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. 7897 04 Civ. 8038 04 Civ. 8060 04 Civ. 8295 04 Civ. 8994 04 Civ. 9479 05 Civ. 3871	x : : : : : : : : : : : : x	04 Civ. 7897 (MBM) ELECTRONIC FILING

LEAD PLAINTIFFS' MEMORANDUM OF LAW IN OPPOSITION TO ALL DEFENDANTS' MOTIONS TO DISMISS THE CONSOLIDATED AMENDED CLASS ACTION COMPLAINT

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Lead Plaintiffs, Public Employees' Retirement System of Mississippi ("PERSM") and Avalon Holdings ("Avalon"), respectfully submit this Memorandum of Law in Opposition to Defendants' Motions to Dismiss the Consolidated Amended Class Action Complaint (the "Complaint").[1] For the reason set forth herein, the Court should deny Defendants' Motions in their entirety.

I. PRELIMINARY STATEMENT

The gravamen of this litigation is that, during the Class Period,[2] Defendants made a series of materially false and misleading statements regarding Converium's loss reserves and financial condition. ¶¶1-5. On July 20, 2004, after years of assuring investors that it was fully and adequately reserved to cover losses stemming from insurance policies it had written in the United States, Converium stunned investors by announcing that it was in fact grossly under-reserved, and would have to take a charge against earnings of a staggering $400 million to increase its North American reserves. ¶¶1, 208 In response to this disclosure, the price of

[1] The Defendants in this case are: Converium Holding AG ("Converium" or the "Company"); Dirk Lohmann, Martin Kauer and Richard Smith, each of whom is a former officer of Converium (collectively, the "Officer Defendants"); Terry G. Clarke, Peter C. Colombo, Georg F. Mehl, Jurgen Forterer, Anton K. Schnyder, Derrell J. Hendrix, and George G.C. Parker, each of whom is or was a member of Converium's Board of Directors during the Class Period (collectively, the "Director Defendants"); Zurich Financial Services Group ("ZFS" or "Zurich"), which was Converium's parent at the time of Converium's December 11, 2001 Initial Public Offering (the "IPO"); and UBS AG and Merrill Lynch International, the co-lead underwriters on the IPO (collectively, the "Underwriter Defendants"). As set forth more fully herein, Lead Plaintiffs have asserted claims arising under the Securities Act of 1933 (the "Securities Act") against the Director Defendants and the Underwriter Defendants, and claims arising under both the Securities Act and the Securities Exchange Act of 1934 (the "Exchange Act") against the Officer Defendants, Converium and Zurich. Defendants filed three separate motions to dismiss; however, because the arguments made by Defendants frequently overlap and are largely redundant of one another, Lead Plaintiffs have filed one memorandum of law in opposition to all three motions. Citations to "¶_" refer to the particular paragraph of the Complaint being cited.

[2] The Class Period runs from December 11, 2001, the date of the Company's initial public offering, through September 2, 2004.

Converium securities in both the United States and Switzerland fell 50% in a single day (in the U.S., Converium American Depositary Shares ("ADSs") fell from $25.02 to $12.61), resulting in a market capitalization loss of $1 billion. ¶¶ 5, 210.

Ultimately, Converium disclosed that it was under-reserved by $562 million. ¶¶1, 217. The charge the Company was forced to incur to correct this massive reserve deficiency was so large that it wiped out every penny of profit Converium had reported in its short history as a public company, and led to the financial ruin of the Company's purportedly lucrative North American business. ¶¶1, 118. In particular, in September 2004, Converium announced that it was placing its North American business – which was responsible for 43% of the Company's insurance business – in "run-off" because of the serious issues with its reserves. ¶¶5, 218. As a result, less than three years after the Company had successfully completed the largest initial public offering of a reinsurance company in history, Converium North America was out of business. ¶¶5, 218.

As the Complaint makes clear, the massive reserve deficiency that led to the demise of Converium North America existed throughout the Class Period, including at the time of the Company's $1.756 billion IPO. ¶¶50-140. Indeed, based on interviews Lead Counsel conducted with the former Converium employees responsible for monitoring and establishing the Company's reserves, and the review and analysis of internal Converium emails and documents, the Complaint describes this massive reserve deficiency with remarkable particularity and extraordinary detail. ¶¶50-140.

For example, prior to the IPO, a consultant retained by Converium to review its reserves told the Company that its reserves were deficient by at least $350 million – and Defendants ignored this conclusion because they knew that they could not disclose this massive reserve

deficiency and still complete the public offering. ¶¶82-87. Similarly, in early 2003, another consultant retained by Converium told the Company that its reserves were deficient by more than $437 million. ¶¶114-22. Once again, however, Defendants refused to increase the Company's reserves to address the massive deficiency. *Id.* Then, in October 2003, Converium's Global Reserving Actuary, Jean Claude Jacob, sent an email to Defendants Lohmann and Kauer (Converium's Chief Executive Officer and Chief Financial Officer), in which Jacob specifically told Converium's two most senior officers that the Company was under-reserved by at least $300 million in both 2002 and 2003. ¶¶107, 132-33. In sum, the evidence of Defendants' scienter is overwhelming. There can be no serious dispute that these allegations are sufficient to state claims for violations of Section 11 of the Securities Act and Section 10(b) of the Exchange Act.

Tellingly, despite their voluminous motion papers, not one Defendant has challenged the reliability of the witnesses described in the Complaint, or contended that these senior employees were not in position to know the facts which they described. Nor do Defendants challenge the veracity or accuracy of the internal Converium documents cited in the Complaint. Instead, Defendants attempt to do what they are prohibited from doing on a Rule 12(b)(6) motion to dismiss. Defendants' principal argument in support of their motions is that Lead Plaintiffs are wrong, and their motions essentially ask the Court to rule as a matter of law at the pleading stage that Converium was adequately reserved. Indeed, Defendants ask that the Court ignore the detailed allegations of the Complaint, and instead consider other, non-public internal documents which are not cited or described anywhere in the Complaint. However, it is axiomatic that, in resolving these motions under Rule 12(b)(6), the Court may not do so. Rather, the Court must accept Lead Plaintiffs' well-pled allegations as true, and can neither accept Defendants' argument that the Company's reserves were adequate, nor consider the extraneous documents on

which Defendants base their Rule 12(b)(6) motions.[3] *Chambers v. Time Warner, Inc.*, 282 F.3d 147, 153 (2d Cir. 2002); *S.E.C. v. McDermott*, No. 99 Civ. 12256, 2004 WL 385197, at *2 (S.D.N.Y. March 1, 2004) (Mukasey, J.).

For the reasons set forth herein, Defendants' motions to dismiss should be denied in their entirety.

II. STATEMENT OF FACTS

A. Introduction

Converium is a global multi-line reinsurance company that provides property and casualty reinsurance products. ¶52. As a reinsurer, Converium agrees to indemnify insurance companies for a portion of the risk they undertake in exchange for a premium. *Id.* Thus, as with any insurance company, Converium receives current income in the form of premiums in exchange for agreeing to pay future claims, and must maintain loss reserves to ensure its ability to pay those claims.[4] However, the establishment of loss reserves negatively impacts Converium's financial results by reducing its current income, earnings-per-share and shareholders' equity, while driving up the Company's combined ratio. ¶¶61-66.[5] The management of the Company's loss reserves is critically important to investors, because it

[3] The documents attached to Defendants' motions to dismiss are the subject of Lead Plaintiffs' Motion to Strike, which is being filed contemporaneously herewith.

[4] Generally Accepted Accounting Principles ("GAAP") require Converium to account for its obligation to pay those claims by establishing adequate loss reserves. ¶¶220-233.

[5] Loss reserves are listed as a liability on the Company's balance sheet and directly offset current income. ¶61. During the Class Period, Converium's loss reserves represented the single largest expense on the Company's income statement. *Id.* When the Company increases its loss reserves, its publicly reported income, earnings-per-share and shareholders' equity all decline. ¶¶61-63. Increases to Converium's loss reserves drive up the combined ratio and, because a combined ratio greater than 100% indicates the Company is unprofitable, investors and analysts relied on the reported combined ratio to provide an accurate snapshot of the Company's profitability and financial performance. ¶¶63, 66.

directly impacts the Company's earnings and profitability. ¶¶56, 61-63. Simply stated, when the Company increases its reserves, its income decreases.

During the Class Period, the Company was organized into three geographic operating units: Converium North America, Converium Zurich and Converium Cologne. From the time of its IPO until the third quarter of 2003, the Company reported its financial results on a consolidated basis and by geographic segment, providing investors with detailed information regarding the financial performance of Converium North America.[6] ¶¶124. Converium North America was the most important of these units, and drove the Company's revenues. ¶¶96-97. Analysts focused on the performance of Converium North America, noting in 2002, for example, that it contributed 40% of the Company's premium volume, and that "North America accounts for 42% of total group business." ¶96. Yet it was in North America that the Company, driven by pressure from Zurich, its former parent, had aggressively under-priced its reinsurance products for years, giving rise to a massive loss reserve deficiency at the time of the IPO. ¶¶74, 75.

Converium and ZFS purportedly established the Company's loss reserves based on exhaustive actuarial analyses performed by teams of experienced professionals who constantly reviewed and updated their determination as to the adequacy of the Company's reserves. ¶¶57, 58, 146. The Company claimed that its highly trained actuaries analyzed the Company's reinsurance policies based upon "actuarial tools that rely on historical and pricing information and statistical models as well as [Converium's] pricing analyses," in order to calculate the claims the Company would be obligated to pay and the reserves needed to cover those claims. ¶¶146.

[6] As explained more fully below in Section I.E., in October 2003, in order to conceal their plan to resolve the Company's reserve deficiencies without public disclosure, Defendants stopped reporting Converium's financial results by geographic segment. ¶¶165.

The Company's senior management, including Defendants Lohmann, Kauer and Smith, closely monitored Converium's loss reserves. According to a former Converium reserving actuary who served as the Chief Reserving Actuary at Converium North America from late 2001 through mid-2002 ("Confidential Witness No. 1"), Converium did not book any reserves without the approval of Lohmann and Kauer. ¶98.

B. Defendants Conceal a $350 Million Reserve Deficiency In Order To Complete Converium's Initial Public Offering

By the end of 2000, Converium's reserves were deficient by at least $350 million. As a result, ZFS, which at that time owned 100% of Converium, decided to dispose of its unprofitable reinsurance business by conducting an initial public offering of Converium stock. ¶¶80-94. In connection with the IPO, in early 2001 ZFS and Converium retained Tillinghast Towers Perrin ("Tillinghast") to conduct a review of the Company's reserves as of year-end 2000. *Id.* Tillinghast conducted that review and, in April 2001, determined that Converium North America was under-reserved by at least $350 million. ¶¶82, 83. Written reports setting forth Tillinghast's conclusion, including a detailed break-down of the reserve deficiency for each of the North American business lines, were distributed to the Company's senior management, including Defendants Lohmann, Kauer and Smith. ¶¶82, 83.

The reserve deficiency identified by Tillinghast was so massive that, had the Company increased its reserves to correct that deficiency, Converium would have reported a loss for 2000 of a staggering $380 million – or more than ten times greater than the $29 million loss it reported in 2000. ¶85. Defendants knew that the Company could not conduct its IPO if it disclosed a reserve deficiency of that size and reported a loss for 2000 of nearly $400 million, because such a significant loss would cause investors to question the financial viability of Converium and the integrity of its reserves. ¶84. Accordingly, rather than reveal the Company's true financial

condition to investors, Defendants deceived Tillinghast into revising its best estimate of the Company's reserve deficiency. ¶¶86, 87. Specifically, Defendants Lohmann, Kauer and Smith decided that $125 million was the most they could increase the Company's reserves and still conduct the IPO. These Defendants then instructed Confidential Witness No. 1 and other senior Converium actuaries to "persuade" Tillinghast to withdraw its original conclusion and revise its estimate of the reserve deficiency to $125 million. ¶86.

Converium "worked [Tillinghast] to death" over the next several months in an effort to get Tillinghast to change its opinion. After several months of intensive pressure from Converium, the ploy succeeded. As Confidential Witness No. 1, who was directly involved in the Tillinghast review, stated, Converium "pulled a fast one" on Tillinghast. ¶87. While Tillinghast was tricked into revising its conclusion, the Officer Defendants and ZFS knew that Tillinghast's original conclusion that the Company was under-reserved by at least $350 million was correct, and that the Company remained severely under-reserved even after it increased its reserves by $125 million in the second half of 2001. *Id.*

Having deceived Tillinghast, Defendants proceeded to conduct the largest public offering of a reinsurance company in history, by representing to investors that the Company had established reserves that were fully adequate and purportedly in-line with Tillinghast's best estimates. ¶¶89, 92. Pursuant to the Registration Statement and Prospectus, which was signed by Defendants Lohmann, Kauer, Colombo, Mehl, Forterer, Schnyder, Hendrix and Parker, ZFS sold 40 million shares of Converium stock – 100% of its holdings – at prices of $24.59 per ADS and 82 Swiss Francs per share, reaping proceeds of approximately $1.67 billion. ¶91. Of the remaining proceeds from the IPO, approximately $54 million was paid in fees to Defendants

UBS and Merrill Lynch, who served as co-lead underwriters of the IPO and sold over 22 million Converium shares on the IPO, and to the other underwriters. ¶93.

C. Converium's Reserve Deficiency Increases After the IPO

Contrary to Defendants' representations that Converium maintained adequate reserves, Converium's new shareholders were in fact saddled with hundreds of millions of dollars in reserve deficiencies. ¶95. That reserve deficiency quickly increased following the IPO. ¶¶102, 103. According to Confidential Witness No. 1, less than 20 days after the IPO, when the year-end results for 2001 were analyzed, Defendant Smith and the most senior actuaries at Converium North America identified an additional $80 million in adverse loss development. *Id.* However, because the Company had just conducted its IPO, Converium's senior officers decided that they could not increase reserves in response to that loss development. *Id.*

Further, in 2002 the Company's reserve position continued to deteriorate. ¶¶104, 105. Converium North America experienced adverse loss development of up to $50 million during each quarter of 2002, which was reported to Defendants Lohmann and Kauer by Defendant Smith in meetings attended by the Company's Global Reserving Actuary. ¶104. Defendants Lohmann, Kauer and Smith refused to materially increase reserves to redress these developments, adding just $5-10 million to the North American reserves for the first two quarters of 2002. ¶105.

While the North American reserve deficiency mounted, Defendant Lohmann repeatedly reassured investors regarding Converium's reserve position. ¶154. For example, in a July 29, 2002 letter to investors, Defendant Lohmann wrote, "We continue to closely monitor the adequacy of our reserves for losses and loss adjustment expenses to uphold high reserving standards." *Id.* In the second half of 2002, the Company increased its reserves by $117 million,

and assured investors that the modest increases had fully addressed its reserve situation. ¶¶160-162. Indeed, in a November 19, 2002 press release, Defendant Lohmann specifically told investors that there would be no need for additional reserving increases in the future, stating that "Converium North America has finalized its loss reserve analysis. "¶165. Defendant Kauer further stated that the increases "keep us at our best estimate within our actuarial range." ¶¶165-168.

As these Defendants knew full well, these statements were not true, and even after these reserve increases the Company remained massively under-reserved. In 2002, Converium's Global Reserving Actuary, Jean-Claude Jacob, initiated his own study of the reserves, for the purpose of determining "how big the hole in New York" was. ¶106. Jacob emailed the results of his study directly to Converium's most senior executives, including Defendants Lohmann and Kauer. In one internal email Jacob told Defendants Lohmann and Kauer that, as of year-end 2002, even after the reserve increases that occurred in 2002, Converium North America was under-reserved by $293.2 million. ¶107.

D. The Reserve Deficiency Swells To Nearly $800 Million in 2003

The severity of the North American reserve deficiency led Converium's Board of Directors to retain B&W Deloitte ("Deloitte") to conduct an independent review of Converium's reserves in or about April 2003. ¶108. To ensure that Deloitte performed an unbiased analysis, the Company provided Deloitte only with its raw claims data, rather than Converium's actuarial conclusions. ¶¶112, 113. In May 2003, Deloitte concluded that Converium North America was under-reserved by a staggering $437 million – a deficiency which represented 25% of Converium North America's total reserves, and did not include "take-out accounts" and finite insurance, which would have increased the total deficiency. ¶¶114-115. The deficiency was so

large that, had Converium increased its reserves to address the deficiency, the charge would have wiped out all of the Company's reported net income for 2002 ($106.8 million) and 2003 ($185.1 million) combined, and resulted in a net loss of at least $145 million for those years. ¶118.

