UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

IN RE CONVERIUM HOLDING AG SECURITIES LITIGATION (Meyer v. Converium Holding AG, et al.) This Document Relates to: 04 Civ. 8038 04 Civ. 8060 04 Civ. 8295 04 Civ. 8994 04 Civ. 9479	Civil Action No. 04 Civ. 7897 (MBM) ECF Case

MEMORANDUM OF LAW IN SUPPORT OF DEFENDANTS UBS AG'S AND MERRILL LYNCH INTERNATIONAL'S MOTION TO DISMISS THE CONSOLIDATED AMENDED CLASS ACTION COMPLAINT

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Table of Contents

Table of Contents
(continued)

Table of Authorities

Page(s)

Cases

Table of Authorities
(continued)

Page(s)

Table of Authorities
(continued)

Page(s)

Statutes

Other

Defendants UBS AG, acting through its business group UBS Warburg ("UBS"), and Merrill Lynch International ("Merrill") submit this memorandum of law in support of their motion to dismiss Counts I (Section 11) and III (Section 12(a)(2)) of plaintiffs' Consolidated Amended Class Action Complaint pursuant to Fed. R. Civ. P. 12(b)(6).

Preliminary Statement

Almost four years after Converium Holding AG's ("Converium") initial public offering, plaintiffs filed their Consolidated Amended Class Action Complaint (the "Complaint") bringing for the first time 1933 Securities Act claims against UBS and Merrill (collectively, the "Underwriter Defendants") based on allegations that Converium's loss reserve estimates for its North American business underwritten from 1997 to 2000 had been understated by $225 million in the Registration Statement and Prospectus for Converium's December 2001 initial public offering. Plaintiffs' claims, which were brought in September 2005, are barred by the maximum three-year limitations period, which expired more than nine months before they or any shareholder named UBS and Merrill as defendants. In an attempt to evade the fact that their claims against the Underwriter Defendants have plainly expired, plaintiffs now argue that they are saved by a tolling agreement that does not mention them and that they did not solicit, sign, comply with, become a party to, or even know about until after class counsel for these plaintiffs had consciously elected not to sue the underwriters and had knowingly allowed the applicable limitations period to expire on these claims.

In addition, within a year of the December 2001 offering, Converium announced four reserve increases amounting to $176.2 million for its North American business underwritten from 1997 through 2000. That amounts to over three-fourths of

the maximum amount by which plaintiffs, exercising their propensity to find fraud by hindsight, allege Converium's loss reserve estimates were deficient at the time of the initial public offering. Combined with contemporaneous statements by Converium's management and ratings downgrades, those subsequent increases were more than sufficient to make clear that reserve estimates in the Registration Statement and Prospectus had been too low, and to place plaintiffs on inquiry notice with regard to the claims based on inadequate reserves they now make against the Underwriter Defendants. This means the statutory period for plaintiffs' claims expired over two years ago (and before there was any tolling agreement with any shareholder). Indeed, in submissions to this Court, lead plaintiffs' counsel admitted that the alleged fraud of understating Converium's loss reserve estimates in December 2001 was disclosed in October 2002 and caused one of the named plaintiffs to sell at a loss. There can be no doubt that plaintiffs' 1933 Act claims in Counts I and III against the Underwriter Defendants are barred plainly and completely by both the one-year and three-year statutes of limitations.

Even had plaintiffs timely initiated these claims against the Underwriter Defendants—and they did not—the Underwriter Defendants are entitled to dismissal under Fed. R. Civ. P. 12(b)(6) because plaintiffs fail to allege facts sufficient to state a 1933 Act claim against these underwriters. The Underwriter Defendants were entitled to rely upon two expert opinions as to the sufficiency of Converium's loss reserve numbers as actually estimated and then stated in the Registration Statement and Prospectus. Outside, as well as inside, actuarial experts analyzed Converium's loss reserves and concluded that those reserves, as adjusted in 2001 and then stated in the Converium Registration Statement and Prospectus, corresponded to the outside expert's best

estimate. Likewise, outside accountants audited Converium's financial statements—which included the company's loss reserve estimates—and certified that they were accurate. The Underwriter Defendants were not required to perform that expert actuarial analysis or to make an estimate of future loss on Converium's policies. Moreover, plaintiffs allege no "red flags" that would suggest the Underwriter Defendants were not entitled to rely upon those experts' opinions, which were included with the permission of the experts in the offering documents.

Plaintiffs' claims against the Underwriter Defendants also fail to allege any statement in the Registration Statement and Prospectus that was material and false or misleading when made in December 2001. Moreover, because certain purchasers of Converium shares in the offerings abroad and subsequent purchasers on the SWX Swiss Exchange ("SWX") were explicitly excluded from the U.S. Registration Statement, they cannot trace their shares back to that U.S. registration with the SEC and, therefore, cannot state a Section 11 claim.

Procedural History

Beginning in the summer of 2004, at least six purported class action suits were brought against Zurich Financial Services ("ZFS"), Converium and a number of Converium's officers and directors based on claims that Converium's loss reserves had been fraudulently understated starting back in 2001. None of those actions named UBS or Merrill, who were the lead underwriters for Converium's December 11, 2001 initial public offering.

The closest the Underwriter Defendants came to a Converium lawsuit was a discussion with a lawyer for Michael Rubin. On December 9, 2004, two days before the three-year maximum limitations period expired for claims based on the initial public

offering, the Underwriter Defendants entered into a private tolling agreement with Mr. Rubin (the "Rubin Agreement"), who that day had brought a 1933 Act suit against Converium, ZFS and others in New York State court. (Zach Decl. Exh. 1.) By December 9, 2004, plaintiffs in this action had already filed several suits against the other defendants in this case, but none of them ever solicited a tolling agreement with respect to the Underwriter Defendants or sued the Underwriter Defendants before the Complaint was submitted on September 23, 2005.

The Rubin action against Converium and others was eventually removed and was the occasion for extended argument in this Court over who ought to be lead plaintiffs. This debate continued at the pre-trial hearing on August 8, 2005, when co-lead counsel actively dismissed the importance of the assertions of Rubin's counsel that the federal plaintiffs and lead counsel had let the statute expire on any Section 11 claims against the underwriters. (Zach Decl. Exh. 2 at 3-4). Lead counsel defended their decisions on selection of claims and defendants by arguing that bringing 1933 Act claims against the underwriters had been considered and rejected as not necessary:

(a) "We did not bobble the ball, your Honor. The Section 11 claims were preserved against the issuer and the primary defendants in this case when we filed the initial complaints." (Id. at 4-5.)

(b) Lead counsel also argued they had plaintiffs who can assert newly pleaded Section 11 claims against the Converium and ZFS defendants on a relation-back theory and, as to the underwriters, said "actually they're not defendants—potential third parties, each of whom has a due diligence defense . . . We didn't drop the ball". (Id. at 8.)

(c) On the question whether a new plaintiff other than Rubin could "take advantage" of the Rubin Agreement, lead counsel asserted that "I don't believe it is or will be [necessary]. Nobody sued the underwriters . . ." (Id. at 9.)

(d) Responding to the Court's question whether "everybody [was] aboard who is going to be aboard before we set a schedule", lead counsel said "my understanding is everyone is, your honor" and then did not sue the Underwriter Defendants until over a month later. (Id. at 14.)

In other words, these inadequate reserves claims against the Underwriter Defendants had not been brought because of their obvious due diligence defense and the statute of limitations had knowingly been allowed to run without any tolling agreement because these Underwriter Defendants were not "necessary".

On September 23, 2005, plaintiffs in this action filed the Complaint, which asserted Section 11 and 12(a)(2) claims against the original federal defendants and named—for the first time—UBS and Merrill as defendants on such newly pleaded claims. It is apparent that these out-of-time claims against "unnecessary" defendants were filed in an attempt to moot the competition for lead plaintiff or co-lead attorney appointment.

On November 11, 2005, Rubin served the Underwriter Defendants with notice that he was terminating the Rubin Agreement, which cleared the way for Rubin to bring suit against UBS and Merrill. (Zach Decl. Exh. 3) Subsequently, on December 12, 2005, Rubin filed a purported class action in New York State court against UBS and Merrill, as well as against the rest of the underwriting syndicate for the Converium initial public offering. (Zach Decl. Exh. 4.)

