, we believe that they are sufficiently specific to avoid dismissal on grounds of particularity.

4. Black Rocket

Plaintiffs' allegations with respect to Black Rocket are insufficiently particularized. Other than general statements about Genuity's difficulty in meeting its 10-day delivery guarantee, inordinately high pricing and difficulty in ascertaining profitability, plaintiffs offer no specific statements that are demonstrably false and materially misleading in the context of the facts pleaded in the Complaint. n26 It is thus impossible to tell from the Complaint whether the statements at issue were false or misleading and, if so, whether they were materially so.

n26 For example, plaintiffs allege that Genuity's statement that Black Rocket was based on "industry-leading hardware and software" was materially misleading because Genuity's "equipment was outdated by the time they installed it and technologically inferior," Compl. P99, presumably because demand was shifting away from dial-up services toward DSL and cable, see id. P167. It is impossible to evaluate from these allegations, however, what hardware was "outdated," to what extent, or how, given that the trend toward DSL and cable was undoubtedly not "inside" information, Genuity's statement could have been materially misleading to the public. Similarly, plaintiffs allege that Genuity's statements that Black Rocket was "extremely profitable" were misleading because it was difficult at the time to calculate the varying profit margin on each installation, but they do not tell us whether Black Rocket was, in fact, profitable at the times the various statements were made. The Complaint's other allegations about Black Rocket are similarly unspecific.

[*47]

Moreover, a substantial portion of plaintiffs' allegations with respect to Black Rocket center on Genuity's public touting of the product and its market potential, without identifying any specific material falsehoods in those statements.

The Second Circuit has made clear, however, that such puffery must be allowed. See, e.g., Rombach v. Chang, 355 F.3d 164, 174 (2d Cir. 2004) ("Up to a point, companies must be permitted to operate with a hopeful outlook: 'People in charge of an enterprise are not required to take a gloomy, fearful or defeatist view of the future; subject to what current data indicates, they can be expected to be confident about their stewardship and the prospects of the business that they manage.'") (quoting Shields v. Citytrust Bancorp, Inc., 25 F.3d 1124, 1129-30 (2d Cir. 1994)). Accordingly, plaintiffs' claims based on statements about the Black Rocket product must be dismissed.

5. Genuity's Network Capabilities

Plaintiffs' allegation that Genuity misrepresented its network capacity is likewise insufficiently specific. The Complaint goes no further in particularity than to allege that Genuity made "public representations [*48] regarding the substantial progress of its network build-out," statements that allegedly were false because "only approximately 10% of Genuity's fiber network was actually lit." Compl. PP38-39. Plaintiffs provide no guidance as to what the alleged false statements were, who made them and when, why they were false when made or why ten percent of Genuity's network being "actually lit" was not "substantial progress." Accordingly, this claim is dismissed.

B. Loss Causation

In light of the discussion above, only three of plaintiffs' post-IPO allegations remain. Those allegations are that Genuity's statements about its financial health were materially misleading because: (i) in the second quarter of 2000, Genuity improperly recognized revenue when it backdated a "sizeable" contract with AOL; (ii) late in the first quarter of 2001, Genuity improperly recognized revenue in connection with its "dark fiber swap" with Qwest; and (iii) in 2001, Genuity improperly delayed by several months the taking of an impairment charge on its outdated networking equipment. We now examine these claims against defendants' argument that plaintiffs have failed to plead "loss causation."

To state a claim [*49] under the securities laws, a plaintiff must allege "loss causation," i.e., a causal connection between the alleged material misrepresentation and the plaintiff's loss. See, e.g., Dura Pharms., Inc. v. Broudo, U.S. , 161 L. Ed. 2d 577, 125 S.Ct. 1627, 1631 (2005). Where a plaintiff alleges that he was harmed by a misleading statement and subsequent decline in stock price, he or she must allege that "the risk that caused the loss was within the zone of risk concealed by the misrepresentations and omissions alleged." Lentell v. Merrill Lynch & Co., Inc., 396 F.3d 161, 173 (2d Cir. 2005) (emphasis in original). In other words, the plaintiff must allege that "'the subject of the fraudulent statement or omission was the cause of the actual loss suffered,' . . . i.e., that the misstatement or omission concealed something from the market that, when disclosed, negatively affected the value of the security." Id. (quoting Suez Equity Investors, L.P. v. Toronto-Dominion Bank, 250 F.3d 87, 95 (2d Cir. 2001)) (emphasis in original). As the Second Circuit has explained, a loss causation analysis examines the relationship between [*50] the loss alleged and the information that the defendant allegedly misstated or concealed. Id. at 174. If that relationship is sufficiently direct, then the loss causation requirement is satisfied.

We find that plaintiffs have failed to plead loss causation with respect to all of the remaining claims. First, with respect to the claim that Genuity improperly delayed taking an impairment charge on its networking equipment in 2001, plaintiffs conceded at oral argument that "there is no loss causation associated with that revelation." July 28, 2005 Tr. 37.

With respect to the allegation that Genuity backdated a contract with AOL in mid-2000, plaintiffs do not allege that a decline in stock price occurred because the fact that the contract was backdated was disclosed to the public or that any stock decline was related to the subject of contract itself. Nor do plaintiffs explain more generally how backdating a contract from one quarter to the previous one could have misrepresented Genuity's aggregate financial position to investors who, like the putative class members, held stock during both quarters. n27 Loss causation is thus not satisfied as to this claim.

n27 It is important to note that these observations apply equally to plaintiffs' other allegations about improperly backdated contracts, which were discussed above. Thus, even if those allegations had been pleaded with sufficient particularity, they would nevertheless be dismissed for failure to plead loss causation.

[*51]

Finally, with respect to the claim that Genuity improperly recorded revenue from its "dark fiber swap" with Qwest, plaintiffs do attempt to allege loss causation, but they fail to do so adequately. The Complaint alleges that, on February 21, 2002, approximately one year after the alleged "dark fiber swap," Genuity held a quarterly analysts' breakfast meeting

at which company management stated, among other things, "that the company never recorded swap revenues, was not in danger of violating its debt covenants and had access to significant funding." Compl. P116. The Complaint further alleges that, "following this announcement, Genuity shares fell nearly 10%--from $22.20 per share on February 20, 2002 to $20 per share on February 21, 2002." Id. P117. In opposing defendants' loss causation argument, plaintiffs contend that Genuity's denial that it recorded swap revenues caused the stock price dip: "Although Genuity falsely denied engaging in such 'recorded swap revenues,' it is reasonable to infer that the market discounted that denial in light of the 'negative news coming out of [that] sector' regarding improperly 'recorded swap revenues.'" Pl. Opp'n at 36 (alteration [*52] in original). In support of this argument, plaintiffs cite the Court's decision in In re Flag Telecom Holdings, Ltd. Securities Litigation, 352 F. Supp. 2d 429, 442 (S.D.N.Y. 2005), which, plaintiffs note, describes a "46% stock price drop on Flag's February 13, 2002 announcement that it had entered into revenue swap transactions." Pl. Opp'n at 36. Plaintiffs conclude that, because it was becoming public at the time that various telecommunications companies had improperly recognized revenue associated with fiber swaps, and because Genuity affirmatively came out and denied that it was engaging in that practice, the public did not believe Genuity's denial and discounted the value of Genuity's stock accordingly.

Plaintiffs' argument must be rejected. There is no allegation that the February 21, 2002 stock price decline followed any revelation of information that Genuity had recorded swap revenues. To the contrary, the relevant statement during the February 21, 2002 analysts' meeting was a denial that Genuity had recorded such revenues. Plaintiffs' speculation that the public disbelieved that denial and therefore discounted the stock price is too strained an inference [*53] even on a motion to dismiss. See, e.g., Lentell, 396 F.3d at 175 (Plaintiffs "must allege facts that support an inference that [defendants'] misstatements and omissions concealed the circumstances that bear upon the loss suffered."). From the facts alleged in the Complaint, the more reasonable inference is that Genuity's stock price fell as part of the general decline in that business sector.

For these reasons, plaintiffs' remaining three claims must be dismissed for plaintiffs' failure to plead any associated loss causation.

C. Scienter

Although each of the post-IPO claims must be dismissed on grounds of insufficient particularity or loss causation, it is important to note that these claims are deficient for the additional reason that plaintiffs have failed to plead scienter. Under the PSLRA, plaintiffs must "state with particularity facts giving rise to a strong inference that the defendant[s] acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2). To satisfy this requirement, which is a particularized version of the Second Circuit's pre-PSLRA scienter pleading standard, see Novak, 216 F.3d at 311 [*54] ("When all is said and done, we believe that the enactment of paragraph (b)(2) did not change the basic pleading standard for scienter in this circuit (except by the addition of the words 'with particularity')."), plaintiffs must specifically allege facts that either: (i) demonstrate that defendants had a motive and opportunity to commit fraud; or (ii) constitute strong circumstantial evidence of conscious misbehavior or recklessness. See Ganino v. Citizens Utilities Co., 228 F.3d 154, 170 (2d Cir. 2000); Rothman v. Gregor, 220 F.3d 81, 90 (2d Cir. 2000). n28

n28 This discussion of scienter is more relevant to plaintiffs' claims against the Individual Defendants than it is to the claims against Verizon, who plaintiffs allege is liable on a "control person" theory under § 20(a) of the 1934 Act. Nonetheless, in the context of a claim under § 20(a), plaintiffs are still required, in order to make out a prima facie case, to allege that Verizon "was in some meaningful sense a culpable participant" in the post-IPO statements. Boguslavsky v. Kaplan, 159 F.3d 715, 720 (2d Cir. 1998) (quoting S.E.C. v. First Jersey Sec., Inc., 101 F.3d 1450, 1472 (2d Cir. 1996)). The Complaint, however, does not allege any involvement by Verizon in the post-IPO statements. In fact, the motives at issue here would suggest that those who were aware of any alleged wrongdoing would desire to keep Verizon in the dark in order to avoid giving Verizon a reason not to exercise its option to reacquire the company. Moreover, plaintiffs' allegations that Verizon had the option to "reacquire" control over Genuity but never exercised that option belie plaintiffs' argument that Verizon was a "control person" under § 20(a). Accordingly, the post-IPO claims against Verizon must be dismissed on the additional grounds that the Complaint does not satisfy the "control person" and the "culpable participation" requirements of § 20(a).