Incredibly, by the time Deloitte concluded its study, Converium's reserve deficiency had increased markedly. Deloitte analyzed the Company's reserves as of year-end 2002 – yet internal Converium documents identified additional adverse loss development of $339.9 million that occurred during the first half of 2003 alone. ¶120. This adverse development exacerbated the existing reserve deficiency, and left Converium North America under-reserved by at least $776.9 million as of June 30, 2003. ¶120. Nevertheless, the Defendants assured the market that Converium's reserves were fully adequate. For example, Defendant Kauer told investors on a July 29, 2003 conference call that "Converium maintains a strong reserving level. . . . We continue to maintain our reserving discipline." ¶183. The Company also expressly assured investors that Converium had not experienced any adverse loss development – notwithstanding the $339.9 million loss development discussed in internal e-mails. ¶¶120, 184.

E. Converium's Novation Scheme and Secret Reserves Increases

Faced with this overwhelming and rapidly increasing reserve deficiency, the Company had limited options. Defendants knew that a public disclosure of the reserve deficiency would have a devastating impact on the Company's business and the price of its stock. Moreover, Defendants Lohmann and Kauer had assured investors only a few months earlier that the Company was adequately reserved and would not need to increase its reserves in 2003. ¶¶161-168. Accordingly, Defendant Lohmann concocted a secret, two-pronged scheme designed to conceal the Company's massive North American reserve deficiency. ¶¶128-130. The Company began "novating" its worst reinsurance policies from Converium North America to Europe, and

also instituted secret reserve increases.[7] *Id.* Through this scheme, the Company secretly improved Converium North America's reserve deficiency by approximately $275 million in the second half of 2003 – without any disclosure to investors. ¶138

According to Confidential Witness No. 6, who served on the Company's Executive Committee, the purpose of the novation scheme was to clean up the balance sheet of Converium North America. ¶129. Confidential Witness No. 1 confirmed this, describing the novation scheme as follows:

> [W]e novated our worst contracts. We took a lot of shit off of North America's books by putting it onto the European company's books, and then said, as a global organization, to paint a rosier picture of New York, but obviously it wasn't enough because it continued to deteriorate. (emphasis added)

¶130.

To conceal the impact of the novation scheme and secret reserve increases on Converium North America, Jacob conceived a plan to obfuscate the condition of its North American operations. ¶¶125-127. On October 3, 2003, as the novation scheme and secret reserve increases were being implemented, Converium announced that the Company would no longer report its financial and operating results by geographic segments. ¶125. The reorganization was done "strictly to hide the fact that New York sucked," in the words of Confidential Witness No. 1. ¶127.

In addition to secretly addressing the existing reserve deficiency, the Company improperly "buried" new adverse loss development. Specifically, Jacob, the Global Reserving Actuary, and Spalla, Converium North America's Chief Reserving Actuary, at the direction of

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[7] A novation is the transfer of an insurance policy or group of policies, including all premiums received and losses paid, from one entity to another. ¶128. Through these novations, Converium North America relinquished to Zurich the premiums it had received for underwriting those policies and Converium North America then released the reserves it had established to cover losses claimed under those policies. *Id.*

senior Company management, instructed Converium North America's actuaries "to bury $45 million" in adverse loss development at Converium North America that the Company incurred during the third quarter of 2003. ¶¶134-136.

Defendants Lohmann, Kauer and Smith received direct reports of the progress of the scheme. ¶¶132-133. Specifically, on October 26, 2003, Jacob, Converium's Global Reserving Actuary, e-mailed Lohmann, Kauer and Smith, among others, that for the third quarter of 2003, "[t]hrough Novations and reserve strengthening CRNA [Converium Reinsurance North America] reserve position improved by US$155M (*i.e.* US$74.1M of actual reserve strengthening and US$81.3M of reserve deficiency on novated contracts transferred to Converium AG (CAG))." ¶132. Yet even after these novations and secret reserve increases, Converium remained under-reserved. Jacob's e-mail concluded that, as of the third quarter, for 2003 North American reserves were still deficient by nearly $300 million. ¶133.

The novation scheme and secret reserve increases enabled the Company to report record financial results for 2003. ¶193. On February 17, 2004, the Company announced that, for the year ended December 31, 2003, Converium had achieved net income of $185.1 million and earnings-per-share of $4.65, which resulted in a return on equity of 10.7%. *Id.* Indeed, rather than publicly increasing its reserves to address its North American deficiency, the Company actually announced that it had lowered its reserves by $31.3 million, thereby boosting income and signaling to the market management's confidence in the adequacy of Converium's reserves. ¶194.

F. The Truth About Converium's Financial Condition Is Revealed

Converium's fraudulent scheme was ultimately unsustainable. After announcing its "best quarter operating income so far" in the first quarter of 2004, the Company needed to bury still more of its reserve deficiency. ¶¶199, 203. According to Confidential Witness No. 1, Defendant Lohmann directed Spalla to "bury $40 million" in reserve deficiencies in the second quarter of 2004 so the Company could "put another good quarter under [its] belt." ¶204. Spalla recognized the futility in continuing Converium's charade, and refused Lohmann's instruction. *Id.* Accordingly, in June 2004, with the second quarter drawing to a close, Defendants Lohmann and Kauer turned to the President of Converium North America (Confidential Witness No. 6) and to the North American CFO, Brian Kensil, and asked them to bury $50 million in reserve deficiencies. ¶¶205, 206. Both refused. *Id.*

With no employees willing to continue concealing the Company's reserve deficiency, Defendants Lohmann and Kauer had no choice but to disclose Converium's true condition. That disclosure set in motion a chain of events that led to the financial ruin of Converium North America.

On July 20, 2004, Converium shocked the market by announcing that it would take a $400 million charge in order to increase reserves in North America. ¶208. The price of the Company's securities collapsed in response, losing 50% of their value in a single day of trading. *Id.* Converium's ADSs fell $12.44, from $25.02 to $12.61 per ADS, while the Company's stock fell 28.80 CHF on the Swiss Stock Exchange from 62.05 CHF per share on July 19 to close at 33.25 CHF per share. *Id.* Then, on August 30, 2004, the Company disclosed that it would need to increase reserves by $50-100 million above the $400 million previously announced. ¶215. This revelation drove the price of the Company's securities down another 11.6%. *Id.* The

Company ultimately increased its reserves by $562 million in 2004, causing the Company to report a loss for 2004 of $761 million – more than three quarters of a billion dollars. ¶217.

Analysts were furious at how they had been misled by Converium's assurances about its loss reserves. ¶211. A Morgan Stanley report described Converium's "bewilderingly large reserve strengthening" as its basis for downgrading the Company, noting that "Management have repeatedly stated over the past 12 months that they did not expect to see large additions to US casualty reserves following address of this issue in 2002 . . . ." *Id.* Numerous analysts also questioned management's credibility. *Id.* Defendant Lohmann's attempts to minimize and explain away Converium's terminal reserve deficiency were soundly refuted by competitors and analysts. ¶¶209, 211, 214.

The ultimate disclosure of the Company's reserve deficiency led to a downgrade of Converium's credit rating in August 2004 by Standard & Poor's and A.M. Best. ¶216. Those downgrades triggered clauses in the Company's reinsurance agreements that enabled Converium's customers to cancel their policies without penalty, and to reclaim previously paid premiums. ¶218. On September 10, 2004, the Company announced that it was placing its North American business in "run-off." Less than three years after the Company had successfully completed its IPO, Converium North America was out of business. *Id.*

G. Summary of the Claims Alleged in the Complaint

The Complaint alleges seven claims against the Defendants. Claims 1 through 4 involve four groups of false and misleading statements that the Defendants made in connection with the IPO on December 11, 2001. *See* ¶¶141-48; *see also infra* Part III (describing the four groups of false and misleading statements made in connection with the IPO). In particular, Lead Plaintiffs have brought the following claims under the Securities Act:

Claim 1 (¶¶237-47) alleges that the Director Defendants and the Underwriter Defendants violated Section 11 of the Securities Act because the Registration Statement and Prospectus contained untrue statements of material fact and failed to disclosed material facts as described in ¶¶141-48. Claim 2 (¶¶248-58) alleges that Converium and the Officer Defendants violated Section 11 for the reasons described in ¶¶141-48. Claim 3 (¶¶259-67) alleges that ZFS (Converium's parent corporation) and the Underwriter Defendants violated Section 12(a)(2) of the Securities Act, and Claim 4 (¶¶268-75) alleges that Converium violated Section 12(a)(2).

Claims 5 and 6 allege that ZFS, the Officer Defendants and certain Director Defendants are liable under Section 15 of the Securities Act, which holds any person (or company) that controls another person (or company) "liable jointly and severally with and to the same extent as such controlled person" violated Section 11 or Section 12. *See* ¶¶ 276-86.

As the Complaint makes clear, for purposes of Lead Plaintiffs' Securities Act claims, Lead Plaintiffs do not allege that any Defendant acted with scienter in issuing the Registration Statement and Prospectus. *See* ¶¶238, 249, 260, 269. Moreover, at trial, Lead Plaintiffs will not be required to prove to the jury any Defendant's state of mind to establish their liability under the Securities Act, as scienter is not an element of either Section 11 or Section 12(a)(2). *See* ¶¶238, 249, 260, 269.

In addition to the Securities Act claims, Lead Plaintiffs have brought the following claims under the Exchange Act against Converium, ZFS, the Officer Defendants and certain Defendant Directors. Claim 7 is asserted against Converium and the Officer Defendants and is based on the false and misleading statements that Converium and the Officer Defendants made from December 10, 2001 until April 24, 2004 in various SEC filings, during analyst meetings and

press releases.[8] *See* ¶292. Lead Plaintiffs allege that these false and misleading statements violated Section 10(b) of the Exchange Act and Rule 10b-5(b) promulgated thereunder. Unlike their other claims arising under the Securities Act, with respect to their Exchange Act claims, Lead Plaintiffs allege that the Company and the Officer Defendants made these statements knowing that they were false and misleading or, at the very least, with reckless disregard for the truth. The Complaint contains extensive and detailed facts that establish a strong inference of scienter for each of these Defendants.

Claim 8 alleges that the Officer Defendants and certain Director Defendants are liable under Section 20 of the Exchange Act, which holds any person (or company) that "directly or indirectly" controls another person or company "liable jointly and severally with and to the same extent as such controlled person [or company]" violated any provision of the Exchange Act or SEC regulation promulgated under it. *See* ¶¶308-15.

Finally, Claims 9 and 10 relate solely to ZFS. In Claim 9, Lead Plaintiffs allege that ZFS violated Rule 10b-5 by intentionally or recklessly making false statements in the Registration Statement and Prospectus which became effective on December 10, 2001. *See* ¶¶316-21. Claim 10 alleges that ZFS is jointly and severally liable under Section 20 for directly or indirectly controlling Converium while it was a subsidiary and violated Rule 10b-5. *See* ¶¶322-28.

[8] In addition to his liability for the materially false and misleading statements that were contained in group published documents (i.e., SEC Filings and Press Releases), Defendants Lohmann and Kauer are liable for the false and misleading statements that they *personally* made during the Class Period in shareholder letters, press releases, and conference calls with analysts. *See* ¶¶ 294 (Lohmann), 296 (Kauer).

III. THE APPLICABLE PLEADING STANDARDS ON A MOTION TO DISMISS

A. Rule 12(b)(6)

Defendants have moved to dismiss the Complaint in its entirety under Rule 12(b)(6) of the Federal Rules of Civil Procedure. *See* Converium at 1; Underwriters Mem. at 1. Resolution of a Rule 12(b)(6) motion requires a court to accept all well-pled allegations in the complaint as true, and to draw all reasonable inferences in the plaintiff's favor. *See Chambers v. Time Warner, Inc.*, 282 F.3d 147, 152 (2d Cir. 2002); *S.E.C. v. McDermott*, No. 99 Civ. 12256, 2004 WL 385197 (S.D.N.Y. March 1, 2004) (Mukasey, J.); *Sedona Corp. v. Ladenburg Thalmann & Co.*, No. 03-Civ.-3120, 2005 WL 1902780, *4 (S.D.N.Y. Aug. 9, 2005). "The issue is not whether the plaintiff ultimately will prevail but whether the plaintiff is entitled to offer evidence to support its claims." *Vtech Holdings Ltd. v. PriceWaterhouseCoopers LLP*, 348 F. Supp. 2d 255, 261 (S.D.N.Y. 2004). "When presented with a Fed. R. Civ. P. 12(b)(6) motion, the Court's task is to assess the legal feasibility of the complaint rather than to weigh the evidence that might be offered in support thereof." *In re WRT Energy*, No. 96 CV 3610, 2005 WL 323729, at *5 (S.D.N.Y. Feb. 9, 2005).

"A court may dismiss a complaint only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations." *Hishon v. King & Spalding*, 467 U.S. 69, 73 (1984). Finally, a court must confine itself to the four corners of the complaint when deciding a Rule 12(b)(6) motion. *Kramer v. Time Warner, Inc.*, 937 F.2d 767, 773 (2d Cir. 1991).

This pleading standard and the presumptions in favor of plaintiffs apply equally in suits alleging violations of the federal securities laws. *See In re Scholastic Corp. Sec. Litig.*, 252 F.3d

63, 69 (2d Cir. 2001) (securities action) ("Accepting all of the allegations in the complaint as true and drawing all reasonable inferences in favor of plaintiffs, dismissal is proper only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations'") (citations and quotation marks omitted); *see also In re Initial Public Offering Sec. Litig.*, 241 F. Supp. 2d 201, 332 (S.D.N.Y. 2003) (securities action) ("*IPO Litigation*").

B. Rule 8's Notice-Pleading Standards Apply to Lead Plaintiffs' Section 11, Section 12(a)(2), Section 15, and Section 20 Claims

"Under the Federal Rules it is remarkably easy for a plaintiff to plead a claim: Unless the claim falls into one of the two exceptions set forth in Rule 9 [which involve claims of fraud of mistake], a plaintiff must simply provide '(1) a short and plain statement of the grounds upon which the court's jurisdiction depends . . . (2) a short and plain statement of the claim showing that the pleader is entitled to relief, and (3) a demand for judgment for the relief the pleader seeks.'" *IPO Litigation*, 241 F. Supp. 2d at 333 (quoting Fed. R. Civ. P. 8(a)). For this reason, the Second Circuit has made it clear that claims brought under Section 11, 12(a) of the Securities Act ("Securities Act") only need to fulfill the requirements of Rule 8 of the Federal Rules of Civil Procedure unless those "sound in fraud." *See Rombach v. Chang*, 355 F.3d 164, 178 (2d Cir. 2004) ("The complaint alleges that the underwriters violated Section 11 and Section 12(a)(2) of the Securities Act . . . . These claims are not subject to the heightened pleading requirements of Rule 9(b), because they sound in negligence . . . ."). While Defendants attempt to ratchet up the pleading requirements for Lead Plaintiffs' Section 11 and Section 12(a)(2) claims, their argument that these claims must satisfy Rule 9 clearly fails.

"Rule 9(b) applies to Section 11 and Section 12(a)(2) claims insofar as the claims are premised on allegations of fraud," *Rombach*, 355 F.3d at 171. In this case, Lead Plaintiffs have explicitly averred that their Section 11 claims are not premised on fraud by pleading:

> This Count does not sound in fraud. All of the preceding allegations of fraud or fraudulent conduct and/or motive are specifically excluded from this Count. Plaintiffs do not allege that the Director Defendants or the Underwriter Defendants had scienter or fraudulent intent, which are not elements of a Section 11 claim.

¶238; *see also* ¶¶249, 260, 269, 277, 282. As Judge Keenan recently explained in holding that Rule 8 governs claims arising under Section 11, "Plaintiffs worded their Complaint carefully to avoid any allegations sounding in fraud. At most, the allegations sound in negligence." *In re WRT Energy*, No. 96 Civ. 3610, 2005 WL 323729, at *6 (S.D.N.Y. Feb. 9, 2005) (citing *Rombach*, 355 F.3d at 167)); *In re WorldCom, Inc. Sec. Litig.*, No. 02 Civ. 3288, 2004 WL 1435356, at *3 n.4 (S.D.N.Y. June 28, 2004) ("*WorldCom*") (holding that Rule 8 applies because "Plaintiffs' Complaint explicitly disclaims that its Securities Act claims are fraud claims.") To the extent that the Complaint contains phrases such as "materially incorrect," "untrue statements" and "did not have reasonable ground to believe," such language merely tracks Sections 11 and 12(a)(2) of the Securities Act and does not mean that the Complaint "sounds in fraud." *See In re WRT Energy*, 2005 WL 323729, at *6.[9]

For these reasons, as Courts in this District have repeatedly held, Rule 8(a) applies to Lead Plaintiffs' Section 11 and Section 12(a)(2) claims in situations such as this one. *See, e.g.*, *In re WRT Energy*, 2005 WL 323729 at *6 (relying on *Rombach*); *IPO Litigation*, 358 F. Supp. at 206 (same); *WorldCom*, 2004 WL 1435356, at *3 (same); ("Plaintiffs' Sections 11, 12(a)(2), and 20(a) claims are governed by the pleading standard set forth in Rule 8(a), Fed. R. Civ. P.").