Statement of Facts[1]

In March 2001, ZFS, a Swiss company headquartered in Zurich, announced its decision to divest substantially all of its third party reinsurance business, which it historically managed under the "Zurich Re" name. (Zach Decl. Exh. 5 at 30.) In preparation for that divestiture, ZFS formed a separate Swiss company—Converium—to manage the Zurich Re business and transferred cash and other assets and liabilities to the newly created company. (Id.) Converium was organized in four operating segments: Converium Zurich, Converium North America, Converium Cologne and Converium Life. (Id.)

On September 6, 2001, ZFS issued a press release stating that it would be divesting the majority of its interest in Converium by means of a sale to the public in the fourth quarter of 2001. (Zach Decl. Exh. 6.) Converium also issued its own press release that same day. (Zach Decl. Exh. 7.) In addition to noting the planned IPO in the following quarter, Converium stated:

> "During the second quarter of 2001, following an independent actuarial review, Converium undertook reserve strengthening amounting to $112 million. As a result, Converium's loss reserves at Dec. 31, 2000

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[1] In general, for purposes of a motion to dismiss, plaintiffs' allegations must be accepted as true. However, the Court of Appeals made clear that "'legal conclusions, deductions or opinions couched as factual allegations are not given a presumption of truthfulness.'" Mason v. Am. Tobacco Co., 346 F.3d 36, 39 (2d Cir. 2003) (quoting United States v. Bonnanno Organized Crime Family of La Cosa Nostra, 879 F.2d 20, 27 (2d Cir. 1989).) In addition, this Court may consider all documents mentioned in the Complaint that form the basis of plaintiffs' claims. See, e.g., Cortec Indus., Inc. v. Sum Holding L.P., 949 F.2d 42, 47 (2d Cir. 1991). The Court also "may review and consider public disclosure documents" id. at 47, along with other public documents such as news articles and press releases, see Shah v. Morgan Stanley, No. 03 Civ. 8761 (RJH), 2004 WL 2346716, *9 (S.D.N.Y. Oct. 19, 2004) ; White v. H & R Block, Inc., No. 02 Civ. 8965 (MBM), 2004 WL 1698628, *6-7 (S.D.N.Y. July 28, 2004) . Moreover, "subjective characterizations of documents properly before" the Court are not entitled to be accepted as true for purposes of a motion to dismiss. Polar Int'l Brokerage Corp. v. Reeve, 108 F. Supp. 2d 225, 241 (S.D.N.Y. 2000).

> correspond to the consulting actuaries' best estimate of provisions for net loss and loss adjustment expenses."

(Id.) UBS and Merrill were retained to underwrite the global offering.

Prior to the September 6, 2001 press release, Tillinghast had been retained by ZFS to analyze the reserves of its reinsurance business in anticipation of ZFS's planned divestiture of that business. (See Compl. ¶ 81.) In a preliminary draft of its report, dated May 25, 2001, Tillinghast estimated a $186 million reserve deficiency for Zurich Re's North American business as of December 31, 2000. (Declaration of Alyson L. Redman in Support of Def. ZFS's Mot. to Dismiss ("Redman Decl.") Exh. B at Summary Exhibit 1, Sheet 1b; see also Compl. ¶ 86.) On September 10, 2001, Tillinghast delivered its final report to ZFS. In the final report, Tillinghast stated that its "best estimates" of the deficiencies in Zurich Re's estimated loss reserves were $162 million for the North American business and $156.5 million overall. (Redman Decl. Exh. A at 5.) The overall range of loss reserves calculated by Tillinghast had a "low" of $3.010 billion and a "high" of $3.716 billion. (Id. at 6.)

Converium filed a Registration Statement on Form F-1 with the U.S. Securities and Exchange Commission ("SEC") on November 19, 2001. (Zach Decl. Exh. 8.) Included in the Registration Statement was a preliminary prospectus for the offering that reiterated the reserve strengthening of $112 million described in the September 6, 2001 Converium press release. (Id. at 123-24.) The preliminary prospectus also identified the outside actuarial firm that conducted the analysis as Tillinghast and attached the "Consent of Tillinghast-Towers Perrin", which allowed reference to Tillinghast and its analysis in the Registration Statement. (Zach Decl. Exh. 9.) In addition, the Form F-1 stated that "[o]ffers and sales of registered shares and American

Depositary Shares outside the United States are being made pursuant to Regulation S and are not covered by this Registration Statement." (Zach Decl Exh. 8 at cover page.)

Converium's initial public offering took place on December 11, 2001. That global offering consisted of three separate offerings. (Zach Decl. Exh. 5 at 10.) First, there was an initial public offering of Converium shares in Switzerland. (Id.) Second, there was an offering in the United States of shares and American Depositary Shares ("ADSs"). (Id.) The ADSs traded on the New York Stock Exchange ("NYSE") under the ticker CHR. (Id. at 1.) The offering was priced at CHF 82 per share, and $24.59 per ADS, with each ADS representing half of one share. (Id.) Third, there was an offering to institutional investors elsewhere in the form of shares and ADSs. (Id. at 10.)

The Prospectus discussed in great detail Converium's loss reserve estimates, the estimation process, the attendant uncertainties and the prospects that the reserve estimates could have to be changed. (See, e.g., Zach Decl. Exh. 5 at 122-23.) As the Prospectus explained, those "reserves are balance sheet liabilities representing estimates of future amounts required to pay claims and claim adjustment expenses for insured claims which have occurred at or before the balance sheet date, whether already known to us or not yet reported." (Id. at 121.) The Prospectus went on to explain that Converium used two approaches to analyze its reserves: (1) a bottom-up approach, which applied a number of standard actuarial reserving methods on a contract-by-contract basis, and (2) a top-down analysis, which aggregated the majority of Converium's businesses into a number of homogeneous classes and applied standard reserving techniques to those classes. (Id. at 122.) Through the use of those methods the company was able to produce a range of reserves and establish their reserve estimates at a

reasonable level within that range. (Id.) Nonetheless, despite the application of those methods, the Prospectus warned that "the establishment of loss reserves is an inherently uncertain process" and that "the ultimate cost of settling claims may exceed our existing loss and loss adjustment expense reserves, perhaps materially." (Id. at 123.)

The Prospectus reiterated what Converium had disclosed in the September 6, 2001 press release, namely that the company "determined to record in the first half of 2001 additional provisions of $112 million, net of reinsurance, principally related to accident years 2000 and prior at Converium North America". (Id.) The Prospectus also disclosed that "[d]uring the first half of 2001, Converium North America increased loss and loss adjustment reserves by approximately $125.0 million relating to accident years 2000 and prior." (Id. at 56.) Those additional reserves were "determined in accordance with [the company's] loss reserving policies", discussed above, with input from Tillinghast. (Id. at 123.) The Prospectus further stated that Tillinghast performed similar reviews of other insurers' reserves and was able to refer to its "proprietary loss development data" in performing its analysis of Converium's reserves. (Id.) Using that data, along with "several top-down approaches including their broad database of insurance and reinsurance loss trends" and previously unavailable fourth quarter 2000 and some first quarter 2001 data from Converium, Converium had learned and reported that there was "adverse loss development across several lines of [Converium's] business, mainly relating to general liability, commercial auto liability and umbrella policy business written in 1996 through 1999." (Id.) The Prospectus further disclosed that "Tillinghast has confirmed to us that our net reserves as of December 31, 2000 plus the first half of 2001 reserve strengthening correspond to Tillinghast's best estimate of our

liabilities for net loss and loss adjustment expenses as of December 31, 2000 for Converium on a historical combined basis." (Id.)

After the December 2001 offering, adverse loss experiences and new analyses led Converium to make a number of additional adjustments to its loss reserves for policies written in the years 2000 and earlier.

First, on May 23, 2002, five months after the initial public offering, Converium filed its 2001 annual report with the SEC on Form 20-F. In that report, the company disclosed that it "recorded an addition of $11.6 million of net adverse loss reserve development based on its year-end review of non-life reserves." (Zach Decl. Exh. 10 at 47.) That increase was based on positive reserve developments in certain parts of the company that offset significant loss reserve development elsewhere, including at Converium North America. As the Form 20-F explained, "Converium North America recorded adverse development of $39 million, mainly related to general liability, auto liability and umbrella business written in 1996 through 1999." (Id.) As disclosed in the earlier Registration Statement and Prospectus, Converium had increased its loss reserves for that same period based on its own reserve calculations and an analysis conducted by Tillinghast. (Zach Decl. Exh. 5 at 123.)