[*55]

Plaintiffs have not argued that motive or opportunity is alleged as to any of the post-IPO statements. n29 With respect to the allegations of GAAP violations, which comprise the bulk of plaintiffs' post-IPO claims, this failure to allege motive

is fatal because allegations of GAAP violations or accounting irregularities alone are insufficient to state a securities fraud claim without evidence of "corresponding fraudulent intent." Novak, 216 F.3d at 309 (quoting Chill, 101 F.3d at 270). Thus, even if it could be established that the Individual Defendants were each aware of the allegedly improper accounting activity, plaintiffs would nevertheless have to establish that the Individual Defendants intended to defraud the public about the content of Genuity's financial statements or had some reason to do so. n30 The Complaint, however, is devoid of factual allegations, circumstantial or otherwise, indicating that the Individual Defendants acted with such intent.

n29 In their opposition papers, plaintiffs do argue that they have adequately alleged motive and opportunity with respect to their claim that the IPO statements were misleading, but they do not do so as to their post-IPO claims. [*56]

n30 Plaintiffs cannot establish the requisite fraudulent motive simply by alleging that the Individual Defendants desired to keep their jobs or increase their compensation by artificially inflating Genuity's stock price. Cf., e.g., Novak, 216 F.3d at 307 ("Plaintiffs could not proceed based on motives possessed by virtually all corporate insiders . . . .") Plaintiffs must "assert a concrete and personal benefit to the individual defendants resulting from the [alleged] fraud." Kalnit v. Eichler, 264 F.3d 131, 139 (2d Cir. 2001). Plaintiffs have failed to do that. Even the Complaint's allegations about reasons that the alleged misrepresentations may have made the company appear to be performing better than it was, see, e.g., Compl. P141 (alleging that "last minute deals" were entered into to "bridge the gap between the company's forecasted sales and its actual sales") do not suggest any concrete benefit received by any Individual Defendant.

With respect to the post-IPO statements regarding Black Rocket and Genuity's network capabilities, which were unrelated [*57] to GAAP, plaintiffs must allege, at the very least, facts constituting strong circumstantial evidence of conscious misbehavior or recklessness. To satisfy this requirement, plaintiffs must allege "highly unreasonable" conduct representing "an extreme departure from the standards of ordinary care . . . to the extent that the danger was either known to the defendant[s] or so obvious that the defendant[s] must have been aware of it." Rothman, 220 F.3d at 90 (quoting Rolf v. Blyth, Eastman Dillon & Co., Inc., 570 F.2d 38, 47 (2d Cir. 1978)); see also Chill v. General Electric Co., 101 F.3d 263, 269 (2d Cir. 1996) (same). Where, as here, there is no indication of motive, "the strength of circumstantial allegations must be correspondingly greater." Kalnit, 264 F.3d at 142 (quoting Beck v. Mfrs. Hanover Trust Co., 820 F.2d 46, 50 (2d Cir. 1987)). Moreover, to the extent plaintiffs claim that defendants had knowledge of specific facts that rendered their public statements misleading, they "must supply some factual basis for the allegation that the defendants [gained this knowledge] at some point during [*58] the time period alleged." Rotham, 220 F.3d at 91 (quoting Posner v. Coopers & Lybrand, 92 F.R.D. 765, 769 (S.D.N.Y. 1981)).

Plaintiffs have not done this. They rely simply on the Individual Defendants' positions as "Genuity's three highest officers" and, without differentiating among the Individual Defendants, argue that those individuals were in a position to know certain things. Pl. Opp'n at 34. n31 As logical as it may be, however, to assume that the Individual Defendants collectively were aware of the specifics of Genuity's business, the PSLRA requires more in order to attach liability to an individual for a specific public statement. It requires that plaintiffs "specifically allege [each] defendant['s] knowledge of facts or access to information contradicting [his] public statements." Novak, 216 F.3d at 308. The general rule, therefore, is that nonspecific allegations that a defendant's knowledge of certain practices can be inferred from his or her high position in a company are not sufficient to satisfy the PSLRA's heightened pleading requirement with respect to scienter. See, e.g., In re NTL, Inc. Sec. Litig., 347 F. Supp. 2d 15, 34 (S.D.N.Y. 2004) [*59] ("Allegations that [defendants] should have known about [corporation's subsidiary's] financial state based solely on their executive positions are not enough to plead scienter."); In re Sotheby's Holdings, Inc. Sec. Litig., 2000 U.S. Dist. LEXIS 12504, No. 00 Civ. 1041,2000 WL 1234601, *7 (S.D.N.Y. Aug. 31, 2000) ("It is well established that boilerplate allegations that defendants knew or should have known of fraudulent conduct based solely on their board membership or executive positions are insufficient to plead scienter."); Duncan v. Pencer, 1996 U.S. Dist. LEXIS 401, No. 94 Civ. 0321, 1996 WL 19043, *14 (S.D.N.Y. Jan. 18, 1996) ("[Plaintiff] would totally thwart the scienter requirements of Section 10(b) and Rule 9(b) if he could satisfy them by simply listing the Individual Defendants' job titles in the Complaint."). n32 Other than general allegations that it would be "logical" for the Individual Defendants to have been aware of certain things, the Complaint gives us no factual basis to conclude that actual knowledge on the part of any Individual Defendant existed. n33 Under the PSLRA, such allegations are insufficient.

n31 In the paragraph of their Complaint that purports to set forth the basis of plaintiffs' allegation that the Individual Defendants "knew or acted in deliberate reckless disregard of the true state of Genuity's business," plaintiffs allege simply that: (i) "the large number of rescissions of sales force commissions as orders were not provisioned or cancelled would logically have been known to the Individual Defendants;" (ii) any failures of Genuity to comply with its 10-day provisioning guarantee "would have been known to the Individual Defendants;" (iii) "the stockpiling of tens of millions of dollars of equipment in 11 data centers owned by the Company would logically have been at the direction of its most senior officers;" (iv) "sales were backdated specifically at the direction of upper management;" (v) "the dark fiber swap with Qwest could not have been accomplished without the complicity of the Individual Defendants;" and (vi) "Genuity's inability to competitively price its outdated equipment was well within the purview of the Individual Defendants' responsibilities." Compl. P191.

[*60]

n32 Plaintiffs' reliance on our decision in In re Complete Management Inc. Securities Litigation, 153 F. Supp. 2d 314, 324-327 (S.D.N.Y. 2001), is misplaced. Although we noted in that case that "it thoroughly strained credulity to imagine that the individual defendants, by virtue of their positions at CMI and the interactions with GMMS that those positions demanded, were ignorant of the practices at GMMS," we also explained that plaintiffs had pleaded the alleged fraud and the defendants' knowledge of it with "great specificity." The same cannot be said here.

n33 Plaintiffs do adequately allege a specific factual basis for one area of knowledge: that Genuity's actual sales were falling short of its sales forecasts. See Compl. P191 (alleging that: (i) defendant Gudonis received "rolled-up sales results;" (ii) defendant Farina received "an Excel spreadsheet with the Company's declining sales results and orders" on a weekly basis; (iii) that defendant Farina received "monthly Flash Reports showing the shortfall between forecasted and actual orders was always 'very significant;'" and (iv) at his "Tuesday Morning Roll Call Sales Meetings," defendant Farina "demanded explanations as to why sales and orders were not materializing"). Such knowledge, however, does not bear on plaintiffs' allegations in this case, which do not include the claim that Genuity publicly stated that actual sales were meeting or exceeding the company's forecasts.

[*61]

CONCLUSION

For the reasons set forth above, defendants' motions to dismiss are granted and the Complaint is dismissed with prejudice. n34 The Clerk of the Court is respectfully requested to close this case on the Court's docket.

n34 In their opposition papers, plaintiffs request that, if the Court deems their allegations insufficient, they be afforded a chance to replead. Plaintiffs do not specify what they would say in such an amended pleading, however. Moreover, in several pre-motion letters submitted by defendants to the Court, plaintiffs were alerted to the specific bases of defendants' arguments in support of dismissal discussed herein. By letter from the Court dated November 4, 2004, plaintiffs were given the opportunity to amend their complaint and were specifically warned that, if they chose not to amend to address the points raised in defendants' pre-motion letters and the Court subsequently determined that defendants' arguments were correct, plaintiffs would not be given another chance to amend. In response, defying the dictates of Fed. R. Civ. P 8(a), and even allowing for the heightened pleading requirements in this case, plaintiffs submitted an exceedingly lengthy 79 page complaint recounting every quarterly and annual S.E.C. filing and myriad public statements made by Genuity during the entire duration of the company's solvency. Notwithstanding its breadth, that pleading is insufficient for the reasons stated above. In these circumstances, we do not see any basis to allow plaintiffs to amend yet again. Accordingly, plaintiffs' request for leave to do so is denied.

[*62]

SO ORDERED.