[9] Indeed, to meet their burden at trial, Lead Plaintiffs do not need to prove to the jury that the Defendants knowingly or recklessly made the alleged untrue statements in the Registration Statement and Prospectus. *See id.* "Neither knowledge nor reason to know is an element in a plaintiff's *prima facie* case" for either claim. *Id.* To the contrary, Lead Plaintiffs need only prove that Defendants made a material misstatement or omission in the Registration Statement to prevail on their Section 11 claim. *See Herman & McLean v. Huddleston*, 459 U.S. 375, 382 (1983).

Given that Rule 8 only requires "a short and plain statement of the claim," Lead Plaintiffs have easily satisfied its requirements. Fed. R. Civ. P. 8(a). [10]

Moreover, Defendants do not contest that Lead Plaintiffs' claims under Section 15 of the Securities Act and Section 20(a) of the Exchange Act must only satisfy Rule 8. Sections 15 and 20 establish joint and several liability for any person or company that "directly or indirectly" controls another person that violates another provision of either the Securities Act or Exchange Act. *See* 15 U.S.C. § 77o (Section 15); 15 U.S.C. § 78t(a) (Section 20). "Rule 9(b) does not apply to the pleading of a Section 15 claim because fraud is not an element of that claim. And the Private Securities Litigation Reform Act ("PSLRA") does not apply, as Section 15 does not require proof of scienter, and because Section 15 arises under the Securities Act." *IPO Litigation*, 241 F. Supp. 2d at 352. Likewise, "scienter is not an essential element of a Section 20(a) claim," and it "must therefore be pleaded only in accordance with Rule 8(a)." *Id.* at 396. Because Defendants have notice of these claims, Rule 8 is easily satisfied.

C. Rule 9(b) and Paragraph (b) of the PSLRA Apply Only to Lead Plaintiffs' Rule 10b-5 Securities Fraud Claim

Section 10(b) of the Exchange Act prohibits the use of "any manipulative or deceptive" practice in connection with the purchase or sale of a security. 15 U.S.C. § 78j(b). To state a claim for securities fraud under Section 10(b), plaintiffs must plead that a defendant: "(1) made misstatements or omissions of material fact; (2) with scienter; (3) in connection with the purchase or sale of securities; (4) upon which plaintiffs relied; and (5) that plaintiffs' reliance was the proximate cause of their injury." *Lentell v. Merrill Lynch & Co.*, 396 F.3d 161, 172 (2d. Cir. 2005) (quoting *In re IBM Corp. Sec. Litig.*, 163 F.3d 102, 106 (2d.Cir.1998)). *See also In re*

[10] Should the Court determine that Rule 9(b) applies to Lead Plaintiffs' Securities Act claims, as set forth in the ensuing section, the Complaint more than satisfies the requirements of that Rule.

Parmalat Sec. Litig., 376 F. Supp. 2d 472, 491 (S.D.N.Y. 2005) (Kaplan, J.); *In re LaBranche Sec. Litig.*, No. 03 Civ. 8201, 2005 WL 3411771, *13 (S.D.N.Y. Dec. 13, 2005). Because Rule 10b-5 prohibits securities fraud, Lead Plaintiffs must satisfy Rule 9(b)'s requirements and plead "the circumstances constituting the fraud . . . with particularity." Fed. R. Civ. P. 9(b).

"The additional requirements of Rule 9(b) were well described by Judge Frank Easterbrook when he wrote that '[particularity] means the who, what, when, where, and how: the first paragraph of any newspaper story.'" *IPO Litigation*, 241 F. Supp. 2d at 327 (emphasis in original). Indeed, the particularity requirements of Rule 9 can be satisfied in "as little as in one paragraph" or even "one sentence." *See id.* (relying on the examples in the Federal Rules); *see also Spanierman Gallery, PSP v. Love*, 320 F. Supp. 2d 108, 113 (S.D.N.Y. 2004) (same). This makes perfect sense given that "Rule 9(b) . . . must be read together with rule 8(a)." *Ouaknine v. MacFarlane*, 897 F.2d 75, 79 (2d Cir. 1990); *see also Felton v. Walston & Co.*, 508 F.2d 577, 581 (2d Cir.1974) ("[I]n applying rule 9(b) we must not lose sight of the fact that it must be reconciled with rule 8 which requires a short and concise statement of claims.").

The PSLRA only altered the pleading requirements with respect to one element of a securities fraud claim: scienter. Under the PSLRA, a plaintiff alleging claims under Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5, must "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). For purposes of a Rule 10b-5 claim, the "requisite state of mind," is scienter: "an intent to deceive, manipulate or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.17 (1976). Lead Plaintiffs may establish scienter either (a) by alleging facts to show that Defendants had both the motive and opportunity to commit

fraud, or (b) by alleging facts that constitute strong circumstantial evidence of conscious misbehavior or recklessness. *Novak v. Kasaks*, 216 F.3d 300, 307 (2d Cir. 2000).

In assessing a complaint's factual allegations, "a court should not consider each relevant factual allegation solely in isolation – though some allegations by themselves may suffice to raise a strong inference of the requisite state of mind – but rather as a part of the overall factual picture painted by the complaint." *In re MicroStrategy Inc. Sec. Litig.*, 115 F. Supp. 2d 620, 631 (E.D. Va. 2000); *see also WorldCom,* 294 F. Supp. 2d at 417. ("The allegations in the Complaint are entitled to be taken together to determine if the facts 'give rise to a strong inference of fraudulent intent.'") (quoting *Acito v. IMCERA Group, Inc.*, 47 F.3d 47, 52 (2d Cir. 1995)). "If the totality of the circumstances alleged raises a 'strong inference' of the requisite state of mind, it is immaterial whether plaintiffs satisfy their burden by 'pleading motive and opportunity, conscious misbehavior, recklessness, or by impressing upon the Court a novel legal theory.'" *MicroStrategy*, 115 F. Supp. 2d at 631 (quoting *In re Health Management, Inc. Sec. Litig.*, 970 F. Supp. 192, 201 (E.D.N.Y. 1997)).

Although complaints alleging violations of Rule 10b-5 must comply with the particularity requirement of Fed. R. Civ. P. 9(b), "courts should not demand a level of specificity in fraud pleadings that can only be achieved through discovery." *Liberty Ridge LLC v. RealTech Sys. Corp.*, 173 F. Supp. 2d 129, 137 (S.D.N.Y. 2001). "Even with the heightened pleading standard under Rule 9(b) and the [PSLRA] we do not require the pleading of detailed evidentiary matter in securities litigation." *Scholastic Corp.*, 252 F.3d at 72.

The detailed allegations in the Complaint meet, if not exceed, the requirements of Rule 9(b) and the PSLRA. There can be no question that the Complaint adequately identifies Defendants' false statements, explains how those statements are false and misleading, and, with

regard to Lead Plaintiffs' Exchange Act claims, gives rise to a strong inference that the Officer Defendants and ZFS acted with scienter. Each of Defendants' false statements is set out in detail in the Complaint, and the reason why those statements are false – including the extent of the reserve deficiency when the statement was made and the amount by which Defendants misstated the Company's income, earnings-per-share and shareholders' equity – is provided. ¶¶141-202. The Complaint sets forth the history and development of the Company's reserve deficiency, beginning with the aggressive under-pricing of contracts from 1996-2000 that gave rise to the deficiency through the Company's various schemes to conceal and secretly redress that deficiency. ¶¶68-140. Finally, as discussed in Section VI below, the Complaint identifies numerous instances on which Defendants were directly informed of the reserve deficiency, establishing that they acted with scienter. *Id.* Lead Plaintiffs have adequately stated their claim.

IV. THE COMPLAINT STATES A CLAIM UNDER SECTION 11

A. Section 11 Liability

"Section 11 [of the Securities Act] was designed to hold those who prepare registration statements in connection with IPOs . . . to a stringent standard of liability for any material misrepresentations contained in those statements, although certain Defendants may raise their due diligence as an affirmative defense at trial."[11] *IPO Litigation*, 241 F. Supp. 2d at 296 (emphasis added) (denying motion to dismiss); *see also Herman & MacLean*, 459 U.S. at 381-82

[11] Section 11 provides that "In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security . . . may, either at law or in equity, in any court of competent jurisdiction, sue," *inter alia*, any signer of the registration statement, director of the company, or bank that underwrote the IPO ("underwriter"). 15 U.S.C. § 77k(a); *see also Herman & MacLean v. Huddleston*, 459 U.S. 375, 381-82 (1983) (footnotes omitted); *WorldCom,*, 346 F. Supp. 2d at 656-57 (outlining the legal framework of the Securities Act, including Section 11).

(1983). For this reason, a plaintiff need not prove at trial that the defendants acted with any particular state of mind under Section 11. *See Herman & MacLean*, 459 U.S. at 382. Rather, a plaintiff "need only show a material misstatement or omission to establish his *prima facie* case." *Id.* Thus, "[Section] 11 places a relatively minimal burden on a plaintiff." *Id.*

As set forth below, the Complaint clearly alleges that the Registration Statement and Prospectus issued in connection with Converium's IPO was materially false and misleading.

B. Converium's Registration Statement and Prospectus Contained Materially False Statements and Omissions

1. The False Statements and Omissions In the Registration Statement and Prospectus

As the Complaint alleges, at the time of the IPO, Converium was under-reserved by $225 million. ¶80-85. Nevertheless, Converium's Registration Statement and Prospectus contained four categories of false statements that "were designed to create the impression that Converium was a company that was fully and adequately reserved." *See, e.g.*, ¶¶4, 141.

First, the Prospectus falsely reported financial results for Converium and Converium North America. Specifically, the Prospectus reported that, for the first six months of 2001, Converium had a net loss of $60.5 million and a non-life combined ratio of 111.2% – which marked a significant improvement from the 117% ratio the Company reported for 2000. ¶142. In addition, the Prospectus reported that the Company had shareholders' equity of approximately $1.65 billion as of October 1, 2001. *Id.* The Prospectus also separately reported financial results for Converium North America, including the fact that North America reported a loss for the first half of 2001 of $81 million. ¶143. These statements were materially false and misleading because, at the time of the IPO, Converium North America was under-reserved by at least $225 million. *Id.* As a result, Converium should have reported a loss of at least $285 million for the

first half of 2001, rather than a loss of only $60 million, and Converium North America should have reported a loss of $306 million for this period, rather than a loss of only $81 million. *Id.* Converium's shareholders' equity was similarly overstated by $225 million, or 16%. *Id.* In addition, because Converium's non-life combined ratio was directly impacted by the level of the Company's loss reserves, the non-life combined ratio Converium reported for the first half of 2001 was materially understated. *Id.*

Second, the Prospectus expressly represented that Converium's loss reserves were established in-line with Tillinghast's best estimates, and that the $125 million increase in the Company's reserves taken in connection with the IPO was sufficient to maintain the adequacy of Converium's reserves. ¶144 ("Our revised estimate of reserves, based mainly on the new ceding company reported data, was in line with Tillinghast's principally top-down reserve estimate within its range of estimates."). This was materially false. ¶145. As Confidential Witness No. 1 stated, Tillinghast actually concluded that Converium was under-reserved by $350 million. *Id.* Converium's senior management, however, increased reserves by only $125 million (resulting in a $225 million deficiency at the time of the IPO) because they determined that was the maximum amount by which Converium could increase reserves and still conduct the IPO. *Id.*

Third, the Prospectus materially misrepresented the method by which Converium calculated its loss reserves by stating that the Company established its reserves "on the basis of facts available at the time," and that its reserves "were reasonable estimates based on the information known at the time our estimates were made." ¶146 (quoting paragraphs from Prospectus that falsely reassured investors). These statements were again false for the same reason: Converium was under-reserved by at least $225 million at the time of the IPO, and the Company's reserves were not reasonable based on the information known at the time. ¶147.

Finally, the Prospectus purported to "warn" investors about potential risks related to the adequacy of Converium's loss reserves, stating that reserves "may prove to be inadequate to cover our actual losses." ¶148. This "boiler-plate" risk warning was itself materially false and misleading, because at the time the statement was made, the loss reserves maintained by the Company were not adequate to cover losses, and the Company's reserves in North America were deficient by at least $225 million. *Id.* As discussed more fully below, "warning" about actual problems that already have materialized as hypothetical risks that might occur in the future does not constitute adequate disclosure under the federal securities laws.

In response, Defendants raise a series of arguments, none of which warrant dismissal of the Section 11 claims. First Defendants argue that the Registration Statement and Prospectus were not materially false and misleading because, according to Defendants, the Company was fully and adequately reserved at the time of the IPO. In essence, Defendants argue that the facts alleged in the Complaint are not correct, and that the Court should ignore the Complaint and accept Defendants' version of the facts as true. These arguments cannot be considered at this stage of the litigation, in the context of a Rule 12(b)(6) motion. Defendants also contend that the Complaint should be dismissed for a host of procedural reasons, including that the claims were not timely, and that Lead Plaintiffs lack standing to assert claims arising under the Securities Act. Finally, Defendants contend that the misstatements and omissions are not material. As set forth below, each of these arguments is without merit.

2. Defendants' False Statements Were Material

Defendants maintain that their false statements were "immaterial" to investors as a matter of law. *See, e.g.*, Converium Mem. 20-30; ZFS Mem. at 17-25; Underwriter Mem. at 31. Defendants' argument is wrong.

The test for materiality is well-established: "[T]o fulfill the materiality requirement 'there must be 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.'" *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988) (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)). The question of whether a statement was material to investors is considered to be a "mixed question of law and fact," *TSC Indus.*, 426 U.S. at 450, and thus courts properly give deference to the role of the jury as the fact finder on questions of materiality.

"The question of materiality is rarely amenable to disposition as a matter of law." *IPO Litigation*, 241 F. Supp. 2d at 379. Indeed, materiality may be resolved as a matter of law "[o]nly if the established omissions are 'so obviously important to an investor, that reasonable minds cannot differ,'" *TSC Indus.*, 426 U.S. at 450 (quoting *Johns Hopkins Univ. v. Hutton*, 422 F.2d 1124, 1129 (4th Cir. 1970)), or, "if the information is trivial . . . or is 'so basic that any investor could be expected to know it,'" *Ganino v. Citizens Util. Co.*, 228 F.3d 154, 162 (2d Cir. 2000), 228 F.3d at 161-62 (quoting *Levitin v. PaineWebber, Inc.*, 159 F.3d 698, 702 (2d Cir. 1998)); *see also Halperin v. EBanker USA.com, Inc.*, 295 F.3d 352, 357 (2d Cir. 2002).

Under these well-established tests, Lead Plaintiffs have plainly alleged that Defendants' false statements regarding Converium's financial results and the purported adequacy of its reserves were material. As an initial matter, when Defendants finally disclosed the Company's massive reserve deficiency in 2004, the stock lost almost 50% of its value in a single day. ¶5, 86, 210. This fact alone is compelling evidence that Defendants' misrepresentations were highly material to investors. Moreover, as the Complaint alleges, maintaining an adequate measure of reserves was critical to Converium's financial condition, because the level of reserves directly

impacted the Company's profitability (or lack thereof). ¶118. Further evidence of materiality is the fact that securities analysts and investors were extremely focused on the Company's reserves, and that the Company repeatedly assured the market throughout the Class Period that it was fully and adequately reserved. *See, e.g.*, ¶5, 45, 96, 210. Finally, the reserve deficiency is clearly material when viewed in connection with the Company's financial results. As the Complaint alleges, had Converium increased its reserves to address the true deficiency, the Company would have reported a loss for 2000 of $380 million – or more than ten times greater than the $29.3 million loss the Company did report. ¶85. Similarly, shareholders' equity (the value of a company's assets less the value of its liabilities) was overstated by 16%. ¶143. Indeed, the $225 million reserve deficiency was equivalent to more than $5 per share of Converium stock. In light of these allegations, it is beyond cavil that a reasonable jury could find that Defendants' failure to disclose the massive reserve deficiencies that existed at the time of the IPO "created a "substantial likelihood that the disclosure of the omitted fact would have been viewed by the average investor as having altered the 'total mix' of information made available." *Basic*, 485 U.S. at 231-32.