Second, on July 29, 2002, Converium announced its half year results. In summarizing those results, the company stated that "Converium Group's 2002 results were impacted as a result of the recognition of a US$ 24.4 million provision for net adverse loss development on prior years' business". (Zach Decl. Exh. 11 at 12.) That charge was attributable to the fact that "Converium Cologne recorded an additional US$ 18.5 million in reserves relating to prior years' business" and "Converium North

America recorded adverse loss development of US$ 19.9 million." (Id.) Those developments were "partially offset by positive reserve development of US$ 14.0 million in Converium Zurich." (Id.)

The half year results also stated that "[i]nsurance and reinsurance stocks were very much in favor during late 2001 and early 2002", but explained that "enthusiasm for our sector diminished during the second quarter 2002 due to the emergence of a number of industry-wide issues." (Id. at 7.) Among those developments was the fact that there were "[s]ignificant reserve adjustments for the underwriting years 1997 to 2000." (Id.) As disclosed in the Registration Statement and Prospectus, that was the same period for which Converium had increased its loss reserves estimate by $112 million in the first half of 2001.

Third, on October 28, 2002, Converium filed a Form 6-K with the SEC that set out its third quarter results. (Zach Decl. Exh. 12.) In that quarter, Converium's results were impacted by, among other things, "the recognition of US$ 59.6 million provision for net reserve development on prior years' business". (Id.) In particular, for "the three months ended September 30, 2002, Converium North America increased loss and loss adjustment reserves approximately US$ 47.0 million, primarily related to accident years 1997 and 2000." (Id.) Thus, in total, "[i]n the first nine months of 2002, [Converium] recorded a US$ 84.0 million provision for net reserve development on prior years' business". (Id.)

In connection with the announcement of its third quarter 2002 results, Converium issued a press release that further explained the loss reserve developments. The company explained that "[a]fter years of reporting significant net reserve releases,

many primary US insurance companies are now confronted with reserve insufficiencies relating to the soft market period of 1997-2000." (Zach Decl. Exh. 13 at 2.) As a result, Converium noted that it was "conducting further actuarial studies" and that "[p]reliminary findings suggest[ed] that additional reserve actions of up to US$ 75.0 million will be required for the 4th quarter 2002." (Id. at 3.)

After those third quarter 2002 results were announced, the ratings agencies immediately downgraded Converium. Moody's revised Converium's outlook from "Stable" down to "Negative". (Zach Decl. Exh. 14.) Moody's explained that it was taking that action because of the "modest earnings outlook for Converium following the company's announcement it will be strengthening reserves for the prior years' claims." (Id.) Likewise, Standard & Poor's revised its outlook on Converium from "Stable" to "Negative" and placed the company on Credit Watch. (Zach Decl. Exh. 15.) Standard & Poor's noted that "coming relatively soon after a fall actuarial review of Converium's business as at year-end 2000, the adverse development also underlines the continuing difficulty for insurers and reinsurers and their advisors in accurately reserving for prior year U.S. long-tail exposures." (Id.)

Fourth, on November 19, 2002, Converium announced details of the predicted additional provisions for prior years' business written by Converium North America from 1997 through 2000. (Zach Decl. Exh. 16.) In a press release, Converium stated that "Converium North America has finalized its loss reserve analysis that will result in the recording of additional provisions for losses . . . of US$ 70.3 million net for the fourth quarter 2002, which are in addition to the US$ 47.0 million that were recorded during the third quarter 2002." (Id. at 1.) The company further explained that "[t]hese

additional provisions are the result of the continued emergence of increased reported losses versus expected losses related to prior years." (Id.)

The allegations against the Underwriter Defendants end at the initial public offering. Plaintiffs do not assert that the Underwriter Defendants participated in any of the remaining allegations set forth in the Complaint, which involve events that extend into the summer of 2004.

Argument

I. COUNTS I AND III AGAINST THE UNDERWRITER DEFENDANTS ARE BARRED BY THE STATUTE OF LIMITATIONS APPLICABLE TO SECTION 11 AND SECTION 12(a)(2) CLAIMS.

Under the statute of limitations provisions of the 1933 Act, for plaintiffs' Section 11 and Section 12(a)(2) claims to be timely, they must have been "brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made", and in any event within three years after the security was offered or sold to the public. 15 U.S.C. § 77m. Here, plaintiffs brought suit against ZFS, Converium and certain of its officers and directors in October 2004, two months before the expiration of the maximum three-year statute of limitations against the Underwriter Defendants. However, no plaintiffs anywhere brought suit against UBS and Merrill until September 23, 2005, almost four years after Converium's initial public offering. Prior to that date, there was no class action claim against the underwriters that could have tolled the statute. In addition, no plaintiff or potential plaintiff save Rubin solicited or signed any tolling agreement with the Underwriter Defendants. Nor did any shareholder, plaintiff or potential plaintiff know about or rely upon the tolling agreement entered into between Mr. Rubin and the Underwriter Defendants. By the time these

plaintiffs knew of the Rubin Agreement, both the one-year inquiry notice statute of limitations and the three-year statute of limitations had expired.

A. The Tolling Agreement Entered Between UBS, Merrill and Michael Rubin Did Not Toll the Period for Assertion of Plaintiffs' Claims Against the Underwriter Defendants.

As plaintiffs are well aware, absent a tolling of the applicable three-year statute of limitations, plaintiffs' Section 11 and Section 12(a)(2) claims against the Underwriter Defendants are time-barred. Plaintiffs' contention that their claims against the Underwriter Defendants are subject to "an agreement that tolled the statute of limitations" (Compl. ¶ 245) is wrong. Plaintiffs never named the Underwriter Defendants as parties to this or any other litigation until they filed the Complaint on September 23, 2005, more than nine months after the limitations period expired on December 11, 2004. Accordingly, their claims against the Underwriter Defendants should be dismissed.

Presumably, the agreement plaintiffs reference in the Complaint is the tolling agreement entered into between Michael Rubin and the Underwriter Defendants dated December 9, 2004. (See Zach Decl. Exh. 1.) Plaintiffs, however, are not a party to or beneficiary of that agreement. They could not, and did not, rely upon its existence when declining to sue the Underwriter Defendants even after they had sued Converium and ZFS on claims of false loss reserves. Plaintiffs brought claims against ZFS, Converium and certain of its officers and directors in October 2004, and thereafter knowingly and intentionally allowed the time period with regard to these claims against the Underwriter Defendants to elapse. Prior to the December 11, 2004, expiration of the maximum three-year limitations period, no plaintiff solicited, signed or became a party to any agreement with the Underwriter Defendants to toll the statute. Not only did plaintiffs

and their counsel have no involvement in the negotiation or performance of the Rubin Agreement, they did not even know of its existence until long after the three-year limitations period had expired. They learned of the tolling agreement only when Rubin and his lawyer sought to contest the lead plaintiff and lead counsel structure agreed by the federal plaintiffs.

Tolling agreements represent a significant abridgment of a defendant's defenses and courts strictly construe them. See, e.g., Caguas Cent. Fed. Sav. Bank v. United States, 215 F.3d 1304, 1308-09 (Fed. Cir. 2000); Eisenberg v. Hughes, No. C97-2466 MJJ, 1999 WL 459358, at *5 (N.D. Cal. June 25, 1999). The express provisions in the Rubin agreement on which the plaintiffs now strategically seek to rely, as well as plaintiffs' conduct in this litigation, demonstrate that plaintiffs in this action are not party to the agreement, nor are they entitled to invoke its terms to allow untimely claims.

The Rubin tolling agreement expressly states that it is between the Underwriter Defendants and "Michael Rubin, individually, and as a representative of a class of all others who purchased shares or American Depository Shares . . .." (Zach Decl. Exh. 1 (emphasis added)). Likewise, "in consideration of the mutual covenants" of the parties, paragraph two of the agreement states that Rubin—and not lead plaintiffs or anyone else—"agrees not to name as defendants the Underwriters in any action asserting claims arising out of the underwriting of Converium's IPO for as long as the Agreement remains in effect." (Id. at ¶ 2 (emphasis added)). Without securing such forbearance, there was no reason for Underwriters to agree with Rubin to begin to toll the statute on a claim he might bring.