Dated: New York, New York

August 19, 2005

NAOMI REICE BUCHWALD

UNITED STATES DISTRICT JUDGE

TAB 2

LEXSEE 2005 U.S. DIST. LEXIS 12845

IN RE: INITIAL PUBLIC OFFERING SECURITIES LITIGATION; This document relates to: AMY LIU, ROBERT TENNEY, ROBERT TATE, MARY GORTON, CARLA KELLY, HENRY CIESIELSKI, ED GRIER, FRANK TURK, JENNIE PAPUZZA, STANLEY WARREN, ELLEN DULBERGER, CRAIG MASON, and SHARON BREWER, Plaintiffs, - against - CREDIT SUISSE FIRST BOSTON CORP., CREDIT SUISSE FIRST BOSTON (USA), INC., CREDIT SUISSE FIRST BOSTON, CREDIT SUISSE GROUP, EFFICIENT NETWORKS, INC., eMACHINES, INC., LIGHTSPAN PARTNERSHIP, INC., TANNING TECHNOLOGY CORP., and TUMBLEWEED COMMUNICATIONS CORP., Defendants.

MDL 1554 (SAS), No. 21 MC 92 (SAS), 04 Civ. 3757 (SAS)

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

2005 U.S. Dist. LEXIS 12845

June 27, 2005, Decided
June 28, 2005, Filed

SUBSEQUENT HISTORY: Sanctions disallowed by Liu v. Credit Suisse First Boston Corp. (In re Initial Pub. Offering Sec. Litig.), 2005 U.S. Dist. LEXIS 15162 (S.D.N.Y., July 27, 2005)

PRIOR HISTORY: In re Initial Pub. Offering Sec. Litig., 2005 U.S. Dist. LEXIS 9318 (S.D.N.Y., May 13, 2005)

DISPOSITION: [*1] Plaintiffs' second motion for reconsideration denied in its entirety.

LexisNexis(R) Headnotes

COUNSEL: For Plaintiffs: John G. Watts, Esq., Yearout & Traylor, P.C., Birmingham, AL.

For Issuer Defendants: Kristin Linsey Myles, Esq., Robert L. Dell Angelo, Esq., Munger, Tolles & Olson LLP, San Francisco, CA; Michael L. Hirschfeld, Esq., John A. Boyle, Esq., Milbank, Tweed, Hadley & McCloy LLP, New York, NY; Randall J. Clement, Esq., Sheppard, Mullin, Richter & Hampton LLP, Costa Mesa, CA; Mitchell E. Herr, Esq., Holland & Knight LLP, Miami, FL.

For CSFB Defendants: Peter K. Vigeland, Esq., Robert W. Trenchard, Esq., Wilmer, Cutler & Pickering, New York, NY.

JUDGES: Shira A. Scheindlin, U.S.D.J.

OPINIONBY: Shira A. Scheindlin

OPINION:

OPINION AND ORDER

SHIRA A. SCHEINDLIN, U.S.D.J.:

I. INTRODUCTION

In an Opinion and Order dated April 1, 2005, this Court dismissed plaintiffs' claims in this action, No. 04 Civ. 3757, in their entirety. n1 Plaintiffs moved for reconsideration. On May 13, 2005, I granted plaintiffs' motion in part, but reaffirmed the dismissal of plaintiffs' claims because plaintiffs had failed to plead loss causation. n2 Plaintiffs now move for reconsideration of the May [*2] 13 Opinion. n3

n1 *See In re Initial Public Offering Sec. Litig.* ("In re IPO"), 2005 U. S. Dist. LEXIS 5339, No. 21 MC 92, 2005 WL 743550 (S.D.N.Y. Apr. 1, 2005) *("Liu II").*

n2 *See In re IPO,* 2005 U.S. Dist. LEXIS 9318, No. 21 MC 92, 2005 WL 1162445

(S.D.N.Y. May 13, 2005) *("Liu Reconsideration")*.

N3 *See* Plaintiffs' Memorandum in Support of the Rule 59(e) Motion to Alter, Amend, or Vacate the Order of May 13, 2005, Dismissing the Plaintiffs' Complaint ("2d Reconsideration Mem."). As they did in their first motion for reconsideration, plaintiffs have styled their motion under 59(e) rather than Local Rule 6.3. As I noted in my May 13 Opinion, there is no difference between the two. *See Liu Reconsideration*, 2005 U. S. Dist. LEXIS 9318, 2005 WL 1162445, at *1.

II. LEGAL STANDARD

A motion for reconsideration is governed by Local Rule 6.3 and is appropriate where a court overlooks "controlling decisions or factual matters that were put before it on the underlying motion . . . and which, had they been considered, might [*3] have reasonably altered the result before the court." n4 Alternatively, a motion for reconsideration may be granted to "correct a clear error or prevent manifest injustice." n5 Reconsideration is an "extraordinary remedy to be employed sparingly in the interests of finality and conservation of scarce judicial resources." n6

n4 *Range Road Music, Inc. v. Music Sales Corp.*, 90 F. Supp. 2d 390, 392 (S.D.N.Y. 2000) (quotation marks and citation omitted). *See also Shrader v. CSX Transp., Inc.*, 70 F.3d 255, 257 (2d Cir. 1995) ("The standard for granting . . . a motion [for reconsideration] is strict, and reconsideration will generally be denied unless the moving party can point to controlling decisions or data that the court overlooked -- matters, in other words, that might reasonably be expected to alter the conclusion reached by the court.").

n5 *Doe v. New York City Dep't of Soc. Servs.*, 709 F.2d 782, 789 (2d Cir. 1983).

n6 *In re Health Mgmt. Sys., Inc. Sec. Litig.*, 113 F. Supp. 2d 613, 614 (S.D.N.Y. 2000).

[*4]

Local Rule 6.3 should be "narrowly construed and strictly applied" to avoid repetitive arguments on issues that have been considered fully by the Court. n7 A motion for reconsideration "is not a substitute for appeal;" n8 nor is it "a 'second bite at the apple' for a party dissatisfied with a court's ruling." n9 Courts have repeatedly been forced to warn counsel that such motions should not be made reflexively, "to reargue those issues already considered when a party does not like the way the original motion was resolved." n10 A motion under Local Rule 6.3 "shall be served within ten (10) days after the entry of the court's order determining the original motion." n11

n7 *Greenes v. Vijax Fuel Corp.*, 2004 U.S. Dist. LEXIS 12503, No. 02 Civ. 450, 2004 WL 1516804, at *1 (S.D.N.Y. July 7, 2004).

n8 *RMED Int'l, Inc. v. Sloan's Supermarkets, Inc.*, 207 F. Supp. 2d 292, 296 (S.D.N.Y. 2002) (quotation omitted).

n9 *Pannonia Farms, Inc. v. USA Cable*, 2004 U.S. Dist. LEXIS 15737, No. 03 Civ. 7841, 2004 WL 1794504, at *2 (S.D.N.Y. Aug. 10, 2004).

n10 *Houbigant, Inc. v. ACB Mercantile*, 914 F. Supp. 997, 1001 (S.D.N.Y. 1996).

[*5]

n11 S.D.N.Y. Local Rule 6.3. *See also* Fed. R. Civ. P. 59(e) (same).

On April 19, 2005, in *Dura Pharmaceuticals, Inc. v. Broudo*, n12 the Supreme Court rejected the Ninth Circuit's permissive pleading standard for loss causation, which required only that a plaintiff allege that she had bought a security at an artificially inflated price. n13 The Court noted that "it should not prove burdensome for a plaintiff who has suffered an economic loss to provide a defendant with some indication of the loss and the causal connection that the plaintiff has in mind. At the same time, allowing a plaintiff to forgo giving any indication of the economic loss and proximate cause that the plaintiff has in mind would bring about harm of the very sort the statutes seek to avoid." n14 *Dura* did not establish what *would* be a sufficient loss causation pleading standard; it merely established what was *not*. However, *Dura* cited the stricter standards of the Second, Third, Seventh and Eleventh Circuits' standards as those with whom "the Ninth Circuit's views [*6] about loss causation differ." n15 The Court did not explicitly modify the stricter standards of those Circuits when it rejected the Ninth Circuit's lenient standard; accordingly, *Dura* did not disturb Second Circuit precedent regarding loss causation.

n12 161 L. Ed. 2d 577, 125 S.Ct. 1627, 1630 (2005).

n13 *See Broudo v. Dura Pharms., Inc.*, 339 F.3d 933, 938 (9th Cir. 2003).

n14 *Dura*, 125 S.Ct. at 1634.

n15 *Id.* at 1630 (citing *Emergent Capital Inv. Mgmt., LLC v. Stonepath Group, Inc.*, 343 F.3d 189, 198 (2d Cir. 2003)).

III. PLAINTIFFS' ARGUMENT

Plaintiffs' second motion for reconsideration focuses on the Court's May 13 decision that plaintiffs had not adequately pled loss causation. n16 Essentially, plaintiffs contend that the Court misconstrued the relevant legal standard for loss causation, as articulated in the Second Circuit's decision in *Lentell v. Merrill Lynch & Co., Inc.* n17 In the May 13 Order, I noted that: [*7]

> in material misstatement and omission cases, a court cannot presume dissipation of the inflationary effect; a plaintiff must explicitly allege a disclosure or some other corrective event. Moreover, to establish loss causation, a plaintiff must allege . . . that the *subject* of the fraudulent statement or omission was the cause of the actual loss suffered, *i.e.*, that the misstatement or omission concealed something from the market that, when disclosed, negatively affected the value of the security. n18

n16 Plaintiffs also quibble with the Court's description of the alleged scheme, devoting four pages to the proposition that "the artificial inflation occurred *before* the actual results were announced to have beaten the pre-existing estimates." 2d Reconsideration Mem. at 8. Because plaintiffs have not sufficiently alleged that the alleged scheme caused their losses, the exact timing of the alleged artificial inflation is irrelevant. Moreover, to the extent that plaintiffs now raise questions of transaction causation that were addressed in my April 1, 2005 Order, the ten-day deadline for reconsideration motions has expired. *See* S.D.N.Y. Local Rule 6.3; Fed. R. Civ. P. 59(e).