3. Defendants' Arguments Attacking Tillinghast's Original Conclusion Have No Merit

Defendants argue that Lead Plaintiffs "fail[ed] to adequately plead that Converium's loss reserves were deficient" at the time of the IPO. Underwriters Mem. at 31. The principal basis for this argument is Defendants' assertion that, after Tillinghast concluded that Converium was under-reserved by $350 million, Tillinghast revised its opinion to state that the reserve deficiency was "only" $156 million, and later opined that the Company's reserves were reasonable. Defendants also contend that Converium's auditor issued a clean audit opinion and supposedly approved Converium's reserves. These arguments fail for several reasons.

First, Defendants' argument ignores the allegations of the Complaint that Tillinghast was duped into abandoning its original conclusion by Converium. As alleged in the Complaint, Tillinghast only changed its original conclusion because Defendant Smith, under direction from Defendants Lohmann and Kauer, instructed Isaac Mashitz, then the Chief Reserving Actuary at Zurich Re (North America), Sheldon Rosenberg, then a Vice President and Actuary at Zurich Re (North America), and Confidential Witness No. 1, to "convince" Tillinghast that the reserve deficiency was far less than $350 million. ¶86. These three individuals -- Mashitz, Rosenberg, and Confidential Witness No. 1 -- then "negotiated" with Tillinghast for several months in an effort to persuade Tillinghast that the North American reserves were not deficient by $350 million. *See id.* When Lohmann and Kauer concluded that the maximum reserve increase that Coverium could take and still conduct the IPO was $125 million, Confidential Witness No. 1 was ordered to get Tillinghast to agree that that was the "right number." *See id.* Then, according to this same person, Converium "pulled out every stop" and "worked them (Tillinghast) to death to get that number down." *Id.* Confidential Witness No. 1 explicitly stated that Converium "pulled a fast one" on Tillinghast. ¶86-87. Confidential Witness No.1 also confirmed that Converium's reserving actuaries and the Company's senior management knew that Tillinghast's original determination was accurate. ¶86. Given these allegations, which must be accepted as true on a motion to dismiss, the fact that a subsequent "study" or report by Tillinghast stated that the reserves were "in line" with their best estimates only raises a fact issue as for the jury to resolve at trial.

Second, as courts have recognized, merely because a consultant or auditor opined that Converium's financial statements or reserves were reasonable is not a basis to disregard the well-pled allegations of the Complaint. Indeed, all this does is create issues of fact that may not be

resolved on this motion. These fact issues include what the auditor or consultant reviewed, why Tillinghast changed its opinion, and how (or if) these "experts" monitored Converium's reserves. The decision in *Aldridge v. A.T. Cross Corp.*, 284 F.3d 72 (1st Cir. 2002) is instructive. In that case, the complaint alleged that the defendant misstated its financial statements. On the motion to dismiss, the defendant argued that the complaint failed to allege a false statement because the auditor issued a clean audit opinion on those financial statements and the Company had never restated. The First Circuit rejected this argument, holding that "the fact that the financial statements for the year in question were not restated does not end [plaintiff's] case when he has otherwise met the pleading requirements of the PSLRA. To hold otherwise would shift to accountants the responsibility that belongs to the courts." *Id.* at 83. Similarly, neither Tillinghast's revised opinion nor the audit opinion mandates the dismissal of Lead Plaintiffs' Claims. This is particularly true where Lead Plaintiffs have alleged that Defendants deceived Tillinghast into changing its opinion.[12]

Third, Defendants' argument fails because Lead Plaintiffs rely on far more than Tillinghast's original conclusion to plead that the Company was under-reserved by hundreds of millions of dollars at the time of the IPO. The Complaint alleges that Tillinghast's original conclusion was corroborated by Converium's own actuaries and loss reserve studies. For example, Defendant Smith, as CEO of Zurich Re (North America), consistently refused to book reserves in line with the best estimates presented by the reserving actuaries of Zurich Re (North America) and consistently refused to book reserves in line with the best estimates presented by the reserving actuaries. *Id.* Likewise, Confidential Witness No. 2, who focused on 1998 and

[12] Defendants recognize that this allegation is fatal to their reliance on Tillinghast's revised opinion. Accordingly, throughout their briefs they contend that Lead Plaintiffs have not alleged that Tillinghast was duped. Contrary to what they say, the Complaint clearly makes this allegation.

1999, stated that the policies written during those years were extremely under-priced, meaning that the premiums Converium charged were not sufficient to cover losses on those policies. ¶74. Confidential Witness No. 2 explained that, every quarter, he performed a study of the reserves for those two years, and his estimates as to the reserves needed to cover those years consistently increased. *Id.* Confidential Witness No. 2 has further stated that "the telling piece of information is that every time I looked at those two years they got worse." *Id.* These facts have been further corroborated by Confidential Witness No. 3 who stated the Company had under-priced its U.S. book of business for 1996-2000. ¶75. This witness explained that ZFS placed intense pressure on its reinsurance business in the late 1990s, when these policies were being written, to help meet the annual growth targets that ZFS had projected for its investors which led to the massive under-reserves at the Company. *Id.*

In sum, the Complaint clearly alleges in extraordinary detail the massive reserve deficiency that existed at the time of the IPO.

4. Defendants' "Estimates" Of Converium's Reserves are Actionable Misstatements

The Court should also summarily reject Defendants' argument that their alleged misstatements relating to Converium's reserves are not actionable as a matter of law because they were merely estimates or "opinions." *See, e.g.*, Converium Mem. at 28. Contrary to what Defendants contend, estimates and opinions have long been held to be actionable under the federal securities law. *See, e.g., Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1093 (1991) (holding that defendants could be held liable under federal securities laws when they stated that a stock price of $42.00 for the purchase of the company's shares was a "high value" and represented a "fair" transaction because it could be both factual and material to investors). Indeed, numerous courts have held that misstatements regarding loss reserves violate the federal

securities laws. *See, e.g., In re Westinghouse Sec. Litig.*, 90 F.3d 696, 709 (3d Cir. 1996) (allegedly misstating loss reserves were "adequate" and established in compliance with GAAP); *In re Wells Fargo Sec. Litig.*, 12 F.3d 922, 927 (9th Cir. 1993) ("While the setting of loan loss reserves is, by all accounts, an 'art and not a science,' . . . the federal securities laws are . . . . implicated when plaintiffs allege specific misrepresentations or material nondisclosures in violation of the federal securities laws."); *Hayes v. Gross*, 982 F.2d 104, 106 (3d Cir. 1992); *In re Direct General Corp. Sec. Litig.*, 398 F. Supp. 2d 888, 896 (M.D. Tenn. 2005); *In re PMA Capital Corp. Sec. Litig.* No. 03-6121, 2005 WL 1806503, at *6 (E.D. Pa. July 27, 2005).

As the Third Circuit has held, there is "nothing unique about representations . . . regarding loan loss reserves that removes them from the purview . . . of the federal securities laws." *Shapiro v. UJB Fin. Corp.*, 964 F.2d 272, 281 (3d Cir. 1992). In *Shapiro*, the court held that the following statements would be actionable if alleged to have been made knowingly or recklessly: "loan loss reserves were 'adequate,' 'adequately maintained,' 'strong,' and 'solid;'" "'loan to value ratio was 'good;'" "asset quality was 'high,' while their level of bad loans was 'low;'" "'loan management and underwriting practices were 'conservative,' 'basic,' 'careful,' 'good,' 'prudent,' and 'cautious.'" 964 F.2d. at 283.

Here, the Complaint specifically alleges that Defendants ignored the estimates and conclusions of the Company's own actuaries when establishing the reserves. *See, e.g.*, ¶¶79, 105. Thus, Defendants' misstatements are actionable.

5. Defendants' Warnings Were Insufficient as a Matter of Law

Defendants also resort to the fall back position that, even if the Registration Statement and Prospectus contained false statements and omissions, "the Prospectus contained detailed, specific warnings about the many uncertainties surrounding loss-reserve calculations." ZFS

Mem. at 20; *see also* id. at 23; Converium Mem. at 25-26. In particular, Defendants rely heavily on page 14 of the Prospectus, which states "[o]ur loss reserves may not adequately cover future losses and benefits" and on the accompanying list of possible future risks. Converium Mem. at 8; *see also* ZFS Mem. at 24.

Courts have repeatedly rejected such arguments because warning someone about a potential risk that may come to pass in the future cannot insulate defendants from liability when they fail to disclose facts and events that have already occurred. More presentations about historical or present fact are not protected merely by providing a warning. *See P. Stolz Family P'ship L.P. v. Daum*, 355 F.3d 92, 97 (2d Cir. 2004). In this case, it was an historical fact that Converium was grossly under-reserved by hundreds of millions of dollars at the time of the IPO. Thus, no amount of warning excuses Defendants' failure to disclose this information. As the Second Circuit has held, the federal securities laws provide "no protection to someone who warns his hiking companion to walk slowly because there might be a ditch ahead when he knows with near certainty the Grand Canyon lies one foot away." *Rombach v. Chang*, 355 F.3d 164, 173 (2d Cir. 2004) (quoting *In re Prudential Secs. Inc. P'ships Litig.*, 930 F. Supp. 68, 72 (S.D.N.Y. 1996)); *see also In re Globalstar Sec. Litig.*, No. 01 Civ. 1748, 2003 WL 22953163, at *11 (S.D.N.Y. Dec. 15, 2003); *Credit Suisse First Boston Corp. v. ARM Fin. Group, Inc.*, No. 99 Civ. 12046, 2001 WL 300733 at *8 (S.D.N.Y. Mar. 28, 2001) (holding that "warnings of specific risks . . . do not shelter defendants from liability if they fail to disclose hard facts critical to appreciating the magnitude of the risks described").

The Third Circuit aptly explained in *In re Westinghouse Sec. Litig.*, 90 F.3d 696, 709-10 (3d Cir. 1996):

> If, as plaintiffs say, defendants knowingly or recklessly misrepresented the adequacy of the loss reserves to protect against known losses and known risks in

> light of the then-current economic conditions, it follows that defendants' cautionary statements about the future did not render those misrepresentations immaterial. In our view, a reasonable investor would be very interested in knowing, not merely that future economic developments might cause further losses, but that (as plaintiffs allege) current reserves were known to be insufficient under current economic conditions. A reasonable investor might well be willing to take some chances with regard to the future of the economy, but might be quite unwilling to invest in a company that knew that its reserves were insufficient under current conditions and knew it would be taking another major write-down in the near future (as plaintiffs allege). Thus, notwithstanding the cautionary language stressed by defendants, we think that there is a substantial likelihood that defendants' alleged misrepresentations-i.e., that the loan loss reserves were established in compliance with GAAP and were believed to be adequate to cover expected future losses given the then-existing economic conditions-would have assumed actual significance to a reasonable investor contemplating the purchase of securities. We therefore cannot say that the cautionary language rendered the alleged misrepresentations immaterial as a matter of law.[13]

Thus, the "boilerplate" warnings contained in the Registration Statement and Prospectus were insufficient as a matter of law.

C. The Underwriter Defendants May Not Assert a "Reliance Defense" on a Motion to Dismiss

The Underwriter Defendants argue that no liability can inure to them as a matter of law because they are purportedly "entitled to rely upon the expert opinions proffered" by Tillinghast and PricewaterhouseCoopers ("PwC"). *See* Underwriters Mem. at 25-30. As set forth below, at this stage of the litigation, this argument is without merit.

The Securities Act provides an affirmative defense under Section 11(b), sometimes referred to as a "reliance defense." *See WorldCom,* 346 F. Supp. 2d at 662-79 (S.D.N.Y. 2004) (providing an extensive discussion of this defense). In particular, Section 11(b) states: "[A]s

[13] Because Lead Plaintiffs' claims are predicated on misrepresentation of historical fact at the time of the IPO, Defendants' sparse and unsupported argument that SEC Rule 175, 17 C.F.R. § 230.175, protects the statements about loss reserves can be quickly rejected. *See* ZFS Mem. at 27 (citing no case law). As Defendants concede, Rule 175 only applies to "forward-looking" statements – *i.e.,* statements about the future – not representations of historical fact. *See id.*

regards any part of the registration statement purporting to be made on the authority of an expert," a defendant other than that expert will not be liable if he can demonstrate that

> he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue or that there was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading.

15 U.S.C. § 77k(b)(3)(C) (emphasis added).

While the Underwriter Defendants argue that they were entitled to rely upon Tillinghast and PwC in conducting their due diligence for the IPO, this argument is clearly premature and cannot be considered in the context of this motion. Defendants cannot establish their affirmative due diligence on a Rule 12(b)(6) motion simply by claiming that they relied on an "expert." The only issue that is relevant here is whether Lead Plaintiffs adequately stated a Section 11 claim. As set forth above, there can be no real dispute that Lead Plaintiffs have done so.

Judge Cote's extensive and thoughtful opinion in *WorldCom*, a decision issued only after extensive discovery was conducted, amply demonstrates the substantial burden that the Underwriter Defendants here bear in asserting the reliance defense. *See* 346 F. Supp. 2d at 678 (denying the defendants "motion for summary judgment on their reliance defense."). The fact that Tillinghast issued a report or that PwC audited the Company's financial statements cannot establish as a matter of law that the Underwriter Defendants have proven by a preponderance of the evidence that they "did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue." 15 U.S.C. § 77k(b)(3)(C).

The simple fact is that Lead Plaintiffs do not bear the burden under Section 11 of proving what the Underwriter Defendants believed, or that the Underwriter Defendants had no reasonable ground to believe that the Registration Statement and Prospectus were untrue. Indeed, without discovery, it is impossible for Lead Plaintiffs to know exactly what the Underwriter Defendants

knew, should have known, or should have investigated. "These are exquisitely fact intensive inquiries that depend on the circumstances surrounding a particular issuer and the alleged misstatement. There is no category of information which can always be ignored by an underwriter on the ground that it constitutes an ordinary business event." *Worldcom*, 346 F. Supp. 2d at 679-80. In short, "[t]he Underwriter Defendants have framed their . . . motion in a way that is incompatible with their burden of proving their due diligence defense under Section 11." *Id.* at 683 (emphasis added).

Moreover, the Underwriter Defendants have inappropriately downplayed their role in underwriting an IPO, including conducting adequate due diligence. "As the SEC has observed, in enacting Section 11, Congress recognized that underwriters occupied a unique position that enabled them to discover and compel disclosure of essential facts about the offering. Congress believed that subjecting underwriters to the liability provisions would provide the necessary incentive to ensure their careful investigation of the offering.'" *Id.* at 662 (quoting *The Regulation of Securities Offerings*, SEC Release No. 7606A, 63 Fed.Reg. 67174, 67230, available at 1998 WL 833389 (Dec. 4, 1998) ("SEC Rel. 7606A")).

"No greater reliance in our self-regulatory system is placed on any single participant in the issuance of securities than upon the underwriter." *Chris-Craft Indus., Inc. v. Piper Aircraft Corp.*, 480 F.2d 341, 370 (2d Cir. 1973) (analyzing Section 11). "Underwriters function as the first line of defense with respect to material misrepresentations and omissions in registration statements." *Worldcom*, 346 F. Supp. 2d at 662 (quotation marks and citation omitted). "As a consequence, courts must be 'particularly scrupulous in examining the[ir] conduct.'" *Id.* (quoting *Feit v. Leasco Data Processing Equip. Corp.*, 332 F. Supp. 544, 581 (E.D.N.Y. 1971)

and citing *In re Enron Corp. Sec., Derivative & ERISA Litig.*, 235 F. Supp. 2d 549, 612-13 (S.D. Tex. 2002)).

For these reasons alone, the Underwriter Defendants' argument that they have already proved by a preponderance of the evidence that they reasonably relied on the Tillinghast Study and PwC must be rejected.

D. Lead Plaintiffs' Section 11 Claims Are Timely

Defendants take an inherently inconsistent position in arguing that the statute of limitations has passed with respect to the Securities Act claims. On the one hand, they argue that the false statements about the adequacy of Converium's loss reserves were not material to investors. On the other hand, they argue that their false statements were so obvious that investors should have sued them two years earlier (*i.e.*, there were sufficient "storm warnings" to put investors on inquiry notice that they had been misrepresenting the truth to the public). Defendants can't have it both ways.