Plaintiffs in their conduct have not even attempted to maintain a pretense that they are a party to the Rubin Agreement and its terms. For example, the agreement prohibits the initiation of litigation against the Underwriter Defendants while the agreement is still in place. (Id. at ¶ 2.) Nonetheless, plaintiffs sued the Underwriter Defendants on September 23, 2005, while the agreement was still in effect (it was not terminated until December 12, 2005). In addition, termination of the agreement required notice to be sent to the parties. (Id. at ¶ 3.) Plaintiffs have never sent such notice to the Underwriter Defendants. If plaintiffs really were a party to the Rubin Agreement, they could and would have followed the clear procedures it sets forth. They did not even pretend to do so.[2]

Rubin—who plainly was the only shareholder party to the tolling agreement and the only shareholder party to the mutual covenants—later served the Underwriter Defendants with notice of termination pursuant to paragraph three of the agreement on November 11, 2005. (Zach Decl. Exh. 3.) Thirty days after service of that notice, any tolling effect of that agreement ended and Rubin filed suit against the Underwriter Defendants in New York State court on December 12, 2005. (Zach Decl. Exh. 4.)

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[2] Even if plaintiffs were a party to the Rubin Agreement—and they are not—their failure to adhere to even its most basic terms amounts to a material breach of the agreement that negates their rights to enforce any of its provisions against the Underwriter Defendants. See, e.g., Tractebel Energy Mktg., Inc. v. AEP Power Mktg., Inc., 03 Civ. 6731 (HB), 2005 WL 1863853, at *7 (S.D.N.Y. Aug. 8, 2005) (citing Computer Possibilities Unlimited, Inc. v. Mobil Oil Corp., 301 A.D.2d 70, 79, 747 N.Y.S.2d 468, 476 (1st Dep't 2002) ("A party who materially breaches or repudiates a contract cannot enforce it . . ."); Restatement (Second) of Contracts § 253(2) (1981).

Plaintiffs in this action cannot reasonably argue that they are a party to a tolling agreement that does not mention them and that they did not solicit, sign, comply with, or even know about until the applicable limitations period had passed.

B. Plaintiffs Were on Inquiry Notice for Purposes of the One-Year Statute of Limitations—at the Latest—by November 17, 2002.

Likewise, the shorter one-year inquiry notice statute of limitations has expired. Indeed, it expired before Rubin sought an individual tolling agreement and this means the new Rubin action in state court and this action are barred on statute of limitations grounds. Under Section 13 of the 1933 Act, "when the circumstances would suggest to an investor of ordinary intelligence the probability that she has been defrauded, a duty of inquiry arises". Dodds v. Cigna Sec. Inc., 12 F.3d 346, 350 (2d Cir. 1993); see also Jackson Nat'l Life Ins. Co. v. Merrill Lynch & Co., Inc., 32 F.3d 697 (2d Cir. 1994) (claims arising under sections 11 and 12(a)(2) dismissed as time barred because plaintiffs were on inquiry notice); White v. H & R Block, Inc., No. 02 Civ. 8965 (MBM), 2004 WL 1698628, *4 (S.D.N.Y. July 28, 2004). In order to trigger the running of the one-year statute of limitations, a plaintiff need only be aware of "the facts forming the basis of his cause of action, . . . not that of the existence of the cause of action itself." Jensen v. Snellings, 841 F.2d 600, 606 (5th Cir. 1988) (internal quotation marks omitted); see also White, 2004 WL 1698628, at *5 (holding storm warnings do not necessitate that plaintiffs be able "to learn the precise details of the fraud . . . [t]hey need only be capable of perceiving the general fraudulent scheme based on the information available to them")(internal quotation marks omitted). In other words, the one-year statute of limitations begins to run as soon as a plaintiff has inquiry notice in the form of "storm

warnings" that would alert a reasonable person to the possibility of an alleged violation. Jensen, 841 F.2d at 607.

In this action, plaintiffs assert that the Registration Statement and Prospectus were misleading because "Converium was under-reserved by at least $225 million at the time of the IPO, and the Company's reserves were not reasonable estimates based on the information known at the time." (Compl. ¶ 147.)[3] That deficiency was, according to plaintiffs' allegations, attributable to reinsurance policies underwritten by ZFS's reinsurance businesses from 1997 through 2000. (See Compl. ¶¶ 73-74, 77-78.) While the Registration Statement and Prospectus disclosed that Converium had increased its reserves by net $112 million for that same business (Zach Decl. Exhs. 5 at 123 & 8 at 123-24), plaintiffs allege that that increase was insufficient in size and that Converium needed to increase its reserves by an additional $225 million (Complaint ¶ 95). As discussed below, however, that number is belied by later allegations in the Complaint that demonstrate that the complained of deficiency was—at the most—on the order of $45 million.

Plaintiffs' assertion that "[l]ess than one year elapsed from the time that Plaintiffs discovered or reasonably could have discovered the facts upon which this

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[3] Plaintiffs' other allegations that statements in the initial public offering were misleading are reformulations of the same reserve deficiency. All those alleged misstatements on the offering flow directly from the alleged $225 million reserve deficiency: (1) Converium's $60 million reported loss for the first half of 2001 (plaintiffs' claim the loss should have been "at least $285 million"); (2) Converium's shareholders' equity was overstated by $225 million as result of the alleged $225 million understatement of reserves; (3) Converium's non-life combined ratio for the first half of 2001 was "materially understated as a result of the Company's reserve deficiency"; and (4) warnings that Converium's reserves "may prove to be inadequate to cover [its] actual losses" were misleading because those reserves were already deficient. (Compl. ¶¶ 143 & 148.)

complaint is based to the time that the first complaint was filed asserting claims arising out of the falsity of the Registration Statement" is simply conclusory argument and is irrelevant to Underwriter Defendants, who were not defendants on the "first complaint". (Compl. ¶ 245.)

(1) The fact that Converium raised its reserves four times within one year of the offering placed plaintiffs on inquiry notice.

The Complaint and Converium's own public disclosures, however, establish that plaintiffs were fully aware as of November 17, 2002—at the latest—that the estimated loss reserves set out in the offering documents had been too low. By that time, it was clear that Converium had reserve deficiencies attributable to business underwritten between 1997 and 2000 that had repeatedly caused it throughout 2002 to increase its loss reserve estimates above the amount stated in the December 2001 initial public offering. In fact, within a year of the initial public offering, Converium raised its reserves relating to prior years' business four times in increasing net amounts of $11.6 million, $24.4 million, $59.6 million and $70.3 million. (See Zach Decl. Exhs. 10 at 47, 11 at 12, 12 & 16 at 1.) All those increases—which total $165.9 million—relate to business underwritten in 2000 and earlier. In fact, the net $165.9 increase during 2002 exceeds the $112 million increase that was taken by Converium in the first half of 2001 for business underwritten in 2000, and disclosed and discussed in detail in the Registration Statement and Prospectus.

For Converium's North American business in particular, the subsequent loss reserve increases during 2002 were for $39.0, $19.9 million, $47.0 million and $70.3 million, which totals $176.2 million. (Id.) That markedly exceeds the $125 million charge taken by Converium in the first half of 2001 for business underwritten in 2000 and

earlier. Moreover, the $176.2 million increase amounts to over three-fourths of the additional reserve charge of $225 million that plaintiffs allege, with the benefit of hindsight, should have been added to the loss reserves prior to the initial public offering. (See Compl. ¶ 95.) Thus, as of November 19, 2002, plaintiffs plainly were on inquiry notice that Converium's stated loss reserves for business it had underwritten in 2000 and earlier, as disclosed in the September 6, 2001 press release and the offering documents, were insufficient.

Under the Second Circuit's decision in LC Capital Partners, LP v. Frontier Ins. Group, Inc., 318 F.3d 148 (2d Cir. 2003), these facts make it clear—as a matter of law—that plaintiffs were on inquiry notice after those reserve increases were announced. In LC Capital Partners, the Court of Appeals addressed whether "plaintiffs, suing for stock fraud, were on inquiry notice that started the running of a statute of limitations early enough to render their suit time-barred" (id. at 150) in an action against an "insurance company that took increasingly large reserve charges and did not disclose its continuing failure to establish adequate reserves." Id.. Plaintiffs there alleged, among other things, that Frontier—an insurance company—"implemented reserve policies with the deliberate purpose and systematic effect of under-reserving for claims." Id. Those claims, the Court of Appeals concluded, were time-barred because Frontier had, over the course of four years, taken loss reserve charges in amounts of $17.5 million, $40 million and $139 million. Id. at 155. The Second Circuit held that "a series of three charges in substantial and increasing amounts for the same purpose within four years should alert any reasonable investor that something is seriously wrong" (id.)and the dismissal of plaintiffs' claims by the district court was, therefore, affirmed. Id. at 157. In this case,

four substantial charges totaling $165.9 million for Converium, and $176.2 million for its North American business, were announced over a six-month period (not four years), which leaves no room for plaintiffs to pretend they were not on inquiry notice.