[*8]

n17 396 F.3d 161 (2d Cir. 2005).

n18 *Liu Reconsideration*, 2005 U.S. Dist. LEXIS 9318, 2005 WL 1162445, at *3 (footnotes and quotation marks omitted).

Plaintiffs contend that *Lentell* simply requires "that the Plaintiffs' Complaint alleges facts to support that the misstatements or omissions were the 'proximate cause' . . . of the investment loss." n19 Plaintiffs contend that, under *Lentell*, "'proximate cause' is construed broadly, except that it logically requires that the *subject* of the fraudulent statement or omission was the cause of the actual loss suffered." n20 Plaintiffs argue that the corrective disclosure requirement of *Lentell* was in fact just one of several possible ways for plaintiffs to allege loss causation, and that plaintiffs' failure to allege any corrective disclosures has no effect on any of the other methods by which plaintiffs may adequately plead loss causation. n21

n19 2d Reconsideration Mem. at 5.

n20 *Id.*

n21 *See id.* at 5-6 (summarizing plaintiffs' apprehension of the *Lentell* test as follows: "[1] was the subject of those 'misstatements and omissions' the cause of the decline in stock values that Plaintiffs claim as their loss? or [2] was there any corrective disclosure regarding the falsity of those 'misstatements and omissions' so as to cause [] the decline in stock values that Plaintiffs claim as their loss? [] or [3] have Plaintiffs alleged that the Defendants concealed or misstated any risks associated with an investment in those securities, some of which presumably caused Plaintiffs' losses?") (bracketed numbers in original).

[*9]

Plaintiffs' confusion is understandable. As the Second Circuit noted in *Suez Equity Investors, L.P. v. Toronto-Dominion Bank*, the Circuit has produced "somewhat inconsistent precedents on loss causation." n22 Indeed, although the Circuit has issued several opinions dealing with loss causation in the last few years, the standard remains ambiguous. n23

n22 250 F.3d 87, 98 n.1 (2d Cir. 2001).

n23 *See Castellano v. Young & Rubicam, Inc.*, 257 F.3d 171, 187 ("While loss causation is easily defined, its application to particular facts

has often been challenging."); *Emergent Capital,* 343 F.3d at 198 (including a section entitled "*Suez Equity* Clarified"); *Lentell v. Merrill Lynch & Co., Inc.,* 396 F.3d 161, 173 (2d Cir. 2005) ("acknowledging that [the] opinion in *Suez Equity* can be mis-read").

n25 *Id.* at 173 (quoting *Suez Equity,* 250 F.3d at 95) (emphasis in *Lentell*).

n26 *Lentell,* 396 F.3d at 173.

n27 *Id.* at 174 (citations omitted).

n28 *Id.* (quotation marks and citations omitted).

IV. DISCUSSION

A. Reconciling the Second Circuit's Loss Causation Standard

The Circuit's most recent decision on loss causation, [*10] *Lentell v. Merrill Lynch,* notes that "we follow the holdings of [three earlier Second Circuit cases,] *Emergent Capital, Castellano* and *Suez Equity.*" n24 Lentell's loss causation standard, though, is difficult to parse. To begin, *Lentell* holds that:

> Thus to establish loss causation, "a plaintiff must allege ... that the *subject* of the fraudulent statement or omission was the cause of the actual loss suffered," i.e., that the misstatement or omission concealed something from the market that, when disclosed, negatively affected the value of the security. Otherwise, the loss in question was not foreseeable. n25

But Lentell's full discussion of loss causation spans several pages, at times asserting different formulations of the loss causation standard. For example, the *Lentell* decision later posits that "this Court's cases -- post-Suez and pre-Suez -- require both that the loss be foreseeable *and* that the loss be caused by the materialization of the concealed risk." n26 On the next page of the decision, the court continues to reformulate its standard, noting that "our precedents make clear that loss causation has to do with the relationship [*11] between the plaintiff's investment loss and the information misstated or concealed by the defendant. If that relationship is sufficiently direct, loss causation is established . . . ." n27 Finally, *Lentell* also states the loss causation standard in the negative: "it is not enough to allege that a defendant's misrepresentations and omissions induced a purchase-time value disparity between the price paid for a security and its true investment quality." n28

n24 *Lentell,* 396 F.3d at 174.

Thus, over time, the Second Circuit has advanced several different standards for pleading loss causation, including "direct causation," n29 "materialization of risk," n30 and "corrective disclosure," n31 all of which are referenced [*12] in *Lentell.* However, a close look at the recent discussion of loss causation by the Second Circuit reveals that the loss causation pleading standard, although murky, is not internally inconsistent.

n29 *See id.* at 174 ("If that relationship [between 'the plaintiff's investment loss and the information misstated'] is sufficiently direct, loss causation is established . . . ."). *See also Suez Equity,* 250 F.3d at 98 n.1 (construing *First Nationwide Bank v. Gelt Funding Co.,* 27 F.3d 763, 769-70 (2d Cir. 1994) as "relying on 'direct causation' analysis for loss causation"). In *First Nationwide,* a RICO case involving allegations that lenders were fraudulently induced to make non-recourse loans for the purchase of real estate, the Circuit dismissed a complaint for a number of reasons, including: (1) plaintiff had not adequately pled materiality; (2) intervening factors (including a market-wide downturn in real estate prices) likely caused plaintiff's losses; and (3) five years had elapsed between the alleged misrepresentations and the losses suffered. *See First Nationwide,* 27 F.3d at 772 (noting that "here, no social purpose would be served by encouraging everyone who suffers an investment loss because of an unanticipated change in market conditions to pick through loan applications with a fine-tooth comb in the hope of uncovering a misrepresentation.") (quotation marks, citation and alteration omitted).

[*13]

n30 *See Lentell,* 396 F.3d at 173 (requiring "that the loss be caused by the materialization of the concealed risk"). *See also Suez Equity,* 250 F.3d at 98 n.1 (calling the Seventh Circuit's "materialization of risk" standard -- which involves "inquiring whether the loss at issue was caused by the materialization of a risk that was not dis-

closed because of the defendant's fraud" -- "both principled and predictable," but noting that the Second Circuit is "not writing on a blank slate, and believe[s] that the approach here articulated best reconciles our precedents to date.").

n31 *See Lentell*, 396 F.3d at 175 n.4 (finding that, because plaintiffs alleged no corrective disclosures, they could not establish loss causation).

Part of the problem lies in the continued expansion of the definition of "securities fraud." Some unlawful activities, such as "jaywalking," have clearly defined limits and comprise a limited range of human behavior. Securities fraud, by contrast, encompasses many distinct types of fraudulent activities, each of which causes [*14] harm in different ways. For example, a broker may "churn" a client's investments -- *i.e.*, make excessive trades to generate broker commissions -- and harm the client by generating large commissions. n32 A broker may assure a client that the broker will only make "safe" investments, and then spend the client's money on extremely risky securities, which lose value; in such cases, the client is harmed when the concealed risk -- the volatility of the actual investments -- lowers the value of her portfolio. n33 A manipulative potential partner may fraudulently persuade a sole proprietor to issue shares in a closely held company, and then dismantle the company or force out the original owner, causing the owner to lose money as the company's profits diminish. n34 A corporation with a right of first refusal on its preferred stock might assure a shareholder seeking to cash in his preferred shares that "nothing [seriously affecting share value] is going to change in the near future" when in fact the corporation knows that a recapitalization likely to enhance share prices is imminent; in such a case, the loss is caused when the employee misses out on a surge in stock prices after the recapitalization [*15] occurs. n35

n32 *See, e.g., Caiola v. Citibank, N.A.*, 295 F.3d 312 (2d Cir. 2002).

n33 *See, e.g., Louros v. Kreicas*, 367 F. Supp. 2d 572, 592-93 (S.D.N.Y. 2005).

n34 *See, e.g., Weiss v. Wittcoff*, 966 F.2d 109 (2d Cir. 1992).

n35 *Castellano*, 257 F.3d at 175.

All of these examples of securities fraud cause a loss to the injured party. The mechanisms for such losses vary widely. However, the common thread is that, in each situation, "the loss be foreseeable and [] the loss be caused by the materialization of the concealed risk." n36 This is true even of the "somewhat inconsistent" precedents the Circuit attempted to reconcile in *Suez Equity*, which resulted in a legal standard that itself has required numerous clarifications. n37

n36 *Lentell*, 396 F.3d at 173 (emphasis omitted).

n37 *Suez Equity*, 250 F.3d at 98 n.1.

[*16]

In *Suez Equity*, the Second Circuit offered the following as an explanation of its holding:

> The standard that we have employed in this opinion attempts to reconcile what we view as our somewhat inconsistent precedents on loss causation. *See, e.g., First Nationwide Bank v. Gelt Funding Co.*, 27 F.3d 763, 769-70 (2d Cir. 1994) (recognizing "foreseeability" approach, but relying on "direct causation" analysis for loss causation); *Weiss v. Wittcoff*, 966 F.2d 109, 111 (2d Cir. 1992) (per curiam) (following "foreseeability" approach); *Mfrs. Hanover Trust Co. v. Drysdale Secs. Corp.*, 801 F.2d 13, 22 (2d Cir. 1986) (finding loss causation where "investment quality" of securities was misrepresented). Were we unconstrained by our own precedents, we might propose a different standard. We note that the approach of the Seventh Circuit -- inquiring whether the loss at issue was caused by the materialization of a risk that was not disclosed because of the defendant's fraud -- appears to be both principled and predictable. *See Bastian v. Petren Res. Corp.*, 892 F.2d 680, 685-86 (7th Cir. 1990); *see also Caremark, Inc. v. Coram Healthcare Corp.*, 113 F.3d 645, 648 (7th Cir. 1997) [*17] ("To plead loss causation, the plaintiff must allege that it was the very facts about which the defendant lied which caused its injuries."). But, we are not writing on a blank slate, and believe that the approach here articulated best reconciles our precedents to date. n38

Upon closer examination, however, the purportedly "inconsistent precedents" are more consistent than they might initially appear to be. That closer examination is

warranted in light of the apparent confusion that reigns with respect to the element of loss causation. A chronological review may be the best approach to the required close examination.

n38 *Id.* (quoting the entirety of footnote one of the *Suez Equity* opinion).