The reality of the situation, of course, is far different than what Defendants portray. The fact is that, prior to July 20, 2004, Lead Plaintiffs and the members of the class were unaware that Converium was under-reserved by hundreds of millions of dollars – and had no reason to suspect that the Company was concealing a massive reserve deficiency. Indeed, less than three months before Converium announced it would need to take a $400 million charge in order to effect a reserve increase, the Company announced the most profitable quarter in its history, and actually reversed $31 million in reserves – creating the false impression that Converium was actually over-reserved. ¶208. Further, after the Company announced on July 20, 2004 that it was under-reserved by at least $400 million, Converium securities lost more than 50% of their value in a single day, and numerous analysts wrote that they were stunned by the disclosure.

¶211. These facts are compelling evidence that the market did not have any idea that Converium was materially under-reserved.[14]

1. The Statute of Limitations For Section 11 Claims

Section 13 of the Securities Act sets forth the applicable statute of limitations for Section 11 claims. It states:

> No action shall be maintained to enforce any liability created under [Sections 11] . . .unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence. . . . In no event shall any such action be brought to enforce a liability created under [Section 11] . . . more than three years after the security was bona fide offered to the public, or under [Section 12(a)(2)] . . . more than three years after the sale.

15 U.S.C. § 77m. (emphasis added).

"The one-year limitations period of Section 13 'begins to run after the plaintiff obtains actual knowledge of the facts giving rise to the action or notice of the facts, which in the exercise of reasonable diligence, would have led to actual knowledge.'" *WorldCom,* 294 F. Supp. 2d at 444 (quoting *Levitt v. Bear Stearns & Co.*, 340 F.3d 94, 101 (2d Cir. 2003) (citation omitted); *see also LC Capital Partners LP v. Frontier Ins. Group, Inc.*, 318 F.3d 148, 154 (2d Cir. 2003). Moreover, information that triggers the notice, which are often referred to as "storm warnings," "must be such that it relates directly to the misrepresentations and omissions the Plaintiffs later allege in their action against the defendants." *Newman v. Warnaco Group, Inc.*, 335 F.3d 187, 193 (2d Cir. 2003). Finally, the wrongdoing indicated by the storm warnings "must be probable, not merely possible." *Newman*, 335 F.3d at 193 (citation omitted).

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[14] Defendants do not contest that the current consolidated class action relates back to the previously filed actions under Rule 15(c) of the Federal Rules of Civil Procedure (nor could they under existing law) and, thus, the critical inquiry is whether the initial actions filed in October 2004 were timely.

As courts have recognized, the question of whether a plaintiff had sufficient facts to place it on inquiry notice is "often inappropriate for resolution on a motion to dismiss under Rule 12(b)(6)." *Marks v. CDW Computer Centers, Inc.*, 122 F.3d 363, 367 (7th Cir. 1997). The Second Circuit has held that "[b]ecause we are, on a motion to dismiss, limited to the facts contained in, or incorporated into, the complaint," courts are encouraged to be cautious in ruling "as a matter of law" on when plaintiff had notice. *Rothman*, 220 F.3d at 98.

In the case at bar, inquiry notice was not triggered until July 20, 2004, when the Company shocked investors by announcing that it would incur a $400 million charge in order to address its massive serve deficiency. ¶208. The IPO occurred less than three years earlier, on December 11, 2001, and the first securities action was brought less than three months after the July 20 announcement. ¶47. In fact, the first lawsuit against Converium and certain of the Officer Defendants was filed on October 4, 2004, and on October 12, 2004, the plaintiff in *Taylor v. Converium Holding AG* filed a securities action against Converium, its Officer Defendants, ZFS and the Director Defendants. *Id.* On December 9, 2004, the Underwriter Defendants entered into a tolling agreement, thereby tolling the statute of limitations for claims by the putative class as against the Underwriter Defendants. *Id.*

Following the Court's appointment of Lead Plaintiffs, and after an extensive investigation undertaken by Lead Counsel, the instant Complaint was filed on September 23, 2005. As pled in the Complaint, "[p]ursuant to Rule 15(c) of the Federal Rules of Civil Procedure, the assertion of the Securities Act claims against Converium, ZFS and the Individual Defendants relates back to the date of the filing of the *Taylor* action," which was filed in a timely fashion on October 12, 2004. ¶48.

Defendants do not dispute that the Securities Act claims relate back. Rather they put forward two reasons as to why Lead Plaintiffs' Section 11 claims are purportedly not timely. First, all of the Defendants argue that inquiry notice was triggered prior to October 4, 2003 (*i.e.*, more than one year before the first action was filed). *See* Converium Mem. at 34-37; ZFS Mem. at 49; Underwriters Mem. at 17-24. Second, the Underwriter Defendants claim that the tolling agreement they entered into with the Class does not apply to this action. *See* Underwriter Mem. at 14-17. As explained below, these arguments are without merit.

2. Investors Were Not Placed on Notice of Converium's Massive Reserve Deficiency Until July 20, 2004

All Defendants point to a series of increases in Converium's loss reserves prior to November 2002, and the resulting market reactions to those increases, to argue that Lead Plaintiffs and members of the class were put on inquiry notice of the Company's massive reserve deficiencies by November 2002.[15] *See* Converium Mem. at 36; ZFS Mem. at 49-53; Underwriters Mem. at 49-53; *see also* ¶¶158-186. There are tell-tale signs, however, that these increases in the loss reserves were not sufficient to trigger inquiry notice. For example, as alleged in the Complaint, management's conduct during this same time period was deceptively designed to assure the market that the truth about Converium's financial condition was not disclosed. ¶¶58-186.

In particular, Defendants point to two relatively minor increases of $11.6 million and $24.4 million in the first half of 2002, another increase of $60 million in the third quarter of 2002 and, finally, an increase of $70 million in the fourth quarter of 2002 in support of their

[15] Defendants' argument regarding inquiry notice cannot impact Lead Plaintiffs' Exchange Act claims because these claims were filed in October 2004, or less than two years after the November 2002 announcement.

contention that investors were on inquiry notice. *See, e.g.*, ZFS Mem. at 49; *see also* ¶158-160; 165. However, these disclosures did not in any way put investors on notice that Converium's reserves were materially understated. Indeed, at the same time these increases were announced, Defendants Lohamnn and Kauer assured investors that the modest increases had fully addressed any reserve issues. ¶161. On October 28, 2002, Defendant Lohmann spun the increases this way: "The steps taken in the third and fourth quarter underline Converium management's determination to confront emerging reserve issues in a forthright and proactive manner. As a result, I am confident that the underlying earnings power of our in-force business will manifest itself." ¶166 (emphasis added). Likewise, in a conference call the same day, Defendant Lohmann explained to investors: "I do also feel that we have turned the corner on the reserve thing with this further study... I really feel very strongly that [in] 2003 you are not going see this sort of development impairing our good performance in the business year 2003, and the improvements that we had hoped would flow through fully in the bottom line of 2002 will flow through in 2003." ¶162. Thus, the market was assured, and believed, that these increases in the reserves were a positive move by the Company.

Not surprisingly, Defendants' assurances that Converium was sufficiently and adequately reserved had their desired effect. ¶163. For example, a report by analysts at Sarasin dated October 28, 2002, stated that "[W]e believe management's claim that the additional reserves strengthening of max USD 75m, which will be booked in 2002Q4, will be sufficient to bring Converium's IBNR reserves (incurred but not reported) to adequate levels." *Id* (emphasis added). A few months later, analysts wrote: "Converium has addressed the sector-wide problem of reserve adjustments for the underwriting years 1997 to 2000 in a very transparent way." *See also* ¶161.

Just as important is the fact that, immediately after these increases, and the purported "transparency" of the Defendants, Converium began to report a string of ever-increasing profits, including record income for 2003 and the first quarter of 2004. ¶118. Likewise, when the Company announced its 2003 year-end financial results on February 17, 2004, Defendants highlighted the fact that Converium had actually reduced its reserves by more than $30 million in 2003. ¶4.

Accordingly, investors could not have known that it was "probable" that the Defendants were fundamentally misrepresenting Converium's liabilities. *Newman*, 335 F.3d at 193 (citation omitted). Here, investors were not placed on inquiry notice "because the warning signs are accompanied by reliable words [and actions] of comfort from management." *LC Capital*, 318 F.3d at 155; *see also id.* at 154 (citing *Milman v. Box Hill Systems Corp.*, 72 F. Supp. 2d 220, 229 (S.D.N.Y. 1999) (stating that "courts have been reluctant to find that public disclosures provided inquiry notice where those disclosures were tempered with positive statements")).[16]

In short, Defendants may not intentionally mislead investors and analysts and then hide behind the statute of limitations when the truth is finally disclosed. To hold otherwise would not only reward such malfeasance, but also "precipitate groundless or premature suits by requiring plaintiffs to file suit before they can discover with the exercise of reasonable diligence the necessary facts to support their claims." *Rothman v. Gregor*, 220 F.3d 81, 97 (2d Cir. 2000)

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[16] Defendants rely on *LC Capital*, *see* Underwriters Mem. at 20; Converium Mem. at 37, but the distinction between that case and this one is obvious: In *LC Capital*, "The 'reassuring' statements by management were mere expressions of hope," 318 F.3d at 156, while in this case managements' reassurances where quickly followed by record earnings over the course of two years and even a decrease of loss reserves. As *LC Capital* holds, inquiry notice is not triggered if it appears to an investor of ordinary intelligence that the problems disclosed are not likely to be of a "recurring nature." *Id.* at 155. *See, e.g.*, ¶162 (Defendant Lohmann further reassured the market that, through the reserve increases announced by the Company, Converium had fully addressed the issues relating to its reserves.).

(quoting *Sterlin v. Biomune Sys.*, 154 F.3d 1191, 1201 (10th Cir. 1998)). The fact that Defendants point to documents outside the record to argue that inquiry notice was triggered, *see* Converium Mem. at 36; ZFS Mem. at 49-50, simply highlights the fact that the "[t]he question of constructive knowledge and inquiry notice may be one for the trier of fact and therefore ill-suited for determination on a motion to dismiss." *AIG Global Securities Lending Corp. v. Banc of America Securities, LLC*, No. 01 Civ. 11448, 2005 WL 2385854, at *14 (S.D.N.Y. Sept. 26, 2005) ("Although the defendant points to various offering memoranda and SEC filings, Banc of America does not point to sufficient disclosures that should have put the plaintiffs on notice of the specific misrepresentations asserted by the plaintiffs. Moreover, in arguing that the plaintiffs' claims are time barred, Banc of America relies on a number of documents outside the pleadings, which allegedly put the plaintiffs on inquiry notice but are not to be considered on this motion to dismiss.") (citing *Chambers v. Time Warner, Inc.*, 282 F.3d 147, 153 (2d Cir. 2002)).

3. Lead Plaintiffs' Claims Against UBS and Merrill Were Tolled Pursuant To Agreement

On December 9, 2004, Defendants UBS and Merrill signed an agreement with Michael Rubin, a Converium shareholder, which tolled the statute of limitations for "any individual or class claims which may be brought against [UBS and Merrill]."[17] The only limitation placed on the types of claims to which the tolling agreement applied were that such claims be "under the Securities Act of 1933 arising out of the underwriting of Converium's IPO." *Id.* Nowhere did the agreement limit the tolled claims to those brought by Mr. Rubin, whom the Underwriter Defendants baselessly claim is the sole beneficiary of the agreement. Indeed, the agreement specifically states that it was intended to "preserve the status quo as to the legal rights of Rubin

[17] Exhibit 1 ("Ex. 1") entitled "Tolling Agreeement" attached to Declaration of John T. Zach in Support of Defendants UBS AG's and Merrill Lynch International's Motion to Dismiss the Consolidated Amended Class Action Complaint (attached to Underwriters' Mem.)

and the putative class of purchasers of shares or ADSs of Converium pursuant or traceable to the Registration Statement and Prospectus issued in connection with Converium's December 11, 2001 IPO . . . ." *Id.* (emphasis added).

Thus, contrary to the Underwriter Defendants' contention, *see* Underwriters Mem. at 14-17, the agreement was clearly intended to benefit not only Mr. Rubin but, by its own terms, the entire "putative class of purchasers of shares or ADSs of Converium" traceable to the December 2001 IPO.[18] This is exactly the type of express intent to benefit non-parties that courts have held sufficient for tolling the statute of limitations as to those non-parties. *See, e.g., Lindner Dividend Fund, Inc. v. Ernst & Young*, 880 F. Supp. 49, 55 (D. Mass. 1995) (holding that absent class members could rely on a tolling agreement entered into by plaintiffs in a previously-filed class action, where the absent class members were members of the same putative class on whose behalf the tolling agreement was entered.). Here, too, named plaintiff Louisiana State Employees' Retirement System ("LASERS") and the class of purchasers of Converium securities on whose behalf the instant case is brought are the same putative class members on whose behalf the agreement entered into by Mr. Rubin and the Underwriter Defendants was made.

Defendants' failure to cite any case in which a court has denied putative class members the benefit of a tolling agreement where the terms of the agreement expressly state that the members of the putative class are entitled to such benefits is telling, since no such case exists. *C.F., Pirelli Armstrong Tire Corp. Retiree Med. Bens. Trust v. Dynegy, Inc. (In re Dynegy, Inc.),*

[18] The Underwriter Defendants also resort to ad hominem attacks, claiming that Lead Plaintiffs only named them as defendants because of a lead plaintiff dispute. This is obviously nonsense. Lead Plaintiffs named the Underwriter Defendants as defendants because Lead Plaintiffs' investigation revealed facts which the Underwriter Defendants, had they bothered to conduct a reasonable due diligence investigation, would have uncovered.

339 F. Supp. 2d 804, 864 (S.D. Tex. 2004) (declining to apply tolling agreement to non-party to the agreement "because the putative class on whose behalf the agreements were executed did not include" the non-party). Indeed, the cases cited by the Underwriter Defendants support the proposition that tolling agreements *can* benefit non-parties to the agreement as long as there is an expressed intent in the agreement to benefit such non-parties. *See Caguas Cent. F.S.B. v. United States*, 215 F.3d 1304, 1309 (Fed. Cir. 2000) ("'The intended beneficiary need not be specifically or individually identified in the contract, but must fall within a class clearly intended to be benefited thereby.'" (emphasis added) (quoting *State of Montana v. United States*, 124 F.3d 1269, 1273 (Fed. Cir. 1997) (additional internal quotations omitted). The terms of the Agreement demonstrate that Lead Plaintiffs fall within a class clearly intended to be benefited thereby. Accordingly, the Underwriter Defendants' Tolling Agreement tolled the period for assertion of Lead Plaintiffs' claims against the Underwriter Defendants.[19]

V. DEFENDANTS ARE LIABLE FOR VIOLATIONS OF SECTION 12(a)(2)

Section 12(a)(2) allows a purchaser of a security to bring a private action against a seller that "offers or sells a security . . . by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order

[19] Defendants attempt to circumvent the undeniable applicability of the Agreement to Lead Plaintiffs' claims by contending that Lead Plaintiffs violated the terms of the agreement when they filed suit against the Underwriter Defendants while the Agreement was in place, an act the Underwriter Defendants claim is prohibited by the terms of the Agreement. Underwriters' Mem. at 16. The Underwriter Defendants fail again, however, to read the express terms of the Agreement. Paragraph 3 of the agreement states that "Rubin agrees not to name as defendants the Underwriters in any action . . . for as long as the Agreement remains in effect." Ex. 1 (emphasis added). Indeed, Michael Rubin did not name the Underwriter Defendants as defendants in any action while the Agreement was in effect. Lead Plaintiffs Avalon and PERSM, and named plaintiff LASERS are the ones who have named the Underwriter Defendants in this action. Nowhere in the agreement does it state that members of the putative class other than Rubin are obliged to refrain from bringing suit against the Underwriter Defendants. There was, accordingly, no breach of the Agreement.

to make the statements . . . not misleading." 15 U.S.C. § 77l(a)(2) (formerly referred to as Section 12(2) prior to the passage of the PSLRA in 1995).[20] "Section 12 turns on status, not scienter: It imposes liability without requiring 'proof of either fraud or reliance.'" *WorldCom*, 346 F. Supp. 2d at 659 (quoting *Gustafson v. Alloyd Co.*, 513 U.S. 561, 582 (1995). "Reliance by the buyer need not be shown, for §12(2) is a broad anti-fraud measure and imposes liability whether or not the purchaser actually relied on the misstatement." *Metromedia Co. v. Fugazy*, 983 F.2d 350, 361 (2d Cir.1992) (citation omitted); *see also WorldCom*, 346 F. Supp. 2d at 659.