(2) Public statements made by Converium and its senior management in 2002 put plaintiffs on inquiry notice.

In addition to Converium's loss reserve charges in 2002, public statements by Converium and its senior management also sufficed to place plaintiffs on inquiry notice as to claims that Converium's stated reserves for business underwritten in 2000 and earlier, as disclosed in its earlier public statements, were materially incorrect.

First, in its 2001 annual report issued in March 2002, the significant loss reserve charge Converium took for its North American business related directly to the alleged loss reserve deficiency plaintiffs assert is "fundamental" to their allegations in the Complaint. Converium's Form 20-F clearly explained that the $39 million charge taken by Converium North America "mainly related to general liability, auto liability and umbrella business written in 1996 through 1999." (Zach Decl. Exh. 10 at 47.)

Second, in reporting its 2002 half year results (and announcing its first reserve increase of net $24.4 million), Converium stated that enthusiasm for its stock (and the stock of other insurance and reinsurance companies) was waning because of "the emergence of a number of industry-wide issues." (Zach Decl. Exh. 11 at 7.) Among those issues was the fact that Converium—and others—were taking "[s]ignificant reserve adjustments for the underwriting years 1997 to 2000." (Id.) Those are the business years for which plaintiffs assert Converium failed to take sufficient reserves prior to the initial public offering. (See Compl. ¶¶ 73-74, 77-78.)

Third, in announcing its 2002 third quarter results on October 28, 2002, Converium again elaborated on issues it was facing with regard to business underwritten in 2000 and earlier. Converium explicitly stated that it was confronting exactly the same reserve deficiency problem on which plaintiffs now seek to base their claims: "US insurance companies are now confronted with reserve insufficiencies relating to the soft market period of 1997-2000." (Zach Dec. Exh. 13 at 2.) Dirk Lohmann, Converium's CEO, stated that the reserve insufficiencies were for business "we left long behind us" and a problem that he "would rather not face". (Id. at 4.)

Fourth, Lohmann reiterated the fact that Converium was addressing its reserve deficiency for prior years' business in a November 17, 2002 press release. (Zach Decl. Exh. 16 at 1-2.) Again, his statements explicitly publicized in 2002 the problem plaintiffs allege was not disclosed until summer 2004—namely that Converium repeatedly experienced loss reserve deficiencies for business underwritten between 1997 and 2000 and that the loss reserve estimates as of December 2001 were too low.

There is simply no avoiding the fact that Converium expressly and publicly disclosed its problem with insufficient reserves for the historic business it had underwritten between 1997 and 2000—the business plaintiffs now claim was inadequately reserved in the December 2001 offering.

(3) Moody's and Standard & Poor's downgraded Converium in October 2002.

Others understood what plaintiffs now pretend had not been disclosed. Immediately following Converium's October 28, 2002, announcement that it was increasing its reserves by $59.6 million, and that it likely would have to raise reserves another $75 million in the fourth quarter of 2002, the major ratings agencies monitoring

Converium downgraded the company. (Zach Decl. Exhs. 14 & 15.) Both Moody's and Standard & Poor's downgraded their outlooks for Converium from "Stable" to "Negative". As Moody's explained, the downgrade was based on a "modest earnings outlook for Converium following the company's announcement that it will be strengthening reserves for the prior years' claims." (Zach Decl. Exh. 14.) Likewise, Standard & Poor's noted that "coming relatively soon after a fall actuarial review of Converium's business as at year-end 2000, the adverse development also underlines the continuing difficulty for insurers and reinsurers and their advisors in accurately reserving for prior year U.S. long-tail exposures." (Zach Decl. Exh. 15.)

Thus, the market was well aware of the fact that—as of October 28, 2002—there were significant adequacy problems with Converium's reserves for business written in 2000 and earlier. That was sufficient to place plaintiffs on inquiry notice. See, e.g., Shah v. Morgan Stanley, No. 03 Civ. 8761 (RJH), 2004 WL 2346716, *9-11 (S.D.N.Y. Oct. 19, 2004) (plaintiff is on inquiry notice where articles described the alleged misconduct); White, 2004 WL 1698628, at *7.

(4) Lead counsel for plaintiffs has admitted that the alleged reserve insufficiencies were disclosed in October 2002 and caused their client to sell at a loss.

Lead plaintiffs' counsel represented to the Court that the alleged fraud was disclosed, in material part, in October 2002. In his August 22, 2004 letter to the Court, lead plaintiffs' counsel wrote—in reference to Converium's October 28 press release announcing its third loss reserves increase—that his client "sold more than a third of the ADSs purchased on the IPO at a loss following the partial disclosure of Converium's true reserve position, which was misrepresented in the registration statement and prospectus." (Zach Decl. Exh. 17, at pg. 2, n.1) According to lead counsel for plaintiffs, that "partial

disclosure" was enough to disclose the earlier misrepresentation, to cause the stock price to fall and to cause an actionable loss to his client from the false statements in the initial public offering. Thus, it was also plainly enough to put plaintiffs on inquiry notice and start the running of the one-year statute. See Jensen, 841 F.2d at 606 (inquiry notice requires only "the facts forming the basis of [a] cause of action, . . . not that of the existence of the cause of action itself") (emphasis on original); White, 2004 WL 1698628, at *5 (storm warnings do not necessitate that plaintiffs be able "to learn the precise details of the fraud . . .. They need only be capable of perceiving the general fraudulent scheme based on the information available to them") (internal quotation marks omitted).

(5) Even plaintiffs admit that the alleged fraud was completely disclosed as of September 2, 2004—more than a year before suit.

Even if the alleged misstatements were not fully disclosed by November 17, 2002, plaintiffs' proposed class period ends on September 2, 2004. By that point, Converium's ADSs were trading at $8.86, down from their original offering price of $24.59. (Compl. ¶ 216.) Moreover, two months prior to the end of the proposed class period, on July 20, 2004, Converium had, according to plaintiffs, "shocked the financial markets by announcing that the Company would incur a $400 million charge in order to effect a reserve increase at Converium North America on policies written for the United States in 1997-2001." (Id. at ¶ 208.) Subsequently, additional reserve increases were taken (id. at ¶ 215) and Converium suffered another ratings downgrade. (Id. at ¶ 216) In other words, by any standard, the alleged fraud was fully disclosed. But, September 2, 2004, is also more than one year before anyone sued the underwriters. These claims are time-barred.

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For all of the reasons discussed above, plaintiffs were on inquiry notice—at the latest—as of November 17, 2002. Because they failed to bring claims against UBS and Merrill until September 2005, Counts I and III against the Underwriter Defendants are time-barred and should be dismissed.

C. The Underwriter Defendants Intend to Make a 12(b)(1) Motion.

The Underwriter Defendants' present motion seeks dismissal of Counts I and III against them in their entirety. Plaintiffs assert these 1933 Act class action claims on behalf of U.S. purchasers that bought ADSs in the initial public offering or thereafter on the NYSE. Purportedly under the judicially prescribed 'conduct test', plaintiffs also assert claims on behalf of "foreign class members who acquired Converium stock on the SWX". (Compl. ¶ 9.) This Court, however, lacks subject matter jurisdiction over claims of non-U.S. Converium shareholders who purchased Converium shares outside the United States. The Underwriter Defendants will make a 12(b)(1) subject matter jurisdiction motion with respect to those foreign purchaser claims at an appropriate time when any resulting demands for discovery by plaintiffs will not have the potential to delay resolution of this dispositive motion.

II. COUNTS I AND III FAIL TO STATE A CLAIM BECAUSE THE UNDERWRITER DEFENDANTS WERE ENTITLED TO RELY UPON THE EXPERTISED PORTIONS OF THE REGISTRATION STATEMENT AND PROSPECTUS.

The Underwriter Defendants are entitled to rely upon the expert opinions proffered in the allegedly false or misleading portions of the Registration Statement and Prospectus. Section 11 provides an explicit safe harbor for underwriters who rely in good faith on the expertised portions of a registration statement. 15 U.S.C. § 77k(b)(3)(C).