In 1986, the Circuit decided *Manufacturers Hanover Trust,* in which the court established the "investment quality" standard for material misrepresentation cases. n39 In that case, the court held that the defendant had misrepresented the risks associated with an investment in a company whose assets were extremely [*18] unstable. Eventually, the very instability that defendant had concealed caused the collapse of the company, resulting in the loss of the investment. Thus the misrepresentation went to the investment quality of plaintiff's investment, because plaintiff "would not have contracted with [defendant] . . . [to invest] had [plaintiff] known of the misrepresentation . . . particularly given that the [] statements were in part a response to the financial community's concern regarding [defendant's] stability." n40

n39 *Manufacturers Hanover Trust,* 801 F.2d at 22. *Manufacturers Hanover Trust* addressed the question of whether the district judge had properly instructed a jury, which ultimately returned an award of $ 17 million, as to the legal standard for *proving* -- not *pleading* -- loss causation. The Circuit found that the district court, in its charge on "proximate cause," had satisfactorily instructed the jury on loss causation. Despite the different procedural posture, *Suez Equity* relied on *Maufacturers Hanover Trust,* as well as *Weiss* and *First Nationwide Bank* (both pleading cases), in formulating its pleading standard for loss causation.

[*19]

n40 *Id.*

In 1992, the Circuit decided the *Weiss* case, in which defendants persuaded plaintiff to sell them half his company in return for defendants' promise to provide necessary supplies. n41 But defendants did not disclose that they had no intention of keeping their promise but rather intended to take over plaintiff's business and force the plaintiff out. The court held that "it was quite foreseeable that the consummation of defendants' secret intention not to perform their promises would cause Weiss to suffer a loss." n42

n41 *See Weiss,* 966 F.2d at 110-11.

n42 *Id.* at 112.

In both *Manufacturers Hanover Trust* and *Weiss,* the court held that loss causation could be pled by alleging that (1) defendants concealed a foreseeable risk associated with a securities transaction between plaintiffs and defendants; and (2) the foreseeable risk occurred causing plaintiffs' loss. [*20] The difference between the two cases is that one involved an *investor* (hence the phrase "investment quality"), and the other involved an *issuer of securities* (hence the term "foreseeability"). But both cases involved a concealment of negative information which caused the plaintiff's loss when the concealed information eventually caused the transaction to fail.

In 1994, the Circuit decided the third loss causation case cited in *Suez Equity,* which allegedly established a "direct causation" requirement. n43 But *First Nationwide Bank* did no such thing, for the following reasons. *First,* it was not a securities case at all, but a RICO case, involving allegations that a lender was fraudulently induced to make nonrecourse loans for purchases of real estate whose value was materially misstated. The case addressed "proximate cause" rather than "loss causation," which the *Lentell* court later described as an "imperfect" analogy. n44 *Second,* the court found that several factors prevented plaintiffs from pleading proximate cause: (1) plaintiff offered no valid methodology for calculating the magnitude of the misrepresentation regarding the value of the real estate; (2) [*21] five years had elapsed between the time of the misrepresentation and the time of the loss; and (3) a massive market-wide downturn in real estate prices had occurred during the interim. n45 Nonetheless, in articulating its standard, *First Nationwide Bank* offered the following summary of the law of proximate cause: "in addition to showing that but for the defendant's misrepresentations the transaction would not have come about, the [plaintiff] must show that *the misstatements were the reason the transaction turned out to be a losing one.*" n46 Although *First Nationwide Bank* is a RICO case, addressing "but-for" causation and "proximate cause," rather than the securities law concepts of transaction causation and loss causation, it articulates requirements similar to those of *Weiss* and *Manufacturers Hanover Trust.* A plaintiff must allege a material misstatement (*i.e.,* concealment of a risk), and that misstatement must be the cause of the plaintiff's loss (*i.e.,* the risk must materialize).

n43 *See First Nationwide Bank,* 27 F.3d at 765-66. Indeed, it is unclear from the text of *First Nationwide Bank* and *Suez Equity* what a "direct causation" requirement might mean in the context of securities fraud, where statements made to no investor in particular, but disseminated to the public, have consistently been found to have caused investor losses when the statements concealed a risk and the risk materialized.

[*22]

n44 *Lentell,* 396 F.3d at 173.

n45 *See First Nationwide Bank,* 27 F.3d at 770-72. Indeed, the Second Circuit decision on which *First Nationwide Bank* relies for support of its "direct causation" requirement -- *Standardbred Owners Ass'n v. Roosevelt Raceway Assocs., L.P.,* 985 F.2d 102, 104 (2d Cir. 1993) -- refers to the requirement that plaintiff's injuries be "directly *related*" to the alleged wrongdoing, not "directly *caused*" by it. *See Standardbred,* 985 F.2d at 104 ("These opinions emphasize the necessity of proof in a RICO case that the defendant's violations were a proximate cause of the plaintiff's injury, *i.e.,* that there was a *direct relationship* between the plaintiff's injury and the defendant's injurious conduct.") (emphasis added). The Supreme Court case on which both *Standardbred* and *First Nationwide Bank* further relied, *Holmes v. Securities Investor Protection Corp,* 503 U.S. 258, 117 L. Ed. 2d 532, 112 S. Ct. 1311 (1992), is a case about indirect injury in the context of the securities laws. *Holmes* involved a multi-tiered chain of injury in a securities fraud case, in which plaintiffs alleged that an individual's manipulation of securities caused securities prices to crash, thereby causing injury to two broker-dealers. Those broker-dealers, in turn, were subsequently unable to fulfill their own obligations to plaintiffs. *Holmes* is a classic proximate cause decision in which the chain of causation is too diffuse to fairly hold a defendant liable for a twice-removed plaintiff's injuries. It does not articulate a standard of loss causation stricter than the Second Circuit's traditional standard.

[*23]

n46 *First Nationwide Bank,* 27 F.3d at 769 (emphasis added).

Thus, on closer examination, all three cases involve the concealment of a risk and the materialization of that risk. Unfortunately, however, the court in *Suez Equity* resolved the conflict in terminology by sticking with the term "investment quality." "Plaintiffs may allege . . . loss causation by averring [] that . . . the defendants' misrepresentations induced a disparity between the transaction price and the true *investment quality* of the securities at the time of the transaction." n47

n47 *Suez Equity,* 250 F.3d at 97-98 (quotation marks omitted).

In *Emergent Capital,* decided only two years later, the court essentially conceded that the legal standard stated in *Suez Equity* was incomplete. "Plaintiff's allegation of a purchase-time value disparity, standing alone, cannot satisfy the loss causation pleading requirement. [*24] " n48 Rather, the *Emergent Capital* court noted that the *Suez Equity* plaintiffs "specifically asserted a causal connection between the concealed information -- *i.e.,* the executive's [bad financial] history [and incompetence] -- and the ultimate failure of the venture." n49 Thus, the *Emergent Capital* court applied the earlier standard of concealment of a risk and materialization of that risk without an explicit acknowledgment. n50

n48 *Emergent Capital,* 343 F.3d at 198.

n49 *Id.*

n50 Indeed, even if *Emergent Capital* had explicitly reaffirmed the standard of *Suez Equity,* which calls only for a disparity between price and investment quality at the time of purchase -- *i.e.,* artificial inflation -- the standard would no longer be valid. In *Dura,* 125 S.Ct. at 1630, the Supreme Court overturned the Ninth Circuit's permissive standard for pleading loss causation, which required only that a plaintiff allege that a security's value was artificially inflated at the time of purchase.

[*25]

Finally, in *Lentell,* the court paid lip service to *Suez Equity* n51 but held that the Second Circuit "require[s] both that the loss be foreseeable *and* that the loss be caused by the materialization of the concealed risk." n52 It is thus beyond cavil that *Lentell* requires more than the bare "proximate cause" standard asserted by plaintiffs here. n53

n51 *See Lentell,* 396 F.3d at 174 ("We follow the holding[] of . . . *Suez Equity.*"); *but see id.* at 173 ("We acknowledge that the pleading principles set out in the foregoing passage require both that the loss be foreseeable and that the loss be caused by the materialization of the concealed risk; and we further acknowledge that our opinion in *Suez Equity* can be mis-read to say that this Circuit has rejected the 'materialization of risk' approach. *Suez Equity* does not purport to express this Circuit's authoritative position, because that wording: (i) is dicta consigned to a footnote; (ii) is framed in terms that are tentative and speculative, *see [Suez Equity,* 250 F.3d] at 98 n. 1 ('The standard that we have employed in this opinion *attempts* to reconcile *what we view* as our *somewhat* inconsistent precedents on loss causation.') (emphasis added); and (iii) is expressly limited to what was (in 2001) 'our precedents *to date,' id.* (emphasis added).") (emphasis and parentheticals in original).

[*26]

n52 *Id.* (beginning of second full paragraph; beginning of third full paragraph) (emphasis in original). Curiously, the exact same language, including the emphasis, appears twice on the same page of the *Lentell* decision.

n53 2d Reconsideration Mem. at 3.