In the case at bar named, plaintiff LASERS purchased 90,000 shares of Converium securities on the IPO pursuant to the Registration Statement and Prospectus. Defendants, however, argue that LASERS' Section 12(a)(2) claim should be dismissed because (1) notwithstanding the fact that named plaintiff LASERS has standing to bring such claims, the Lead Plaintiffs – PERSM and Avalon – do not have standing to sue and (2) ZFS, Converium and the Individual Defendants argue that they did not "solicit[] the purchase of Converium stock" – an argument that is completely undermined by the allegations contained in the Complaint.

A. LASERS Has Standing to Bring a Section 12(a)(2) Claim

Defendants argue that since the Lead Plaintiffs did not purchase Converium stock pursuant to the Registration Statement and Prospectus, Section 12(a)(2) claims cannot be pled because Lead Plaintiffs lack standing to maintain the action. This argument is incorrect. Defendants concede, as they must, that LASERS has standing to bring a Section 12(a)(2) claim against the defendants. *See* ZFS Mem. at 28-29; Underwriters Mem. at 39. As pled in the

[20] Section 12(a)(2) entitles purchasers of a security "to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security." *Id.*; *see also Commercial Union Assurance Co. v. Milken*, 17 F.3d 608, 615 (2d Cir.1994); *see also Randall v. Loftsgaarden*, 478 U.S. 647, 655 (1986) ("§ 12(2) prescribes the remedy of rescission except where the plaintiff no longer owns the security.").

Complaint, LASERS purchased 90,000 ADSs issued by Converium on the day of the IPO and, as a result of those purchases, LASERS suffered losses in excess of $430,000. ¶18. These are sufficient allegations for LASERS to have standing to sue under Section 12(a)(2). *See* 15 U.S.C. § 77 l (a)(2); see *also Yung v. Lee*, 432 F.3d 142 (2d Cir. 2005). The Second Circuit has held that the lead plaintiffs do not need to have standing to assert every claim, so long as named plaintiffs have standing. *See Hevesi v. Citigroup Inc.*, 366 F.3d 70, 82-83 (2d Cir. 2004).

B. Defendants Either Sold or Solicited the Purchase of Converium Stock

"Defendants may be liable under Section 12(a)(2) either for [1] selling a security or [2] for soliciting its purchase." *Worldcom*, 346 F. Supp. 2d at 659 (alterations added). Under the first prong, Section 12 creates a cause of action against sellers who "passed title, or other interest in the security, to the buyer for value." *Pinter v. Dahl*, 486 U.S. 622, 642 (1988); *see also Wilson v. Saintine Exploration & Drilling Corp.*, 872 F.2d 1124, 1126 (2d Cir. 1989); *Capri v. Murphy*, 856 F.2d 473, 478 (2d Cir. 1988). The Underwriter Defendants do not contest that they were "sellers" of Converium securities for good reason: "As underwriters in a firm commitment underwriting become the owners of any unsold shares, they may be liable as sellers for direct sales to the public." *Worldcom*, 346 F. Supp. 2d at 659 (citing *Pinter*, 486 U.S. at 644 n.21; *see also* ¶93 ("The lead underwriters on the IPO were UBS and Merrill Lynch, each of which sold 11.1 million shares of Converium stock on the IPO . . . .").

Under the second prong, the Supreme Court has explained, companies or individuals who are not in privity with the plaintiff may be nonetheless be liable if they "successfully solicit[ed] the purchase, motivated at least in part by a desire to serve [their] own financial interests or those of the securities owner." *Pinter*, 486 U.S. at 647; *see also Commercial Union Assurance Co.*, 17 F.3d at 616. In finding that Section 12 created liability for solicitation, the Supreme Court

emphasized that "[t]he solicitation of a buyer is perhaps the most critical stage of the selling transaction . . . . [and] the stage at which an investor is most likely to be injured." *Pinter*, 486 U.S. at 646.

ZFS, Converium and the Individual Defendants erroneously argue that they did not "solicit" the purchase of Converium securities. *See* ZFS Mem. at 30-32; Converium Mem. at 31-34. This argument is belied by the facts alleged in the Complaint. *See* ¶¶261, 262, 270. "In connection with the IPO, and pursuant to the Registration Statement and Prospectus, ZFS sold 40 million shares of Converium in the form of shares and ADSs, representing its entire stake in the Company, for proceeds of approximately $1.9 *billion*." ¶21. There can be no doubt that ZFS was "motivated at least in part by a desire to serve [its] own financial interests." *Pinter*, 486 U.S. at 647.

As far as Converium and the Individual Defendants are concerned, "[a]n officer or director who signs a Registration Statement containing materially false or misleading statements or omissions is deemed, for pleading purposes, to have solicited a purchase within the meaning of this section." *In re Flag Telecom Holdings, Ltd. Sec. Litig.*, 352 F. Supp. 2d 429, 454 (S.D.N.Y. 2005) (emphasis added) (citing *Degulis v. LXR Biotechnology, Inc.*, 928 F. Supp. 1301 (S.D.N.Y. 1996)); *see also In re OPUS360 Corp. Sec. Litig.*, No. 01 Civ. 2938, 2002 WL 31190157, at *10 (S.D.N.Y. Oct. 2, 2002) ("It is significant that the officers and directors of OPUS signed the registration statement that is the basis of the plaintiffs' claim.") (citations omitted); *id.* ("The signing of a registration statement is significant for purposes of finding that an issuer is a seller, even in the context of a firm commitment underwriting.").[21]

[21] It is worth noting that a corporation can act only through the actions of natural persons and therefore the actions of its agents, acting within the scope of their agency, are attributed to the corporation. *See Affiliated Ute Citizens v. United States*, 406 U.S. 128, 154 (1972) (liability of

Signing the Registration Statement is more than sufficient at the pleading stage for two reasons. First, as the Supreme Court held in *Gustafon v. Alloyd Co.*, 513 U.S. 561 (1995), "the term prospectus refers to a document soliciting the public to acquire securities." *Id.* at 574 (emphasis added). "Courts have concluded that because the prospectus itself is a document that solicits the purchase of securities, those who sign the registration statement should be deemed persons who solicited the purchase of the offered securities." *In re APAC Teleservice, Inc. Sec. Litig.*, No. 97 Civ. 9145, 1999 WL 1052004, at *11 (S.D.N.Y. Nov. 19, 1999) (citations omitted).

Second, whether a company or its officers and directors were, in fact, motivated at least in part by a desire to serve its/his own financial interests should only be decided on a fully developed record. *See Pinter*, 486 U.S. at 624 (vacating and remanding case because "[t]he record is insufficient to determine whether Dahl may be liable as a statutory 'seller'"); *see also Capri*, 856 F.2d at 479 ("Based on the record before us, we are unable to determine whether [the defendant] made any such solicitations. Accordingly, we remand to the district court for further factual findings on this issue.") (remanded after a bench trial). Moreover, while it is theoretically possible that a defendant signed a document and yet had no financial motivation, such a scenario is highly unlikely.

Nonetheless, Converium and the Individual Defendants attempt to encourage this Court to split with other courts in this District and follow decisions of the Third and Fifth Circuits and hold that signing a registration statement is not sufficient at the pleading stage. *See* Converium

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bank for violations of § 10(b) and Rule 10b-5 is co-extensive with that of its employees). Thus, when Lead Plaintiffs refer to the conduct, actions, or scienter of Converium, they are referring to the conduct of the Company's employees which, of course, includes the Individual Defendants. *See SEC v. Ballesteros Franco*, 253 F. Supp. 2d 720, 728-29 (S.D.N.Y. 2003); *S.E.C. v. Lum's Inc.*, 365 F. Supp. 1046, 1061 (S.D.N.Y. 1973) (noting "it is difficult to conceive of a corporation acting in any other way than by its managing officers and directors").

Mem. at 34 n.24. Defendants' invitation should be rejected out of hand, however, for two reasons. First, those decisions pay no heed to those decisions, including the Supreme Court's opinion in *Gustafon*, 513 U.S. at 574, which held that a registration statement and prospectus are designed to solicit the public to acquire securities, as each defendant who signed the document must have known. Second, the decisions by the Third and Fifth Circuit disregard the fact that both the Supreme Court and Second Circuit have been cautious about deciding a defendant's true motivation without a fully developed record. Far from being well reasoned, the Defendants' argument ignores the procedural posture of their motions to dismiss. Thus, there is no compelling reason to split with the decisions of the courts in this District – signing a document designed to solicit the purchase of securities is sufficient to plead a Section 12(a)(2) claim against a defendant.

Accordingly, ZFS, Converium, the Individual Defendants, and the Underwriter Defendants are liable under Section 12(a)(2).

C. The Court Should Not Determine the Scope of the Class on a Motion to Dismiss

The Underwriter Defendants and ZFS also argue that the Court should dismiss the Section 12(a)(2) claims of certain purchasers of the putative class. *See* Underwriters Mem. at 39; ZFS Mem. at 33-34. The argument is obviously convoluted and misleading, and at best, premature, as the Underwriter Defendants rely on the statutory language Section 11 – not Section 12(a)(2) – to make their argument. *See id.* (quoting Section 11(e)).

Section 12(a)(2), and not the Defendants, determines the damages that members of the class should receive for violations of the statute. *See* 15 U.S.C. § 77l(a)(2) (stating that purchasers of a security may "recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for

damages if he no longer owns the security.") (emphasis added); *see also Commercial Union Assurance Co. v. Milken*, 17 F.3d 608, 615 (2d Cir.1994). Thus, the Court should not prematurely dismiss the claims of any putative class member based on Defendants' speculation that they may not have been injured. The scope and size of the putative class should be resolved by this Court on a motion for class certification, not a motion to dismiss the Lead Plaintiffs' Complaint.

VI. THE COMPLAINT STATES A CAUSE OF ACTION UNDER SECTION 10(b) OF THE EXCHANGE ACT

The Complaint alleges claims arising under Section 10(b) of the Exchange Act against ZFS (solely for the false and misleading statements contained in the Registration Statement and Prospectus), and Converium and the Officer Defendants. All Defendants have moved to dismiss this claim on the grounds that the Complaint does not adequately allege scienter. In addition, Defendant ZFS has moved to dismiss this claim on the grounds that (1) none of the allegedly false statements are attributable to it, but to Converium and the Officer Defendants; and (2) the Complaint fails to plead loss causation as to the false statements in the Registration Statement and Prospectus. As set forth below, these arguments are incorrect.

A. ZFS Is Liable for "Making" the Material Misrepresentations Because The Statements are Publicly Attributable To ZFS

Defendant ZFS, Converium's parent corporation prior to and at the time of the IPO, ¶¶21, 278-327, contends that the Second Circuit's ruling in *Wright v. Ernst & Young, LLP*, 152 F.3d 169 (2d Cir. 1998) compels dismissal of Lead Plaintiffs' Section 10(b) claim because the Complaint does not allege that any material misstatements are publicly attributable to it, but are instead statements made solely by Converium and the Officer Defendants. It should be noted that, even if ZFS's argument is accepted, it is still liable as a control person for Converium's

violations of the Exchange Act. ZFS Mem. at 35-36. However, Defendant's argument is contradicted by Second Circuit law, and the plain allegations of the Complaint.

Although the *Wright* court adopted a bright-line rule stating that in order to state a Section 10(b) misrepresentation claim, a plaintiff must allege that "the misrepresentation ... be attributed to [the defendant] at the time of public dissemination, that is, in advance of the [plaintiff's] investment decision," (*id.* at 175), in a subsequent ruling, the Second Circuit in *Scholastic*, held that a defendant can be held liable pursuant to Section 10(b) for a false and misleading statement even if the statement at issue was not attributed to the defendant at the time of its public dissemination. 252 F.3d 63, 75-76 (2d Cir. 2001). Indeed, the *Scholastic* court held that the complaint properly pled a primary violation of Section 10(b) by the defendant company's vice president where facts were alleged demonstrating that: (1) the company had disseminated false and misleading statements to its investors; (2) the defendant had primary responsibility for the company's communications with investors and securities analysts; and (3) the defendant "was involved in the drafting, producing, reviewing and/or disseminating of false and misleading statements."

Interestingly, the *Scholastic* decision did not refer to *Wright*, and no subsequent Second Circuit panel has attempted to synthesize the two decisions. In the absence of guidance from the Second Circuit, a number of district courts have held that *Scholastic* did not significantly alter the public attribution rule articulated in *Wright*. *See, e.g., In re Parmalat Sec. Litig.*, 376 F. Supp. 2d 472 (S.D.N.Y. 2005) (stating that the *Scholastic* court "did not question, let alone purport to set aside, the attribution rule set forth in *Wright* . . . ."). Other courts have adopted the view that *Scholastic* relaxed *Wright*'s public attribution requirement. *See, e.g., SEC v. PIMCO Advisors Fund Mgmt. LLC*, 341 F. Supp. 2d 454, 466 (S.D.N.Y.2004).

This Court's recent decision in *LaBranche* is particularly instructive on the issue of the public attribution of misstatements. In *LaBranche*, the defendant corporate subsidiary, LaBranche, LLC, asserted that it could not be subject to primary liability for statements made by its corporate parent, LaBranche & Co. 2005 WL 3411771 at 14. The Court, rejecting the defendants' argument, held that:

> Under these facts, it is reasonable to infer that LaBranche LLC's financial data were incorporated directly into LaBranche & Co.'s public statements regarding the earnings of its specialist operations. Therefore, even though LaBranche & Co. failed to explicitly identify LaBranche LLC as the source of the information concerning revenue and earnings of its specialist operations, the misrepresentations may be constructively attributed to LaBranche LLC.

Id. at 16 (citing *Global Crossing*, 322 F. Supp. 2d at 333 n.14 (noting that a rule of constructive attribution comports with the Second Circuit's emphasis on reliance)).

In reaching its decision, the *LaBranche* court recognized that the resolution of this issue hinged in large measure upon the application of the Supreme Court's holding in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994) and the "useful synthesis" of the *Wright* and *Scholastic* decisions found in *Global Crossing*, 322 F. Supp. 2d at 330-32. *Id.* The court in *Global Crossing* held that :

> [A] plaintiff may state a claim for primary liability under section 10(b) for a false statement (or omission), even where the statement is not publicly attributed to the defendant, where the defendant's participation is substantial enough that s/he may be deemed to have made the statement, and where investors are sufficiently aware of defendant's participation that they may be found to have relied on it as if the statement had been attributed to the defendant. (Emphasis added).

322 F. Supp. 2d at 332-333 (citing *In re Lernout & Hauspie Sec. Litig.*, 230 F. Supp. 2d 152 (D.Mass. 2002)) (emphasis added).

Thus, the *LaBranche* court reasoned that:

> Under the circumstances, the misstatements -- namely quarterly and annual reporting of principal trading revenues and profits for LaBranche & Co.'s specialist activity -- could

> have come only from LaBranche LLC. In other words, when LaBranche & Co. disseminated financial information to the public regarding its specialist operations, it related only to the activity of LaBranche LLC and could have been provided only by LaBranche LLC.

Id. at 16. The Court further reasoned that because LaBranche & Co. referred only to the activity of LaBranche LLC in reporting its specialist earnings, "investors may be deemed to have been 'sufficiently aware of [LaBranche LLC's] participation that they may be found to have relied on it as if the statement[s] had been publicly attributed to [it].'" *Id.* (citing *Global Crossing*, 322 F. Supp. 2d at 332).[22]

In light of these rulings, it is clear that Lead Plaintiffs' allegations sufficiently establish that the misstatements in the Registration Statement and Prospectus are publicly attributable to defendant ZFS. Specifically, Lead Plaintiffs allege that at the time of the IPO, Converium was a wholly-owned subsidiary of ZFS. ¶21.[23] Lead Plaintiffs further allege that ZFS desperately wanted to spin-off Converium because of problems with the North America book of business. ¶¶68-72. Importantly, Lead Plaintiffs allege that ZFS "participat[ed] in the preparation" of the Prospectus and is liable for the false statements contained in the Registration Statement and

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[22] "To hold otherwise would enable parent companies to create subsidiaries under which all of its business would be conducted and then to shield the subsidiaries from section 10(b) liability by disseminating the subsidiary's false information." *Id.* (citing *Global Crossing*, 322 F. Supp. 2d at 333 (holding that the strict requirement of public attribution would allow those primarily responsible for making false statements to avoid liability by remaining anonymous and thus would place a premium on concealment and subterfuge rather than on compliance with the federal securities laws.)). *See also In re Vivendi Universal S.A. Sec. Litig.*, No. 02 Civ. 5571 (HB), 2003 WL 22489764, at *25 (S.D.N.Y. Nov. 3, 2003) (sustaining claim against CFO for public statements made by company but not specifically attributed to him); *Lernout & Hauspie*, 230 F. Supp. 2d at 166-67 (sustaining claims against auditor where auditor's role was widely disseminated to the public and it was "appropriate to infer that ... investors reasonably attributed the statements" to the auditor); *In re Livent, Inc. Noteholders Sec. Litig.*, 174 F. Supp. 2d 144, 152 (S.D.N.Y. 2001) (holding broker potentially liable for "structuring and keeping secret the misrepresented [relationship]" between the underwriter and the company).