That safe harbor has also been applied to the due diligence standard applied under Section 12. See In re Worlds of Wonder Sec. Litig., 814 F. Supp. 850, 867-68 (N.D. Cal. 1993), aff'd, 35 F.3d 1407 (9th Cir. 1994); see also In re Worldcom, Inc. Sec. Litig., 346 F. Supp. 2d 628, 663 (S.D.N.Y. 2004); Lorber v. Beebe, 407 F. Supp. 279, 285 (S.D.N.Y. 1976). Under the safe harbor, absent any "red flags" underwriters are not required to perform due diligence regarding the expertised portions of a registration statement or prospectus to avail themselves of this defense. See In re Worldcom, 346 F. Supp. 2d at 672; In re Worlds of Wonder, 814 F. Supp. at 867-68.[4]

(1) The Underwriter Defendants were entitled to rely upon Tillinghast and PricewaterhouseCoopers.

In this action, Converium's loss reserve estimates were analyzed by an expert actuarial firm, and Converium's financial statements incorporating those loss reserve estimates were audited by independent accountants. The Underwriter Defendants were entitled to rely upon their work and a claim is not stated because such numbers were included, as they had to be, in the offering documents and were later changed.

First, as plaintiffs themselves explain in the Complaint, the alleged "fundamental fraud at issue here relates to Converium's reserves". (Compl. ¶ 11.) Converium's reserves were analyzed by Tillinghast, an internationally known actuarial firm, and Tillinghast confirmed in the Registration Statement and the Prospectus that the company's reserves corresponded to its "best estimate". (Zach Decl. Exhs. 5 at 123 & 8

[4] Although due diligence is a defense under Section 11 and Section 12, "the Court may dismiss a claim pursuant to a Rule 12(b)(6) motion when an affirmative defense appears on the face of the complaint". In re WRT Energy Sec. Litig., 96 Civ. 3610 (JFK), 2005 WL 323729, at *6 (S.D.N.Y. Feb. 9, 2005).

at 123-24.) Specifically, the Registration Statement and the Prospectus disclosed:

> Based on the Tillinghast analysis, which reflected certain information that became available after the issuance of our December 31, 2000 financial statements and based on our own evaluations of these new developments, we determined to record in the first half of 2001 additional provisions of $112 million, net of reinsurance, principally related to accident years 2000 and prior at Converium North America. Tillinghast has confirmed to us that our net reserves as of December 31, 2000 plus the first half of 2001 reserve strengthening correspond to Tillinghast's best estimate of our liabilities for net loss and loss adjustment expenses as of December 31, 2000 for Converium on a historical combined basis.

(Id.) Tillinghast consented to the inclusion of the conclusions of its actuarial analysis in the Registration Statement (Zach Decl. Exh. 9), thus making that analysis an expert opinion for purposes of the 1933 Act. 15 U.S.C. § 77k(a)(4) (expert defined as "any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any report or valuation which is used in connection with the registration statement . . .").

The Underwriter Defendants were not required to perform the actuarial analysis required to determine or adjust Converium's loss reserves, and even plaintiffs do not attempt to claim otherwise. As the Second Circuit has explained, calculation of a reinsurance company's loss reserves is conducted through the use of three actuarial methods that are well known in the reinsurance industry. Delta Holdings, Inc. v. Nat'l Distillers & Chem. Corp., 945 F.2d 1226, 1229 (2d Cir. 1991). Those methods—described at length in the Delta Holdings opinion—involve the application of complex actuarial tests that often rely on the professional judgment of an experienced actuary. Id. at 1229-30. There is no dispute that such complex actuarial work is the bailiwick of actuarial experts such as Tillinghast, not the Underwriter Defendants.

Second, Plaintiffs assert that the alleged understatement of loss reserves had "a direct impact on Converium's financial results" that were publicly reported in the company's financial statements. (Compl. ¶¶ 61-67.) They are correct but this simply ignores the fact that PricewaterhouseCoopers, the company's outside accountants, audited and certified the company's financial statements—which included the Company's loss reserve estimates. (Zach Decl. Exh. 5 at 198.) The Underwriter Defendants were entitled—as a matter of law—to rely upon the expert opinion proffered by PricewaterhouseCoopers on the financial statements now challenged by plaintiffs as having understated in December 2001 Converium's loss reserves. The underwriters simply are not required to re-audit an issuer's financial statements themselves. See In re Software Toolworks, Inc. Sec. Litig., 789 F. Supp. 1489, 1498 (N.D. Cal. 1992).

(2) Plaintiffs allege no "red flags".

Plaintiffs do not allege any facts that indicate, or even suggest, that the Underwriter Defendants had or should have had any reason in December 2001 to believe that the Tillinghast actuarial analysis and PricewaterhouseCoopers' audit of the financial statements contained material misstatements or omissions on the now challenged loss reserve estimates.[5] As Judge Cote stated in her opinion in the WorldCom litigation,

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[5] The Court of Appeals has applied the particularity requirements of Fed. R. Civ. P. 9(b) to 1933 Act claims that sound in fraud. See Rombach v. Chang, 355 F.3d 164, 171 (2d Cir. 2004) ("We hold that the heightened pleading standard of Rule 9(b) applies to Section 11 and Section 12(a)(2) claims insofar as the claims are premised on allegations of fraud."). Plaintiffs cannot evade those pleading requirements simply by stating—as co-lead plaintiffs do in the Complaint (Compl. ¶¶ 238, 260)—that their Section 11 and Section 12 claims "do not sound in fraud". See Rombach, 355 F.3d at 172. Here, plaintiffs' 1933 Act claims are premised on the same allegations used to support their 1934 Act fraud claims and, therefore, those claims plainly do sound in fraud and must comply with Rule 9(b) pleading requirements. See id. at 172 (allegations that "Registration statement was 'inaccurate and misleading'; that it contained 'untrue statements of material facts'; and that 'materially false and misleading written statements

underwriters are permitted to rely on experts unless there is evidence of "red flags" regarding the reliability of those expert opinions. In re Worldcom, 346 F. Supp. 2d. at 672. According to Judge Cote, for purposes of Section 11 and Section 12 claims, a "red flag" is "[a]ny information that strips a defendant of his confidence in the accuracy of those [expertised] portions . . .". Id. at 673.

In the Complaint, plaintiffs not only fail to allege any "red flags", they do not make a single substantive factual allegation relating to the Underwriter Defendants. Plaintiffs reference the Underwriter Defendants in only three places: (1) in the list of parties to the action (Compl. ¶¶ 34-36); (2) in a two paragraph discussion of the number of shares sold in Converium's initial public offering, the underwriters' fees for that offering and their exercise of the overallotment (id. at ¶¶ 93-94); and (3) in the recitation of the elements necessary to make out Section 11 and Section 12 claims in the "Claims for Relief" portion of the Complaint. (Id. at ¶¶ 237-247, 259-267)

There is not a single reference in the Complaint that relates to the conduct of the Underwriter Defendants or any employee of the Underwriter Defendants. Plaintiffs do not make any allegation—factual or conclusory—that the Underwriter Defendants acted in bad faith or with any improper motive. Moreover, there is no suggestion that the Underwriter Defendants were even aware of any piece of information that undermined or should have undermined their necessary and statutorily endorsed reliance upon Tillinghast and PricewaterhouseCoopers, much less any specific factual

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were issued'" sound in fraud); see also Cent. Laborers Pension Fund v. Merix Corp., No. CV04-826-MO, 2005 WL 2244072, at *5 (D. Or. Sept. 15, 2005); In re Van Wagoner Funds, Inc. Sec. Litig., No. C 02-03383 JSW, 2004 WL 2623972, at *2 (N.D. Cal. July 27, 2004).

allegation indicating any awareness of deficiencies or of untrue statements regarding loss reserves. The only mention of the Underwriter Defendants' reliance upon those expert opinions is in the "Claims for Relief" section, and it is a wholly conclusory and non-factual assertion that is legally irrelevant: "[t]he Underwriter Defendants did not make a reasonable investigation or possess reasonable grounds to believe that the statements contained in the Registration Statement were true and without omissions of any material facts and were not misleading." (Id. at ¶ 242.)

Plaintiffs do not accuse Tillinghast or PricewaterhouseCoopers of wrongdoing, despite the fact that they were the experts directly responsible for the complex actuarial analysis of Converium's reserves and incorporation of those reserves into the company's financial statements. Nor do plaintiffs allege that Tillinghast or PricewaterhouseCoopers acted inappropriately in expertising the company's estimates of loss reserves that were included in the offering documents.