B. Application to *Liu v. CSFB*

It is vital to understand the nature of the risks that plaintiffs in the instant action allege were concealed. There are two kinds of risk. One risk is that the market could simply discover that the earnings estimates had been tainted by fraud, and that confidence in the securities would diminish, causing their prices to fall. The other risk is more central to plaintiffs' alleged scheme. Plaintiffs have alleged that defendants' scheme lowballed earnings estimates, warned the public that those estimates might be too low, and then reported earnings that exceeded those estimates. As a result, defendants induced the public to overvalue the securities. But when the investors eventually learned that the earnings did not always exceed expectations, their confidence collapsed, as did the price of the [*27] stock, causing their loss.

1. Disclosure of Falsity

The first type of "concealed risk" at issue here -- *i.e.,* that the public might learn that the earnings estimates were fraudulent when made -- *could* support a claim for securities fraud if plaintiffs had pled a disclosing event. *Lentell* teaches, however, that such a concealment can only cause losses after it is disclosed:

> plaintiffs have argued (affirmatively) on this appeal that the falsity of Merrill's recommendations was made public no earlier than April 2002, when the NYAG's affidavit "described the inner workings of Merrill's Internet Group," and that until then plaintiffs (and presumably the market at large) therefore lacked knowledge of the fraud. The complaints withstand the statute of limitations on the strength of that argument. By the same token, however, Merrill's concealed opinions regarding 24/7 Media and Interliant stock could not have caused a decrease in the value of those companies before the concealment was made public. n54

The reasoning is simple. Where the alleged misstatement conceals a condition or event which then occurs and causes the plaintiff's loss, it is the materialization [*28] of the undisclosed condition or event that causes the loss. n55 By contrast, where the alleged misstatement is an intentionally false opinion, the market will not respond to the truth until the falsity is revealed -- *i.e.* a corrective disclosure. n56

n54 *Lentell,* 396 F.3d at 175 n.4.

n55 *See, e.g., Suez Equity* (concealed incompetence led to company's collapse); *Castellano,* 257 F.3d at 187 (concealed intent to recapitalize led plaintiff to sell stock in ignorance of the fact that company would recapitalize thereby vastly increasing stock value).

n56 *See Lentell,* 396 F.3d at 173 ("the misstatement or omission [involving favorable analyst recommendations] concealed something from the market that, when disclosed, negatively affected the value of the security.); *In re WorldCom, Inc. Sec. Litig.,* 2005 U.S. Dist. LEXIS 2216, 2005 WL 375314, at *6 ("A concealed fact cannot cause a decrease in the value of a stock before the concealment is made public.").

Plaintiffs [*29] have not alleged that defendants' fraudulent concealment of their true opinions was ever disclosed, and plaintiffs have made no attempt to tie such a disclosure to their alleged losses. Under *Lentell,* plaintiffs' failure to allege a corrective disclosure of the falsity

of defendants' opinions precludes any claim that such falsity caused their losses. n57

n57 *See id.* at 175 n.4.

The circumstances of *Lentell* are strikingly similar to those alleged in the instant case. In both cases, plaintiffs argued that the fraud was not disclosed, if ever, until years *after* their losses were realized, in successful efforts to withstand dismissal based on the statute of limitations. n58 Both cases allege that plaintiffs' losses were caused when negative market events (*i.e.*, a downgrading of "buy" recommendations or a failure to meet earnings forecasts) were followed by a decline in securities prices. In *Lentell*, though, the court held that the fraudulent nature of the analysts' conduct was not revealed [*30] until "the inner workings of the [analyst] Group" were disclosed; the downgrading of "buy" recommendations did not disclose that the analysts' reports had been tainted. n59 In this case, the gulf between what was alleged to have been the concealed risk and the events that materialized is even more apparent: what was concealed was the analysts' belief that revenue *would* exceed forecasts, and what materialized was exactly the opposite. Accordingly, plaintiffs have *never* alleged any disclosure of the falsity of defendants' opinions.

n58 Specifically, the concealment in *Lentell* was alleged to have been disclosed when the New York Attorney General's office issued an affidavit describing the analysts' behavior. *See id.* In the instant case, no such disclosure has been alleged.

n59 *Id.* In *Lentell*, the "inner workings" of the analysts' group showed that the analysts ignored warnings that certain companies might fail. However, the analysts never lied about those specific defects; rather, their alleged fraud was to be unfailingly upbeat and to inflate share prices through repetitive positive reviews of the securities at issue. *See id.* at 165-66 (summarizing the alleged fraud, which involved "bullish research reports," publication of "BUY or ACCUMULATE" recommendations, and "profoundly unrealistic price targets," issued pursuant to agreements to pump up share prices and share in the investment banking proceeds). Thus, what the analysts concealed was that they did not believe in their own statements, and the effect of their false praise dissipated only when their alleged fraud came to light. *Compare id. with Fogarazzo v. Lehman Bros et al.*, No. 03 Civ. 5194 (Order of 2/10/05), in which I noted that plaintiffs had made the following allegations regarding concealment of specific investment risks:

> On September 7, 1999 . . . Lehman analysts resumed [Lehman's] 1-Buy rating and evaluated RSL's break-up value as exceeding $ 40 per share. Additionally, [an] analyst cited RSL's Delta 3 IPO as "pure upside to our valuation" of RSL. Documents reveal that RSL . . . in fact, thought little about Delta 3's long-term prospects.
>
> . . .
>
> Morgan Stanley . . . reiterated its Strong Buy rating and a $ 38.00 per share price target for RSL, even though . . . RSL announced [three days earlier] that it had taken a massive $ 32 million restructuring charge. Incredibly, in the same [] report, Morgan Stanley characterized the $ 32 million charge to earnings as "a positive for RSL."

2/10/05 Order in *Fogarazzo*, No. 03 Civ. 5194, at 3-4.

[*31]

2. The Market Conditioning Theory

With respect to the other allegedly concealed risk -- that a complicated scheme misled the public as to the true value of the stock -- the loss can only be caused when the true value of the securities is revealed to the public. This theory depends on the supposition that the investing public would disregard the available objective evidence of a company's performance (*e.g.*, its past verified earnings statements, its stature in the marketplace, and its posture in mergers and acquisitions) and instead overvalue the company by relying on the fraudulently nurtured belief that the company would continue to exceed earnings estimates indefinitely.

Lentell acknowledges that "systematically overly optimistic" analysts' reports (and, by analogy, the systematically pessimistic earnings forecasts alleged here), might sometimes support a claim of securities fraud. n60 However, "where [] substantial indicia of the risk that materialized are unambiguously apparent on the face of the disclosures alleged to conceal the very same risk,"

Lentell imposes a heavy burden on plaintiffs to plead their losses specifically. n61 As in *Lentell*, the hundreds [*32] of statements that accompanied defendants' earnings forecasts warned that defendants' estimates were unreliable and could be beaten. n62 In such cases, "a plaintiff must allege (i) facts sufficient to support an inference that it was defendant's fraud -- rather than other salient factors -- that proximately caused plaintiff's loss; or (ii) facts sufficient to apportion the losses between the disclosed and undisclosed portions of the risk that ultimately destroyed an investment." n63

n60 *Lentell*, 396 F.3d at 177.

n61 *Id. Lentell* refers to the fact that the allegedly fraudulent analysts' recommendations in that case (*i.e.*, "buy" or "accumulate") were invariably accompanied by cautionary language that the stock prices were volatile. In fact, the securities at issue in *Lentell* were rated in the "most risky" possible category on a four-point scale. Plaintiffs in *Lentell* alleged that defendants' analyst reports concealed the risk of volatility in share prices -- *i.e.*, the chance that the prices could plummet despite earlier "buy" recommendations. Thus, the "substantial indicia of the risk" were the warnings that the stock price was volatile, and they appeared "on the face" of the analyst reports. Put another way, *Lentell* establishes a standard for those situations in which allegedly misleading statements include cautionary language that the statements might be wrong or misleading. In such cases, plaintiffs must meet a heavy burden of alleging specific losses that are connected to the risks that were actually *concealed*, rather than those risks that were *disclosed* by defendants in their cautionary statements. *See id.*

[*33]

n62 *See* Exs. D, E to Third Amended Complaint.

n63 *Lentell*, 396 F.3d at 177.

Plaintiffs have failed to allege facts sufficient to do either. Rather, they have alleged that the concealed risks materialized when one of three "Disclosing Events" occurred: (1) reported revenue failed to meet or exceed earnings forecasts; (2) a company announced such a shortfall before reporting revenues; or (3) analysts revised their estimates downward. n64 As I noted in my June 8, 2004 Opinion granting plaintiffs' motion for leave to amend their complaint, "each Disclosing Event was the unfortunate but commonplace event of a publicly traded company failing to meet its revenue forecast, coupled with a concomitant and predictable immediate drop in share prices." n65 Plaintiffs have made no effort to allege that it was the defendants' fraud that caused their losses. Nor have plaintiffs alleged "facts sufficient to apportion the losses" between that predictable immediate drop in share prices and any loss that might be attributable to investors abandoning their belief that earnings would exceed [*34] estimates forever. n66

n64 Third Amended Complaint P225.

n65 *In re IPO ("Liu I")*, 341 F. Supp. 2d 328, 350 (S.D.N.Y. 2004).

n66 *Lentell*, 396 F.3d at 177.

Accordingly, plaintiffs have failed to allege loss causation.

V. CONCLUSION

For the foregoing reasons, plaintiffs' second motion for reconsideration is denied in its entirety. The Clerk is directed to close this motion and this case.

SO ORDERED:

Shira A. Scheindlin

U.S.D.J.