[23] In fact, Converium has referred to ZFS as its "parent." ¶187.

Prospectus. ¶¶261, 319. Similarly, the press release issued on September 6, 2001, which publicly announced the IPO, was issued jointly by ZFS and Converium. That press release contained specific representations about Converium's 2001 financial results and the adequacy of its reserves, and stated that "ZFS management believes that an IPO will create the most value for ZFS shareholders." ¶88. Accordingly, these allegations are sufficient to demonstrate that ZFS' "participation is substantial enough that [it] may be deemed to have made the statement[s]." *See Global Crossing*, 322 F. Supp. 2d at 333. Moreover, the facts presented here are quite similar to those in *LaBranche*, with the only difference being that in the case at bar, it is the subsidiary's statements that are being attributed to the parent corporation. Thus, under *Wright*, *Scholastic*, *Global Crossing*, and *LaBranche*, it is clear that the foregoing allegations sufficiently establish that these misstatements are publicly attributable to ZFS as well as Converium.

B. Lead Plaintiffs Have Properly Alleged Causation

1. Lead Plaintiffs Have Pled Reliance

It is well settled that reliance is an element of a Rule 10b-5 cause of action. *See Basic Inc. v. Levinson*, 485 U.S. 224, 243 (1988). Where there has been a material misrepresentation or omission pertaining to securities that trade in a developed market, "the plaintiff may meet its burden of proof through a 'fraud on the market' presumption of reliance on market price." *Black v. Finantra Capital, Inc.*, 418 F.3d 203, 209 (2d Cir. 2005) (citing *Basic*, 485 U.S. at 247 and *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 153-54 (1972)). The "fraud on the market" theory entitles plaintiffs "to a rebuttable presumption of reliance based on the notion that 'in an open and developed securities market, the price of a company's stock is determined by the available material information.'" *Securities Investor Protection Corp. v. BDO Seidman, LLP*,

222 F.3d 63, 72 n.5 (2d. Cir. 2000) (quoting *Basic Inc.*, 485 U.S. at 241 (internal quotation marks omitted)).

The determination of whether a market is efficient is a question of fact that cannot be resolved under Rule 12(b)(6). "The question of whether securities were traded in an efficient market should not be decided on a motion to dismiss." *IPO Litigation*, 241 F. Supp. 2d. at 377 (citing *RMED Int'l, Inc. v. Sloan's Supermarkets, Inc.*, 185 F. Supp. 2d 389, 404 (S.D.N.Y. 2002) (deciding applicability of fraud on the market doctrine at summary judgment)). Thus, at the pleading stage of the litigation, plaintiffs need only allege that the subject securities traded in an efficient market to benefit from the presumption of reliance. "The question on a motion to dismiss is not whether plaintiff has proved an efficient market, but whether he has pleaded one." *Parmalat*, 376 F. Supp. 2d at 508-509 (emphasis added; citations omitted) (Kaplan, J.). *See also Ellison v. American Image Motor Co., Inc.*, 36 F. Supp. 2d 628, 643-44 (S.D.N.Y. 1999) ("At this [motion to dismiss] stage in the litigation, before discovery has even commenced, I am not prepared to hold as a matter of law that the allegations [that the fraud on the market doctrine applies] fail."); *In re Laser Arms Corp. Sec. Litig.*, 794 F. Supp. 475, 490 (S.D.N.Y.1989) ("Whether in fact Laser Arms traded in an efficient market is a question of fact. Therefore, resolution of that issue must await presentation of further proof at trial.").

Here, Lead Plaintiffs alleged that they and the Class are "entitled to the presumption of reliance established by the fraud-on-the-market doctrine" because Converium's common stock and ADSs traded on efficient markets.[24] ¶45. Specifically, Converium's ADSs traded on the New York Stock Exchange and its common stock traded on the SWX Swiss Exchange, both of

[24] Converium stock and ADSs immediately began trading on these established exchanges on the day of the IPO. ¶91.

which are highly efficient markets. *Id.* Moreover, Converium filed periodic public reports with the SEC and the Company's common stock and ADSs were followed by numerous securities analyst firms including Banc of America, J.P. Morgan and Credit Suisse First Boston. *Id.* These allegations are sufficient to entitle Lead Plaintiffs to the presumption of reliance.

Defendant ZFS's argument that there was not an efficient, well-developed market for Converium's securities at the time of the IPO ignores the well-pled allegations of the Complaint and presents an issue of fact that cannot be resolved at this stage of the litigation. ZFS Mem. at 37. To the extent that ZFS contends that the fraud on the market theory does not apply to initial public offerings, its argument fails as a matter of law. *Werner v. Satterlee, Stephens, Burke & Burke*, 797 F. Supp. 1196, 1215 (S.D.N.Y. 1992) ("Defendant's argument that the fraud on the market theory is not applicable to the IPO is unavailing"); *In re Proxima Corp. Sec. Litig.*, 1994 WL 374306 (S.D. Cal. May 3, 1994) ("the fraud-on-the market presumption applies to IPOs") (citing *In re VeriFone Sec. Litig.*, 11 F.3d 865, 868 n.3 (9th Cir.1993)). Indeed, ZFS fails to cite any controlling precedent in support of its argument.[25] In fact, ZFS's only citation to case law in this Circuit is to dicta in a footnote in the district court's class certification opinion in *Berwecky v. Bear, Stearns & Co.*, 197 F.R.D. 65, 69 n.5 (S.D.N.Y. 2000). While *Berwecky* suggests that the fraud on the market theory should not apply to an IPO, the Court's reasoning in *Werner* is much more persuasive. *See Werner*, 797 F. Supp. at 1215.

[25] ZFS's parallel contention, that "the Complaint has not pled any facts suggesting when (if ever) and how the markets" for the Converium securities became well-developed, is utter nonsense. ZFS Mem. at 38. Courts that have applied the fraud on the market theory to IPOs have explicitly rejected this argument. *See IPO Litigation*, 241 F. Supp. 2d at 376-377 ("The increased ability of the market to quickly assimilate information from a wider array of sources tips the balance more heavily in favor of applying the efficient market hypothesis in these cases.").

2. Lead Plaintiffs Have Pled Loss Causation

On July 20, 2004, Converium announced that it would take a charge to earnings of at least $400 million to increase its loss reserves, decimating the price of the Company's publicly traded securities which fell by nearly 50% in a single day of trading. ¶5. The price of Converium ADSs plummeted from $25.02 to $12.61 per ADS, while Converium shares dropped from 66.10 CHF per share to 59.50 CHF, both on heavy trading volume. *Id.* This disclosure (and the Company's subsequent announcement that the charge would exceed $560 million), caused a market capitalization loss of nearly $1 billion and set off a chain of events that soon brought about the demise of Converium North America. ¶¶53, 164, 210.

Despite the obvious connection between the July 20 announcement and Lead Plaintiffs' allegations that Converium was under-reserved since its IPO, Defendant ZFS asserts that Lead Plaintiffs have failed to properly plead loss causation. ZFS Mem. at 40. In essence, ZFS argues that its pre-IPO conduct could not have been the legal cause of the Class' losses at the end of the Class Period because, it contends, "intervening causes" such as Converium's post-IPO losses as well as general "difficulties" in the insurance industry break the causal connection. *Id.* at 41-42. However, this argument presents a question of fact that cannot be resolved at this stage. Courts in the Second Circuit have repeatedly held that the question of whether intervening events broke the chain of causation is "a matter for proof at trial." *WorldCom*, 2005 WL 375314, at *6 (quoting *Emergent Capital Investment Management, LLC v. Stonepath Group*, Inc., 343 F.3d 189, 197 (2d Cir. 2003)) (emphasis added); *see also Lentell*, 396 F.3d at 174 ("[I]f the loss was caused by an intervening event, like a general fall in the price of Internet stocks, the chain of causation ... is a matter of proof at trial and not to be decided on a Rule 12(b)(6) motion to dismiss" (citing *Emergent Capital*, 343 F.3d at 197)).

At this early stage of the litigation, Lead Plaintiffs are simply required to "alleg[e] either that (1) 'the market reacted negatively to a corrective disclosure regarding the falsity' of the defendant's misstatements, or (2) that the defendant 'misstated or omitted risks that did lead to the loss.'" *In re The Warnaco Group, Inc. Sec. Litig. II*, 388 F. Supp. 2d 307, 317 (S.D.N.Y. 2005) (quoting *Lentell*, 396 F.3d at 175)). In other words, a plaintiff must allege that the "misrepresentation[s] (or other fraudulent conduct) proximately caused the plaintiff[s'] economic loss." *In re NYSE Specialists Sec. Litig.*, No. 03 Civ. 8264 (RWS), 2005 WL 3411776, at *28 (S.D.N.Y. Dec. 13, 2005) (citing *Dura Pharmaceuticals, Inc. v. Broudo*, __ U.S. __, __, 125 S. Ct. 1627, 1633 (2005)). It should be noted that Federal Rule of Civil Procedure 8(a)(2), and not Rule 9(b), controls the pleading of loss causation allegations, as there is no "special further requirement in respect to the pleading of proximate causation or economic loss." *NYSE Specialists*, 2005 WL 3411776 at *28 (citing *Dura*, 125 S.Ct. at 1634).[26]

The Second Circuit has acknowledged that these pleading principles require that the loss be foreseeable and caused by the materialization of the concealed risk. *Lentell*, 396 F.3d at 172; *see First Nationwide Bank*, 27 F.3d at 769 (loss causation requires a showing "that the misstatements were the reason the transaction turned out to be a losing one"); *Citibank, N.A. v. K-H Corp.*, 968 F.2d 1489, 1495 (2d Cir. 1992) ("To establish loss causation a plaintiff must show, that the economic harm that it suffered occurred as a result of the alleged misrepresentations."). However, a plaintiff "is not required to prove that defendant's act was the sole and exclusive cause of his injury; he need only show that it was substantial, i.e., a significant contributing cause." *Parmalat*, 376 F. Supp. 2d at 509 (citing *Wilson v. Comtech Telecomms. Corp.*, 648 F.2d 88, 92 (2d Cir. 1981)).

[26] Defendant ZFS incorrectly asserts that Federal Rule of Civil Procedure 9(b) controls. *See* ZFS Brief at 41.

Lead Plaintiffs adequately allege the direct causal connection between the revelation of the truth and their losses. Indeed, the Complaint details the market's reaction to the Company's July 20, 2004 press release, and the Company's subsequent announcements through the end of the Class Period, which destroyed the value of the Company's securities. ¶¶208-19. *Id.* The Complaint further alleges that these disclosures revealed to the market the truth about the Company's reserve deficiency, which stood in the hundreds of millions of dollars from the date of the Company's IPO. Clearly, these allegations are sufficient to plead loss causation.

VII. LEAD PLAINTIFFS HAVE ALLEGED HIGHLY PARTICULARIZED FACTS GIVING RISE TO A STRONG INFERENCE OF SCIENTER[27]

To state a claim under Section 10(b) of the Exchange Act, a plaintiff must "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2). For purposes of a Rule 10b-5 claim, the "requisite state of mind," is scienter: "an intent to deceive, manipulate or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 n.17 (1976); *see also In re BISYS Securities Litig.*, 397 F. Supp. 2d 430, 437 (S.D.N.Y. 2005).

Lead Plaintiffs may establish scienter by alleging facts that (1) constitute strong circumstantial evidence of conscious misbehavior or recklessness, or (2) show that defendants had both the motive and opportunity to commit fraud. *See Novak v. Kasaks*, 216 F.3d 300, 307 (2d Cir. 2000). "If the totality of the circumstances alleged raises a 'strong inference' of the requisite state of mind, it is immaterial whether plaintiffs satisfy their burden by 'pleading motive and opportunity, conscious misbehavior, recklessness, or by impressing upon the Court a novel legal theory.'" *In re MicroStrategy Inc. Sec. Litig.*, 115 F. Supp. 2d 620, 631 (E.D. Va.

[27] This Section only applies to the Defendants against whom Exchange Act claims have been asserted: Converium, ZFS and the Officer Defendants.

2000) (quoting *Acito v. IMCERA Group, Inc.*, 47 F.3d 47, 52 (2d Cir. 1995)). Under the securities laws, "recklessness" includes "conduct which is highly unreasonable and which represents an extreme departure from the standards of ordinary care", *Benjamin v. Kim*, No. 95 Civ. 9597 (LMM), 1999 WL 249706, at *8 (S.D.N.Y. April 28, 1999) (quotations omitted); *see also Rothman v. Gregor*, 220 F.3d 81, 90 (2d Cir. 2000).

"Although the inference of scienter must be reasonable and strong, it need not be irrefutable." *In re Regeneron Pharm., Inc. Sec. Litig.*, No. 03 CV 3111, 2005 WL 225288, at * 24 (S.D.N.Y. Feb. 1, 2005). "Plaintiffs need not foreclose all other characterizations of fact, as the task of weighing contrary accounts is reserved for the fact finder." *Id.* (quoting *Aldridge v. A.T. Cross Corp.*, 284 F.3d 72, 83 (1st Cir. 2002)). The Court, in determining whether the Complaint alleges facts giving rise to a strong inference of scienter, must read the Complaint "in toto and most favorably to plaintiff." *In re Complete Mgmt. Sec. Litig.*, 153 F. Supp. 2d 314, 333 (S.D.N.Y. 2001); *see also WorldCom*, 294 F. Supp. 2d at 417 ("The allegations in the Complaint are entitled to be taken together to determine if the facts 'give rise to a strong inference of fraudulent intent.'").

A. Defendants Either Knew Or Recklessly Disregarded The Fact That Converium Was Under-Reserved By Hundreds Of Millions Of Dollars

A plaintiff can show conscious misbehavior or recklessness by alleging a defendant's "knowledge of facts or access to information that contradict[ed] the [defendants'] public statements," or by alleging that "Defendants failed to review or check information [that] they had a duty to monitor, or ignored obvious signs of fraud." *Novak*, 216 F.3d at 308; *see also Scholastic*, 252 F.3d at 76; *SEC v. Price Waterhouse*, 797 F. Supp. 1217, 1240 (S.D.N.Y. 1992) (recklessness is the "egregious refusal to see the obvious, or to investigate the doubtful") (internal citations omitted). Here, it is clear that the Complaint alleges that the Defendants knew,

or at minimum recklessly disregarded, the fact that Converium was grossly under-reserved throughout the Class Period.

1. Defendants Were Directly Informed Of The Reserve Deficiency

The Complaint alleges that Defendants Smith, Lohmann and Kauer were directly informed, on numerous occasions, that Converium was massively under-reserved. Specifically:

- In April 2001, Tillinghast reported to Defendants Smith, Lohmann and Kauer that Converium North America was under-reserved by $350 million. ¶82. According to Confidential Witness No. 1, the Company's senior management and its actuaries knew that this conclusion was accurate. ¶86. Indeed, internal Company documents disseminated to the Officer Defendants specified the extent of the deficiency in each of Converium's lines of business. ¶83. Lohmann's and Kauer's knowledge of Tillinghast's conclusion is evidenced by the fact that they determined that Converium could not take such a massive charge and still complete the IPO, and ordered Defendant Smith and the North American actuaries to dupe Tillinghast into revising its conclusion. ¶86. Despite the fact that the Company "pulled a fast one" by conning Tillinghast into revising its determination to find that the deficiency was just $125 million, these Defendants knew that the Company remained under-reserved by at least $225 million at the time of the IPO.