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On plaintiffs' own alleged facts, the Underwriter Defendants plainly were allowed as a matter of law to rely on the expert opinions proffered by Tillinghast and PricewaterhouseCoopers. The only factual allegation about either UBS or Merrill relates to the fully disclosed fee they charged and the number of shares they sold. Plaintiffs point to no "red flags" that might even arguably negate the Underwriter Defendants' right to rely on those experts, and plaintiffs make no claims that those experts were unreliable in evaluating the loss reserves.

III. COUNTS I AND III SHOULD BE DISMISSED BECAUSE THE ALLEGED MISREPRESENTATION ON THESE COUNTS WAS NEITHER MATERIAL NOR FALSE.

The Second Circuit has explained that an alleged omission "is material if there is 'a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the total mix of information made available.'" Halperin v. eBanker USA.com, Inc., 295 F.3d 352, 357 (2d Cir. 2002) (quoting Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1988) (citation and internal quotations omitted)). "A fact is to be considered material if there is a substantial likelihood that a reasonable person would consider it important in deciding whether to buy or sell shares." Halperin, 295 F.3d at 357.

A. Plaintiffs Fail Adequately To Allege that Converium's Loss Reserve Estimates Were Deficient.

In the Complaint, plaintiffs fail to adequately plead that Converium's loss reserves were deficient. The calculation of loss reserves, as the Second Circuit explained in the Delta Holdings case, is "based in large part upon informed guesswork." Delta Holdings, 945 F.2d at 1231. Their measurement is—at best—an estimate:

> It must be emphasized that no actuarial method is so accurate that it eliminates conjecture in the calculation of IBNR liabilities. Even case reserve decisions involving reported claims entail uncertainty as to the amount of final loss.

Id. at 1231. That is why both the Registration Statement and Prospectus stated in their respective "Risk Factors" sections that the company's "[l]oss reserves do not represent an

exact calculation of liability, but rather are estimates of the expected cost of the ultimate settlement of losses." (Zach Decl. Exhs. 5 at 14 & 8 at 13.)[6]

Plaintiffs' claims against the Underwriter Defendants are based solely on their assertion that Converium's loss reserve estimates were untrue because they departed materially from Tillinghast's estimate as to their proper amount. (See Compl. ¶¶ 86-87.) In the Complaint, plaintiffs initially assert that "[i]n or about April 2001, Tillinghast presented the results of its study, which showed that the reserves maintained by Zurich Re (North America) were deficient by approximately $350 million." (Id. ¶ 82.) That alleged deficiency, as the Complaint goes on to assert, was a preliminary estimate that was later reduced to $186 million. (Id. at ¶ 86.) The $186 million number alleged by plaintiffs is also incorrect. Tillinghast actually concluded that loss reserves were deficient by $162 million for North America, and $156.5 million overall. (See Redman

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[6] The offering documents contained numerous additional warnings as to the uncertainty attendant to calculating loss reserves:

> Because estimation of loss reserves is an inherently uncertain process, quantitative techniques frequently have to be supplemented by professional and managerial judgment . . ..
>
> The uncertainty inherent in loss estimation is particularly pronounced for long-tail lines such as umbrella, general and professional liability and motor liability, where information, such as required medical treatment and costs for bodily injury claims, will only emerge over time. In the overall reserve setting process, provisions for economic inflation and changes in the social and legal environment are considered. The uncertainty inherent in the reserving process for primary insurance companies is even greater for the reinsurer . . ..
>
> [S]ince the establishment of loss reserves is an inherently uncertain process, the ultimate cost of settling claims may exceed our existing loss and loss adjustment expense reserves, perhaps materially.

(Zach Decl. Exh. 5 at 122-23.)

Decl. Exh. A at 5.) In fact, Converium ultimately raised reserves by $125 million for North America, and $112 million overall, which Tillinghast certified "corresponded" to its best estimate. (See Zach Decl. Exh. 5 at 123.)

In the Complaint, plaintiffs do not allege that Tillinghast's "best estimate" was in fact wrong. Instead, plaintiffs attempt to make much of a difference between Tillinghast's report and Converium's announced reserves increase by claiming a fifty percent discrepancy. (See Compl. ¶ 86.) That is misleading. Converium, at the time of the Tillinghast analysis estimate, carried reserves in excess of $3.1 billion. (See Redman Decl. Exh. A at 6.) The $44.5 million difference between Tillinghast's analysis of Converium's loss reserves and Converium's announced reserves increase is a difference of slightly more than one percent in Converium's loss reserves. That difference, in light of the fact that loss reserves are emphatically uncertain estimates, and of the warnings in the offering documents repeating that caution, is not material to Converium's overall business and loss reserves. See In re CIT Group, Inc. Sec. Litig., 349 F. Supp. 2d 685, 689-90 (S.D.N.Y. 2004) (noting that plaintiffs' allegation that company understated reserves was "further undercut" by express warnings in the prospectus).[7]

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[7] In addition, courts have stated that "[i]t would seem rather beyond argument that such projections [as loss reserve estimates] about the company's future economic health are forward-looking". In re Kindred Healthcare, Inc. Sec. Litig., 299 F. Supp. 2d 724, 738 (W.D. Ky. 2004); Hess v. Am. Physicians Capital Inc., No. 5:04-CV-31, 2005 WL 459638, at *7 (W.D. Mich. Jan. 11, 2005). In this case, the Registration Statement and Prospectus warned that "loss reserves may not adequately cover future losses and benefits" and, as noted above, those documents contained extensive meaningful cautionary language relating to loss reserves. Thus, the "bespeaks caution" doctrine dictates that plaintiffs' alleged misrepresentations "are immaterial as a matter of law because it cannot be said that any reasonable investor would consider them important in light of adequate cautionary language set out in the same offering." Halperin, 295 F.3d at 357; see also P. Stolz Family P'ship L.P. v. Daum, 355 F.3d 92, 96 (2d Cir. 2004) ("A defendant may not be liable under § 12(a)(2) for misrepresentations in a prospectus if the alleged misrepresentations were sufficiently balanced by cautionary language within the

Converium established its loss reserve estimates well within the range of estimates calculated by Tillinghast. The "low" for Converium's reserves was set at $3.010 billion with a "high" of $3.716 billion. After raising reserves $112 million, Converium had a total of $3.256 billion in loss reserves, which is $245 million more than Tillinghast's floor estimate. (Redman Decl. Exh. A at 6.)

B. Plaintiffs Fail to Allege that the Underwriter Defendants—or Any Other Defendant—Knew or Believed that Converium's Loss Reserve Estimates Were Wrong.

Plaintiffs have not alleged—as they must—that the Underwriter Defendants, or any of the other defendants, knew or had any basis to believe that Converium's loss reserves were inadequate in December 2001. It is indisputable that calculations of loss reserves are estimates for purposes of the securities laws. See Delta Holdings, 945 F.2d at 1231 (loss reserves "based in large part upon informed guesswork"). Despite the fact that they are estimates, "the adequacy of loan loss reserves could be actionable if it is alleged that defendants did not actually believe that loan loss reserves were adequate, or if defendants had no reasonable factual basis for their belief." In re CIT Group, 349 F. Supp. 2d. at 690; see also Virginia Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1092-93 (1991); In re IBM Corp. Sec. Litig., 163 F.3d 102, 108-9 (2d Cir. 1998); Nolte v. Capital One Fin. Corp., 390 F. 3d 311, 315-16 (4th Cir. 2004).

The Complaint, however, does not contain a single factual allegation asserting that the Underwriter Defendants knew or had any basis to believe that Converium's loss reserves were inadequate in December 2001. Instead, Tillinghast

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same prospectus such that no reasonable investor would be misled about the nature and risk of the offered security.").

analyzed Converium's loss reserves and concluded that those loss reserves "corresponded" with their "best estimate". (Zach Decl. Exh. 5 at 123.) There is no allegation that Tillinghast knew or believed in 2001 that its conclusion was wrong. Likewise, there is no allegation that the Underwriter Defendants knew, or had any factual basis to know, that the loss reserve estimates disclosed in the Registration Statement and Prospectus were wrong.

The most that can be said about plaintiffs' allegations is that the Underwriter Defendants included in the December 2001 initial public offering documents loss reserve estimates that turned out to be wrong—they were too low and were adjusted upward in 2002 and subsequent periods. That does not allege that these defendants knew the reserves were inadequate when included in the offering documents with the extended description of the uncertainties attendant to the calculation of loss reserve estimates. The Underwriter Defendants cannot properly be found liable for including a loss reserve estimate that they are not alleged to have disbelieved and that was externally analyzed and confirmed by outside experts.