Dated: New York, New York

June 27, 2005

TAB 3

LEXSEE 2005 US DIST LEXIS 15466

CAROLYN L. PORTER, FRANZ SCHLEICHER, HERB LANESE, DENNIS SMITH, Plaintiffs, vs. CONSECO INC, GARY C. WENDT, WILLIAM J. SHEA, CHARLES B. CHOKEL, JAMES S. ADAMS, Defendants.

NO. 1:02-cv-01332-DFH-TAB

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF INDIANA, INDIANAPOLIS DIVISION

2005 U.S. Dist. LEXIS 15466

July 14, 2005, Decided

NOTICE: [*1] NOT INTENDED FOR PUBLICATION IN PRINT

DISPOSITION: Defendants' motions to dismiss granted. Consolidated Class Action Complaint dismissed.

LexisNexis(R) Headnotes

COUNSEL: For FRANZ SCHLEICHER, HERB LANESE, DENNIS SMITH, Plaintiffs: Brian Joseph Barry, LAW OFFICES OF BRIAN BARRY, Los Angeles, CA; Kwasi Abraham Asiedu, Torrance, CA; Lionel Zevi Glancy, Avraham Noam Wagner, GLANCY & BINKOW LLP, Los Angeles, CA; Michael Marc Goldberg, GLANCY BINKOW & GOLDBERG, Los Angeles, CA; Claudia Jean Bugh, Peter A. Binkow, GLANCY BINKROW & GOLDBERG LLP, Los Angeles, CA; Robin B. Howald, GLANCY BINKOW & GOLDBERG LLP, New York, NY; Bruce D. Brattain, BRATTAIN & MINNIX, Indianapoilis, IN.

For GARY C. WENDT, WILLIAM J. SHEA, CHARLES B. CHOKEL, Defendants: John W. Reale, Daniel Edward Laytin, KIRKLAND & ELLIS, LLP, Chicago, IL; Robert J. Kopecky, Elizabeth A. Larsen, KIRKLAND & ELLIS, Chicago, IL; Steven Kenneth Huffer, HUFFER & WEATHERS, Indianapolis, IN.

For JAMES S. ADAMS, Defendant: Michael H. Gottschlich, Jonathan D. Mattingly, BARNES & THORNBURG LLP, Indianapolis, IN; Brian Eugene Casey, BARNES THORNBURG, South Bend, IN.

JUDGES: DAVID F. HAMILTON, JUDGE, United States District Judge.

OPINIONBY: DAVID F. HAMILTON

OPINION:

ENTRY ON DEFENDANTS' [*2] MOTIONS TO DISMISS

Plaintiff Franz Schleicher and others who purchased securities from Conseco, Inc. have sued four senior executives of the company for securities fraud between April 24, 2001, and August 9, 2002 (the "Class Period"). Plaintiffs dismissed their claims against Conseco itself after the company went through bankruptcy, which both delayed this case and resulted in discharge of these plaintiffs' claims against the company. Plaintiffs accuse the individual defendants of violating Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, 15 U.S.C. § § 78j(b) & 78t(a), by issuing false and misleading statements to the investing community on the status of Conseco's operations during the Class Period. The court has not yet addressed plaintiffs' class allegations. The issue now before the court is whether the consolidated amended complaint survives a motion to dismiss.

Invoking the heightened pleading standards of both Rule 9(b) of the Federal Rules of Civil Procedure and the Private Securities Litigation Reform Act of 1995 ("PSLRA"), codified in 15 U.S.C. § 78u-4(b), defendants have [*3] moved to dismiss plaintiffs' complaint for failure to state a claim upon which relief can be granted. As explained below, the court finds that plaintiffs have failed to allege loss causation adequately under the standards set forth by the Supreme Court's recent decision in *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. , 161 L. Ed. 2d 577, 125 S. Ct. 1627 (2005). Accordingly, the defendants' motion to dismiss is granted. Plaintiffs have an opportunity to amend their complaint if they wish to do so. n1

n1 Defendants Wendt, Shea, and Chokel have filed one brief, and defendant Adams has filed a separate brief. Adams' brief raises issues specific to him but adopts and incorporates much of the other defendants' brief. The court's decision does not depend on any differences among the four defendants.

I. *Standards for Dismissal*

In ruling on a motion to dismiss under Rule 12(b)(6) for failure to state a claim, the court must assume as true all well-pleaded facts set forth in the complaint, construing [*4] the allegations liberally and drawing all inferences in a light most favorable to the plaintiff. *Forseth v. Village of Sussex,* 199 F.3d 363, 368 (7th Cir. 2000). Under the liberal notice pleading standard in federal civil actions, the plaintiff is entitled to the benefit not only of his allegations but of any other facts he might assert that are not inconsistent with his allegations. Defendants are entitled to dismissal only where "it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson,* 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957); *Chaney v. Suburban Bus Division,* 52 F.3d 623, 626-27 (7th Cir. 1995).

In a securities fraud case like this one, however, the standards are raised by two provisions of the law. Rule 9(b) of the Federal Rules of Civil Procedure requires a plaintiff alleging fraud to allege "with particularity" the circumstances constituting fraud. *In re HealthCare Compare Corp. Securities Litigation,* 75 F.3d 276, 281 (7th Cir. 1996); Fed. R. Civ. P. 9(b). This [*5] requirement means in essence that the plaintiff must allege "the who, what, when, where, and how: the first paragraph of any newspaper story." *In re HealthCare Compare,* 75 F.3d at 281, quoting *DiLeo v. Ernst & Young,* 901 F.2d 624, 627 (7th Cir. 1990). Rule 9(b) allows intent, knowledge, or other states of mind to be alleged generally. In securities fraud cases, the PSLRA further requires that plaintiffs "state with particularity facts giving rise to a strong inference that the defendant acted with the requisite state of mind." 15 U.S.C. § 78u-4(b)(2); accord, *e.g., In re HealthCare Compare,* 75 F.3d at 281.

II. *Loss Causation*

To state a viable § 10(b) claim, a plaintiff must allege that "the act or omission of the defendant alleged to violate [§ 10(b)] caused the loss for which the plaintiff seeks to recover damages." 15 U.S.C. § 78u-4(b)(4); see also *Bastian v. Petren Resources Corp.,* 892 F.2d 680, 685 (7th Cir. 1990) (plaintiff must show that "but for the defendant's wrongdoing, the plaintiff would not have incurred the harm of which he complains"). [*6]

In *Dura Pharmaceuticals, Inc. v. Broudo,* 544 U.S. , , 125 S. Ct. 1627, 1631, 161 L. Ed. 2d 577 (2005), the Supreme Court addressed the requirement of loss causation, "a causal connection between the material misrepresentation and the loss." In *Dura Pharmaceuticals,* the Ninth Circuit had held that a plaintiff adequately alleged loss causation by alleging that the defendants' misrepresentation caused the market price of the security to be artificially inflated when the plaintiff bought it. The Supreme Court reversed, holding unanimously that more was required.

How much more? As *Dura Pharmaceuticals* came to the Supreme Court, the issue was whether plaintiffs could pursue a claim that the defendants falsely claimed that a new spray device for treating asthma would receive FDA approval. At the close of the class purchase period, the defendant's stock price fell dramatically for other reasons. Not until eight months after the close of the class period did the defendant announce that the FDA had not approved the new spray device. Defendants argued that the timing meant that the alleged misrepresentation concerning the spray device could not possibly [*7] have caused any loss to the plaintiffs.

Plaintiffs pursued the securities fraud claim on the theory that the defendants' false predictions for the spray device had artificially inflated the stock price above an honest price. The problem lay in the timing of the relevant disclosure. The key allegation missing from the complaint, in the Supreme Court's view, was an allegation "that Dura's share price fell significantly after the truth became known." 125 S. Ct. at 1634. The absence of such an allegation, wrote the Court, "suggests that the plaintiffs considered the allegation of purchase price inflation alone sufficient." *Id.* The Court went on to affirm the district court's dismissal of the relevant claims in the complaint because it did not allege loss causation with respect to the alleged misrepresentations concerning the spray device. The complaint would need to give the defendants notice of the alleged economic loss and the alleged causal connection between the loss and the relevant misrepresentation. *Id.*

In the 1980s and 1990s, Conseco grew rapidly in the insurance and financial services industries. The company began to encounter serious financial difficulties [*8] after its $ 6 billion acquisition in 1998 of Green Tree Financial Corporation, which later became known as Conseco Finance. After the acquisition, Conseco took on an additional $ 3.6 billion in debt to cover losses at Conseco Finance. In April 2000, Conseco CEO Steve Hilbert and other senior executives resigned. At that time, Conseco's stock price had fallen to $ 5.62 per share, meaning

it had lost more than 90% of the value it had before the Green Tree acquisition. This loss occurred *before* the plaintiffs in the present case made any of their investments at issue here.

In the summer of 2000, the Conseco board brought in a new management team to turn the company around after two disastrous years. The new team included the individual defendants in this case: Gary C. Wendt as CEO, William J. Shea as COO and CFO, Charles B. Chokel as CFO, and James S. Adams as chief accounting officer. The new team ultimately did not succeed in turning the company around. On December 17, 2002, Conseco filed for Chapter 11 bankruptcy protection.

The focus in this lawsuit is on a particular 16-month period during the long slide of Conseco stock price from lofty heights to zero. In early September [*9] 2000 under the new management, Conseco stock traded around $ 9.00 per share. By the start of the Class Period, the price had risen to $ 16.98, and it climbed as high as $ 19.82 per share on May 3, 2001. Plaintiffs seek to represent a class of those who bought Conseco stock beginning on April 24, 2001, and ending on August 9, 2002, when the company announced that it was delaying payment on some debt and had retained legal and financial advisors to help it restructure its corporate debt. In October 2001, the stock went below $ 5.00 per share. It never went above that level again. On August 9, 2002, the last day of the Class Period, the stock price declined from 34 cents per share to about 11 cents per share. On August 12th, the New York Stock Exchange halted trading in Conseco stock. The stock continued to trade on "pink sheets" for a few cents per share, but lost all value in the bankruptcy proceeding launched in December 2002.