Beyond the absence of allegations about the Underwriter Defendants, the Complaint contains no allegation that the other defendants, sued for fraud in 2004, did not believe the loss reserve estimates set forth in the Registration Statement and Prospectus. Nowhere do plaintiffs include any allegation that any of the other defendants knew that a $225 million deficiency existed.[8] Likewise, the Complaint makes no

[8] The only allegation plaintiffs make as to who believed the loss reserves were inaccurate relates to certain unidentified "senior management". (See Compl. ¶ 86.) Those persons are not identified, nor is there any factual basis provided to support their alleged knowledge.

allegation that Confidential Witness No. 1—who is claimed to have "negotiated" with Tillinghast—aided or abetted a scheme to trick Tillinghast into certifying a false number. Nor does the Complaint allege that any specific information was withheld from Tillinghast, or that any part of Converium's business was distorted to mislead them. Instead, that anonymous witness asserts only that "we pulled out every stop" and "worked them to death", without even suggesting they acted inappropriately with regard to Tillinghast. (See Compl. at ¶ 29.) The Complaint alleges nothing more than negotiations between Converium and Tillinghast as to what the appropriate estimate of the company's loss reserves should then be. That does not state a claim for an alleged misstatement by anybody of Converium's loss reserve estimates in December 2001. See In re CIT Group, 349 F. Supp. 2d at 690 (defendant must actually believe loss reserves are not adequate, or have no reasonable basis for its belief, for an estimate to be actionable).

IV. CO-LEAD PLAINTIFF AVALON HOLDINGS INC. AND OTHER PURCHASERS OF CONVERIUM SHARES ABROAD CANNOT TRACE THEIR SHARES TO THE U.S. REGISTRATION STATEMENT AND SHOULD BE DISMISSED.

Avalon Holdings Inc. ("Avalon") is a named plaintiff on the Complaint whose individual claim illustrates that it and other purchasers of Converium shares abroad cannot trace their shares back to the Registration Statement because that SEC filing explicitly does not apply to them or the shares they purchased. It is well established that to make out a claim under Section 11, a plaintiff must be able to trace their shares back to the registration statement that they allege contains a material misrepresentation or omission. See DeMaria v. Anderson, 318 F.3d 170, 176 (2d Cir. 2003); Barnes v. Osofsky, 373 F.2d 269, 271 (2d Cir. 1967). Plaintiffs bear the burden of

explicitly pleading that they purchased shares that are in fact traceable to the allegedly false registration statement. See Ciresi v. Citicorp, 782 F. Supp. 819, 823 (S.D.N.Y. 1991); Lorber, 407 F. Supp. at 286-87.

In this case, the Form F-1 filed by Converium with the SEC explicitly carved out from the Registration Statement purchasers of Converium shares abroad that plaintiffs assert are bringing a Section 11 claim against the Underwriter Defendants. Specifically, the Registration Statement stated that "[o]ffers and sales of registered shares and American Depositary Shares outside the United States are being made pursuant to Regulation S and are not covered by this Registration Statement." (Zach Decl. Exh. 8. at cover page.) As the Prospectus explained, the global offering of Converium shares was divided into three offerings: (1) "a public offering of shares in Switzerland"; (2) "a public offering in the United States in the form of shares or ADSs"; and (3) "an offering to institutional investors elsewhere in the form of shares and ADSs". (Zach Decl. Exh. 5, at 10.)

Co-lead plaintiff Avalon is "an institution based in Athens, Greece" that purchased Converium shares abroad. (See Mem. of Law in Support of Mot. of Avalon Holdings Inc. and Richard Schneider for Consolidation, Appointment as Lead Pls. and Approval of Choice of Lead Counsel, dated December 3, 2004, at 5.) Because Avalon bought its shares on the SWX, an internationally recognized exchange with its own regulatory scheme for issuing securities, it necessarily cannot trace those shares to the Form F-1 Registration Statement, which explicitly does not apply to shares purchased or traded abroad. As the Second Circuit explained in the DeMaria case, "we read § 11's plain language to state unambiguously that a cause of action exists for any person who

purchased a security that was originally registered under the allegedly defective registration statement—so long as the security was indeed issued under that registration statement and not another." DeMaria, 318 F.3d at 176 (emphasis in original) (quoting Lee v. Ernst & Young, LLP, 294 F.3d 969, 976-77 (8th Cir. 2002)). The shares on the SWX purchased by Avalon were carved out from the shares registered under Converium's Form F-1 filed with the SEC and are, therefore, not traceable to the Registration Statement.

V. SECTION 12(a)(2) CLAIMS OF CO-LEAD PLAINTIFFS AND ALL OTHER AFTERMARKET PURCHASERS AND PURCHASERS THAT SOLD SHARES AT OR ABOVE THE OFFERING PRICE SHOULD BE DISMISSED.

It is well-established that purchasers of Converium securities in the aftermarket—such as the two lead plaintiffs—cannot bring a claim under Section 12 of the 1933 Act. See In re Cosi, Inc. Sec. Litig., 379 F. Supp. 2d 580, 588-89 (S.D.N.Y. 2005) (noting that the Supreme Court "indicated that a § 12(a)(2) claim may only be maintained by a purchaser who purchased stock in the public offering at issue rather than in a secondary market transaction") (citing Gustafson v. Alloyd Co., 513 U.S. 561, 578, 584 (1995)); Glamorgan Coal Corp. v. Ratner's Group PLC, No. 93 CIV. 7581 (RO), 1995 WL 406167, at *2 (S.D.N.Y. July 10, 1995) ("Every court since Gustafson, including this district, has held in light of Gustafson, that section 12(2) applies only to initial public offerings."). As is clear from certifications filed with this Court, both of the co-lead plaintiffs purchased their shares in the aftermarket (Avalon first purchased on January 29, 2002 (see Zach Decl. Exh. 18), and Public Employees' Retirement System of Mississippi first bought on March 18, 2002 (see Zach Decl. 19)). Accordingly, the

individual claims of the co-lead plaintiffs and, to the extent they seek to bring a claim for their aftermarket purchases, those of named plaintiff LASER, should be dismissed.[9]

In addition, purchasers who sold their Converium shares or ADSs at or above the offering price should have their claims dismissed because they did not suffer any damages. As the Supreme Court explained in Randall v. Loftsgaarden, 478 U.S. 647 (1986), Section 12(a)(2) prescribes a rescission remedy "except where the plaintiff no longer owns the security." Id. at 655. If the purchaser sold its shares, "a rescissory measure of damages will be employed; the plaintiff is entitled to a return of the consideration paid, reduced by the amount realized when he sold the security and by any 'income received' on the security." Id. at 656. Section 11 limits damages to the difference between "the amount paid for the security (not exceeding the price at which the security was offered to the public) and (1) the value thereof as of the time such suit was brought, or (2) the price at which such security shall have been disposed of in the market before suit, or (3) the price at which such security shall have been disposed of after suit but before judgment . . ." 15 U.S.C. § 77k(e) (emphasis added). Accordingly, any purchaser who bought at the offering price and later sold at the same or a higher price will not have suffered a loss because the consideration paid will be equal to or less than the proceeds of the subsequent sale. Those purchasers' claims should therefore be dismissed.

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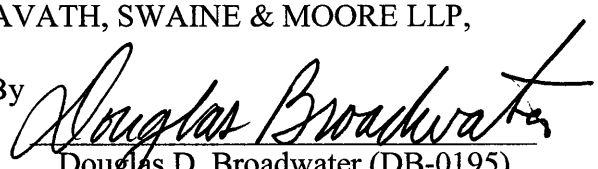
[9] The absence of loss causation is an affirmative defense for claims under Section 11 and Section 12. See 15 U.S.C. § 77k(e); 15 U.S.C. § 77l(b). As discussed above, a defendant may raise an affirmative defense on a motion to dismiss if the defense appears on the face of the Complaint. See In re WRT Energy Sec. Litig., 96 Civ. 3610 (JFK), 2005 WL 323729, at *6 (S.D.N.Y. Feb. 9,2005).. The Underwriter Defendants will not reiterate the arguments made by ZFS in its papers and instead join in ZFS's arguments relating to loss causation to the extent those arguments are applicable to UBS and Merrill.

Conclusion

For the foregoing reasons, the Underwriter Defendants respectfully request that the Court dismiss the Complaint against them in its entirety and with prejudice.

December 23, 2005

CRAVATH, SWAINE & MOORE LLP,

By 

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