Plaintiffs allege that, during the 16-month period from April 24, 2001, to August 9, 2002, defendants were responsible for misleading the investing community about the success of their rescue efforts in several ways:

> 1. Undisclosed guaranty obligations [*10] of $ 900 million on so-called "B-2" certificates that Conseco Finance pledged as collateral for its credit facility with Lehman Brothers, combined with accounting that treated Conseco's payments to itself as operating income.
>
> 2. Undisclosed operating deficit from inadequate loan servicing fees.
>
> 3. Undisclosed $ 2 billion loss contingency arising from poor documentation on "exception loans" sold to securitization trusts.
>
> 4. Failure to write-down the value of interest-only securities as projected cash flows and interest rates dropped.
>
> 5. Concealing the number of delinquent consumer loans.
>
> 6. Failing to adhere to published credit-quality standards for consumer loans.
>
> 7. Undisclosed losses from loans to directors and officers. Under Hilbert's management, Conseco had set up a program under which officers and directors borrowed hundreds of millions of dollars from a bank and used the proceeds to buy Conseco stock, which of course continued to fall in value. Conseco guaranteed to the bank that the loans would be repaid. During the Class Period, Conseco continued to list the scheduled loan repayments as assets, yet according to plaintiffs, the defendants knew [*11] that Conseco did not expect and was not planning to seek repayment by the officers and directors.
>
> 8. Failure to include the director and officer loans in debt repayment plans, with the effect of misrepresenting the company's viability.

Notwithstanding these allegations, the record of Conseco's public statements and SEC filings during the attempted turnaround is replete with other bad news. Effective January 1, 2002, Conseco wrote off approximately $ 2.9 billion in goodwill. In May 2002, Moody's downgraded Conseco's senior debt rating from "B-2" to "Caa1." In July 2002, A.M. Best downgraded the financial strength rating for the company's insurance subsidiaries. In the third quarter of 2002, Conseco realized nearly $ 500 million in losses in its investment portfolio. This is not so much a case where plaintiffs are alleging that defendants painted a falsely rosy picture. It is more as if plaintiffs allege that defendants painted with shades of gray that were not quite dark and gloomy enough.

For present purposes, the most important point here is that the truth about matters that plaintiffs allege were concealed or misrepresented did not come out publicly until months after the [*12] end of the class period, even during the bankruptcy litigation itself. This is not a case where plaintiffs can point to a sharp drop in the company's stock price following announcement of the allegedly concealed truth. The stock had long since hit bottom before these alleged misrepresentations became known.

Plaintiffs' brief in opposition to dismissal relied on the Ninth Circuit's decision in *Dura Pharmaceuticals* and other cases taking a similar approach, holding that a plaintiff could allege loss causation merely be stating that the misrepresentation artificially inflated the price of the security at the time of purchase. See Pl. Br. at 42-43 (Docket No. 101). In fact, the brief asserts "the absurdity of applying a loss causation standard which requires the value of plaintiffs' shares to decline following the revelation of the truth." *Id.* at 41. The brief was written before the Supreme Court decided the case, of course, and adopted that very position.

Plaintiffs have responded to the Supreme Court's decision by suggesting that there may be other ways in which a securities fraud plaintiff might plead loss causation. For example, plaintiffs seize on Justice Breyer's use of [*13] the phrase "leak out" in the sentence: "But if, say, the purchaser sells the shares quickly before the relevant truth begins to leak out, the misrepresentation will not have led to any loss." 544 U.S. at , 125 S. Ct. at 1631; see also *In re Tyco Int'l Ltd.,* 2004 U.S. Dist. LEXIS 20733, 2004 WL 2348315, *14 (D.N.H. Oct. 14, 2004) (denying motion to dismiss where complaint alleged that company's "stock price declined in part because investors concluded that they could no longer credit the company's denials of accounting misconduct"). Plaintiffs in this case suggest they can prove that the truth was beginning to "leak out" about some of the matters they allege, contributing to the massive decline in Conseco stock prices during the Class Period as Conseco disclosed a host of financial problems it faced. See Docket No. 128 at 5. Whether the Court's use of the phrase "leak out" shows that plaintiffs' suggestion would be sufficient under *Dura Pharmaceuticals* is not clear. It is clear, however, that this theory is certainly not what plaintiffs have alleged in the operative complaint. The Supreme Court's opinion makes clear that a plaintiff must give a defendant fair notice of his loss causation [*14] theory in the complaint. 544 U.S. at , 125 S. Ct. at 1634.

Plaintiffs also suggest that they have alleged loss causation when the stock lost its last 34 cents or so of value in August 2002 in response to the company's own announcement that it was delaying payment on some debts and had hired advisors to help restructure its corporate debts. Plaintiffs described this latter announcement as "a stunning blow" to the investing public. It is not clear to the court how the investing public could be "stunned" by news that drove a company's already battered stock value down from a mere 34 cents per share, especially since the stock had once been worth approximately $ 60.00 per share. All of plaintiffs' investments during the class period can fairly be described as speculative investments in a company in deep trouble.

In any event, the Supreme Court's decision in *Dura Pharmaceuticals* has undermined plaintiffs' theory of loss causation as pleaded in the complaint. Perhaps plaintiffs can salvage some portions of the case under the *Dura Pharmaceuticals* standard. They are entitled to try to do so by amending their complaint, though in light of the many and daunting problems Conseco [*15] faced, the problem of loss causation may pose a major challenge of proof even if plaintiffs can plead it adequately for a portion of the case. The court does not reach the issue of whether plaintiffs adequately alleged scienter because it seems likely that any amended version of the complaint may be considerably different from the current version.

III. *Control Person Liability*

Although the complaint must be dismissed on the loss causation ground, the potential for an amended complaint makes it prudent for the court to address another defense argument that seeks complete dismissal. Plaintiffs allege that the individual defendants are liable for securities fraud under § 20(a) as "controlling persons" of Conseco. Section 20(a) of the Exchange Act establishes liability as follows:

> Every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person acted in good faith and did not directly or indirectly induce the [*16] act or acts constituting the violation or cause of action.

15 U.S.C. § 78t. Defendants argue that they can be held liable under § 20(a) only "*to the same extent as*" Conseco is held liable. Since Conseco was discharged in bankruptcy from any potential liability under the Exchange Act, defendants argue, plaintiffs cannot state a claim against them under § 20(a).

Plaintiffs counter by citing *Kemmerer v. Weaver,* 445 F.2d 76 (7th Cir. 1971). In *Kemmerer,* the alleged primary violator was dissolved by the defendants. Defendants there, like the defendants here, argued they could be held liable under § 20(a) only to the same extent as the alleged primary violator; *i.e.,* not at all. The court disposed of the defendant's argument as follows:

> The premise of this argument is that there is a finding of "no liability" with respect to the [alleged primary violator]. No such finding exists, it appearing instead that the Association was dismissed from the suit for lack of jurisdiction due to a failure to obtain service of process. It further appears that the reason for the failure to obtain process was that the Association had [*17] been dissolved on the initiative of many of the individual defendants in the present suit. On such facts it is evident that [§ 20(a)] is of no avail to defendants.

Id. at 78. While *Kemmerer* involved the alleged primary violator's dissolution rather than its bankruptcy, the Seventh Circuit's reasoning applies here. Accord, *In re Citi-Source, Inc. Securities Litigation,* 694 F. Supp. 1069, 1077 (S.D.N.Y. 1988); *Elliott Graphics, Inc. v. Stein,* 660 F. Supp. 378, 381-82 (N.D. Ill. 1987). Conseco has not been found "not liable" for securities fraud. Also, it would be inconsistent with the broad remedial purposes of the securities laws to permit senior executives of a bankrupt corporation - whose actions allegedly contributed to the bankruptcy - to avoid liability by relying on the corporation's bankruptcy.

Plaintiffs' allegations purporting to establish defendants' control over Conseco are sufficient. The Seventh Circuit views § 20(a) "as remedial, to be construed liberally, and requiring only some indirect means of discipline or influence short of actual direction to hold a control person liable." *Harrison v. Dean Witter Reynolds, Inc.,* 974 F.2d 873, 880 (7th Cir. 1992) [*18] (quotation omitted). The Seventh Circuit looks to whether the alleged control-person "actually participated in, that is, exercised control over, the operations of the person in general and, then, to whether the alleged control-person possessed the power or ability to control the specific transaction or activity upon which the primary violation was predicated, whether or not that power was exercised." *Id.* at 881. The fact that each defendant signed at least one of the SEC filings alone satisfies this standard. And the complaint as a whole makes clear that each defendant - as CEO (Wendt), COO and CFO (Shea), CAO/Treasurer (Adams), and Executive Vice President/CFO (Chokel) - cannot plausibly deny the kind of control implied by the Seventh Circuit's liberal construction of § 20(a). See also Complaint PP290-91. Because of changes in the defendants' positions during the Class Period, issues of potential individual liability will still need to be reconsidered in light of amendments plaintiffs might make to their complaint in response to this decision.

Accordingly, the defendants' motions to dismiss are hereby granted. The Consolidated Class Action Complaint is hereby dismissed. [*19] The dismissal is without prejudice to plaintiffs' right to file an amended complaint no later than August 24, 2005.

So ordered.

Date: July 14, 2005

DAVID F. HAMILTON, JUDGE

United States District Court

Southern District of Indiana