- Each quarter during the Class Period, Defendant Smith presented to Defendants Lohmann and Kauer the Loss Reserve Study prepared by Converium's North American Actuaries, which consistently identified a significant reserve deficiency. ¶¶58, 76, 77. When the North American actuaries identified an additional $80 million in adverse loss development shortly after the IPO, and additional loss development for each quarter in 2002, Defendant Smith reported those developments directly to Defendants Lohmann and Kauer. ¶¶103, 104.

- Confidential Witness No. 2 provided Defendants Lohmann, Kauer and Smith with the results of his own reserve study, conducted independently of the quarterly Loss Reserve Study, which consistently showed a reserve deficiency roughly $100 million greater than that identified by the Loss Reserve Study. ¶¶100, 101.

- Converium's Global Reserving Actuary concluded that Converium North America was under-reserved by approximately $300 million as year-end 2002, and reported that conclusion to Defendants Lohmann, Kauer and Smith. ¶¶106, 107.

- Internal Converium documents show that the North American reserve deficiency increased by $339.9 million during the first half of 2003. ¶120. Deloitte's conclusions corroborated the extent of that loss development. ¶121.

- In May 2003, Deloitte reported that it had identified a reserve deficiency of $437 million as of year-end 2002, and additional adverse loss development of $334.1 million for the first half of 2003. ¶¶114, 122. Deloitte's conclusions were detailed in a May 28, 2003 e-mail sent by the Chief Reserving Actuary at Converium North America to the Company's senior executives. ¶114.

- In response to this massive reserve deficiency, in the second half of 2003, Defendant Lohmann devised a scheme to cook the Company's books by novating Converium North America's worst contracts to Europe while secretly increasing the North American reserves by more than $100 million – all without any disclosure to investors. ¶¶128-138. To conceal the impact of these machinations, Converium changed its reporting structure and ceased reporting financial results by geographic region. ¶¶123-127.

- Even with these novations and secret reserve increases, the Company remained under-reserved. On October 26, 2003, the Company's Global Reserving Actuary sent an e-mail to Defendants Lohmann, Kauer and Smith, as well as other senior Converium executives, stating that, despite Defendant Lohmann's machinations, Converium North America remained under-reserved by $300 million. *Id.*

- When the novation scheme and secret reserve increases failed to correct the reserve deficiency, Defendants Lohmann and Kauer ordered actuaries to "bury" tens of millions of dollars adverse lose development. ¶¶134-136, 204-206. When the Chief Reserving Actuary refused to bury additional loss development in the second quarter of 2004 (after having already buried $45 million in the fourth quarter of 2003), Defendant Lohmann stated "we're going to announce this all in the third quarter, we just want to put another good quarter under our belt." ¶204.

These uncontested and particularized allegations establish "'in your face facts,' that cry out, 'how could [defendants] not have known that the financial statements were false.'" *In re Oxford Health Plans, Inc. Sec. Litig.*, 51 F. Supp. 2d 290, 294 (S.D.N.Y. 1999). Indeed, if these well-pled, highly particularized facts are not sufficient to establish a strong inference of scienter, then it is difficult to imagine what allegations would. The fact that Defendants Lohmann, Kauer and Smith were directly informed of the reserve deficiency by Tillinghast in April 2001, by Deloitte in May 2003 and by the Global Reserving Actuary on October 26, 2003, are alone sufficient to sustain Lead Plaintiffs' Exchange Act claims.

Tellingly, Defendants do not argue that the direct notice they received of the reserve deficiency does not demonstrate scienter. Instead, they ask the Court to ignore the well pled

allegations in the Complaint and accept Defendants' own version of the facts. Converium Mem. at 47-48. Once again, Defendants argue that the Company was adequately reserved during the Class Period, and ask the Court to consider other non-public, internal documents which Lead Plaintiffs never reviewed and which are not referenced in the Complaint. These documents include purportedly "final" reports prepared by Tillinghast and Deloitte, including the report Tillinghast prepared after Defendants "pulled a fast one." ¶87. As stated above, and in Lead Plaintiffs' Motion to Strike, these documents only serve to create clear issues of fact, and may not be considered at this stage of the proceedings. The Court is bound by Rule 12(b)(6) and well-established precedent to accept as true Lead Plaintiffs' allegations, which are highly detailed and based upon the statements of witnesses and on internal Company documents. *See Chambers v. Time Warner, Inc.*, 282 F.3d 147, 153 (2d Cir. 2002); *S.E.C. v. McDermott*, No. 99 Civ. 12256 (MBM), 2004 WL 385197, at *2 (S.D.N.Y. March 1, 2004) (Mukasey, J.).

Moreover, even if these reports are considered, they are of no moment. In arguing that the Court should disregard Tillinghast's conclusion that Converium was under-reserved by $350 million, Converium and the Officer Defendants ignore Lead Plaintiffs' allegation that Defendants "pulled a fast one" on Tillinghast to con it into signing-off on a number pre-determined by Defendants Lohmann and Kauer. ¶¶86, 87. There can be no question that, based on the statements of Confidential Witness No. 1, who participated in the deception of Tillinghast at the instruction of Defendant Smith, the Complaint alleges that Tillinghast was duped. *Id.* The subsequently rendered opinion on which Defendants rely is simply the product of Defendants' fraud, and cannot be relied upon to contradict Lead Plaintiffs' allegations. There is no basis to disregard Lead Plaintiffs' well-pled allegations and accept Defendants' alternate version of the facts at this stage of the litigation.

Curiously, Defendants also argue that Deloitte ultimately concluded in September 2003 that Converium North America was under-reserved by "only" $172 million. Converium Mem. at 48. However, rather than showing that Converium North America was adequately reserved, this is further evidence that Defendants were aware of a massive reserve deficiency. Defendants' argument that this material deficiency can be disregarded because, they claim, the Company had excess reserves on a consolidated basis, is not only an issue of fact, but directly belied by the fact that, after Deloitte issued its report. The assertion is also contradicted by the fact that Converium's Global Reserving Actuary sent an e-mail to Lohmann and Kauer which contradicted Deloitte's "conclusion" and confirmed that Converium North America was under-reserved by $300 million. ¶132-33. Defendants announced that the Company would take a charge of $400 million to correct its North American reserve deficiency less than nine months after Deloitte issued its report. ¶208. This issue of disputed facts cannot be resolved prior now, and further demonstrates why consideration of Defendants' extraneous facts and documents is inappropriate under Rule 12(b)(6).[28]

Defendants also attempt to downplay each of the instances, set forth above, in which they were directly provided with detailed reports of the Company's reserve deficiency. Converium Mem. at 46-54. For example, Defendants suggest that the e-mail sent by the Company's Global Reserving Actuary to Defendants Lohmann, Kauer and Smith in 2003 provided only a

[28] Significantly while Defendants place great weight on their assertions that Deloitte and Tillinghast subsequently changed their conclusions, they fail to provide any reason or explanation as to why Tillinghast and Deloitte abandoned their original conclusions and changed their opinions by such staggering amounts. Indeed, if Defendants' version of the facts is to be believed, between April and September 2001 Tillinghast "innocently" determined that its original conclusion was wrong by $225 million, or almost 200%. Similarly, between May and September 2003, Deloitte "innocently" determined that its original conclusion was wrong by a staggering $265 million. In contrast, Plaintiffs have provided a reason for these changes: Defendants' deception. In any event, the size, timing and suspicious nature of these "revisions" clearly create issues of fact that may not be resolved on this motion.

"preliminary" analysis of the reserve deficiency as of year-end 2002. Whether or not the Global Reserving Actuary's conclusion was preliminary is clearly a question of fact that cannot be resolved on this motion. Even assuming that his conclusion was preliminary, that does not undermine its accuracy or lessen the relevance of that e-mail to inferring that Defendants acted with scienter. Further, Defendants' argument clearly contradicts the text of the e-mail. *Id.* The Complaint alleges that the e-mail stated that, as of year-end 2002, "Net Loss reserves as at 4Q02 were US$268M below Group Corporate Actuarial (CGA) preliminary estimate." ¶107. The plain text of the e-mail makes clear that the Global Reserving Actuary, Jean Claude Jacob, was comparing the final results of his own study to the preliminary results reached by Group Corporate Actuarial.

Similarly, Defendants' argument that Lead Plaintiffs failed to adequately identify this e-mail is belied by the allegations of the Complaint: Jacob e-mailed Defendants Lohmann, Kauer and Smith on October 26, 2003 with the results of his study of the loss reserves as of December 31, 2002 and the third quarter of 2003. ¶¶107, 132, 133. The date, subject line, primary recipients, and relevant content of the e-mail are all provided. *Id.* Pointedly, Defendants only question the sufficiency of the allegations in Paragraph 107 of the Complaint with regard to the 2002 reserve deficiency – they do not contest that Jacob's e-mail fully informed Defendants Lohmann, Kauer and Smith that Converium North America was under-reserved by roughly $300 million as of the third quarter of 2003.

Defendants similarly argue that the Complaint provides insufficient information regarding the presentation of the Loss Reserve Study to Defendants Lohmann and Kauer. Converium Mem. at 46. Yet the Complaint alleges in great detail that the Loss Reserve Study was prepared each quarter and at year end by the North American actuaries, including

Confidential Witness No. 1. ¶¶58, 76, 77, 100. Defendant Smith personally presented the Loss Reserve Study to Defendants Lohmann and Kauer via teleconference each quarter and at year end. *Id.* The Complaint identifies the reserve deficiency identified by the North American actuaries throughout the Class Period, including the $80 million in adverse loss development identified within weeks of the IPO, and the additional $50 million of adverse development identified each quarter during 2002. ¶¶103, 104. Indeed, the Complaint specifically alleges that Jean Claude Jacob, the Global Reserving Actuary, who participated in the meetings with Defendants Lohmann and Kauer when Defendant Smith presented the Loss Reserve Study, confirmed to Confidential Witness No. 1 that Defendants Lohmann and Kauer were informed about these massive increases to the reserve deficiency during 2002. ¶104.

In sum, the Complaint is replete with extraordinarily detailed facts establishing that ZFS and the Officer Defendants knew of the massive reserve deficiency throughout the Class Period.

2. Defendants Are Deemed To Have Knowledge Of Facts That Contradict Their Public Statements

The facts cited by Lead Plaintiffs as the basis for these allegations directly contradict statements by Defendants Lohmann and Kauer, giving further support to the inference that they acted with scienter. Defendants are deemed to have notice of such internal facts when they make contradictory statements. *In re NTL, Inc. Sec. Litig.*, 347 F. Supp. 2d 15, 28 (S.D.N.Y. 2004) ("Allegations of defendants' knowledge of facts or access to contradictory information usually are sufficient to state a claim based on recklessness."). The court in *In re Atlas Air Worldwide Holdings, Inc. Securities Litig.* discussed this rule, stating:

> If facts that contradict a high-level officer's public statements were available when the statements were made, it is reasonable to conclude that the speaker had intimate knowledge of those facts or should have known of them. Accordingly, if a plaintiff can plead that a defendant made false or misleading statements when contradictory facts of critical importance to the company either were apparent, or

> should have been apparent, an inference arises that high-level officers and directors had knowledge of those facts by virtue of their positions with the company.

324 F. Supp. 2d 474, 489 (S.D.N.Y. 2004) (citing *Cosmas v. Hassett*, 886 F.2d 8, 13 (3d Cir. 1989)); *see also In re Reliance Securities Litig.*, 91 F. Supp. 2d 706,724 (D. Del. 2000) (allegation that defendants had knowledge of deteriorating loan portfolio while reassuring investors that loan loss reserves were sufficient adequately pled scienter). Here, for example, Defendants Lohmann and Kauer signed the Company's July 30, 2003 Form 6-K, which reported that "[t]here was no material non-life prior years' reserve development in 2003," yet internal Converium documents prepared contemporaneously with that filing identified adverse loss development of $339.9 million during the first half of 2003. ¶¶120, 185.

Further, there is no merit to Defendants' argument that the Complaint does not identify exactly how or when they were informed that Deloitte had identified a $437 million reserve deficiency. Lead Plaintiffs have alleged that the Board of Directors retained Deloitte to review the Company's reserves because the Board was concerned that reserves were inadequate. Given this allegation, it is obviously reasonable to infer that the Board – and the Company's CEO and CFO – were informed of Deloitte's conclusion. Indeed, Deloitte's conclusions were hardly a well-kept secret at Converium. Lead Plaintiffs' have identified internal Converium documents proposed in April and May 2003 which informed a number of Converium senior executives of Deloitte's conclusion. These facts are clearly sufficient to establish Defendants' recklessness, because these Defendants made contemporaneous statements that are contradicted by those documents. *Compare* ¶¶114-117 (May 2003 e-mail to the Global Reserving Actuary discussing

$437 million reserve deficiency) to ¶¶182-186 (Defendants falsely report quarterly income of $59.1 million, improved profitability and a "strong reserving level").[29]

3. Defendants Are Deemed To Have Knowledge Of Facts Concerning Converium's Loss Reserves

Defendants Lohmann, Kauer and Smith, as senior officers of Converium, are deemed to have knowledge of the Company's "core operations." "Knowledge of the falsity of a company's financial statements can be imputed to key officers who should have known of facts relating to the core operations of their company that would have led them to the realization that the company's financial statements were false when issued." *Atlas Air*, 324 F. Supp. 2d at 490. *See also Epstein v. Itron, Inc.*, 993 F. Supp. 1314, 1326 (E.D. Wash. 1998) ("[F]acts critical to a business's core operations or an important transaction generally are so apparent that their knowledge may be attributed to the company and its key officers."); *Chalverus v. Pegasystems, Inc.*, 59 F. Supp. 2d 226, 233-34 (D. Mass. 1999) (same).

It is beyond dispute that the establishment and monitoring of loss reserves constitute a core operation of a reinsurance company such as Converium. ¶56-66. Converium employed teams of highly trained actuaries to monitor its reserves, which represented the single largest expense on the Company's balance sheet. ¶¶58, 61. The Company addressed the adequacy of its reserves in nearly all of its public statements, and retained independent consultants to examine the adequacy of those reserves twice in just three years. This point is further established by the numerous studies and emails regarding Converium's reserve deficiencies that were sent to the Officer Defendants.

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[29] For the same reason, Defendants' argument that the Complaint does not adequately describe the manner in which the Loss Reserve Study, or the reserve study performed by Confidential Witness No. 2, were presented to Defendants is not compelling. Given the importance of the loss reserves, the Court can infer from Lead Plaintiffs' allegations that the Defendants knew, or should have known, the results of those reserve studies.

4. The Officer Defendants' Role In Managing Converium's Reserves And Concealing The Reserve Deficiency Supports The Inference Of Scienter

The Complaint also alleges that Defendants Lohmann and Kauer took an active role in managing Converium North America's loss reserves, demonstrating that they were keenly aware that those reserves were deficient by hundreds of millions of dollars. Defendants Lohmann and Kauer were ultimately responsible for approving the reserves established by Converium North America, and the North American actuaries "didn't book anything without their ok." ¶¶58, 98. This is corroborated by Confidential Witness No. 4, who stated that "Any reserve decisions... was discussed at a very high level... It was all handled out of Switzerland." ¶99.

Further, it was Defendants Lohmann and Kauer who directed that Tillinghast acquiesce to a reserve deficiency of no more than $125 million, driving the North American actuaries to "pull a fast one" on Tillinghast. ¶¶86, 87. And it was Defendant Lohmann who devised the novation scheme and secret reserve increases that the Company implemented in the second half of 2003 to hide the massive North American reserve deficiency. ¶128. To conceal that scheme from investors, these Defendants implemented a major reorganization of the Company's reporting structure. ¶¶125, 126. Defendant Lohmann then personally ordered Converium's actuaries to simply bury millions of dollars in adverse loss development. ¶¶134-136, 204-206

Defendants argue that the novation of contracts from North America to Europe, and the reorganization of Converium's reporting structure, do not give rise to an inference of scienter. Converium Mem. at 52-53. Yet Defendants pointedly do not deny that the secret reserve increases Defendants implemented together with the novations during the second half of 2003 are clear evidence of scienter. *Id.* There can be little question that increasing the Company's reserves by $118 million without public disclosure – after the disclosure of similar reserve

increases in 2002 significantly impacted the Company's share price – provides direct evidence of Defendants' fraudulent intent. ¶131. Moreover, the Complaint clearly alleges that the novation scheme and corporate reorganization were implemented for the purpose of misleading investors. ¶¶129, 130. The fact that the Global Reserving Actuary reported to Defendants Lohmann, Kauer and Smith on the progress of the novation scheme in connection with the secret reserve increases, and in the context of the overall reserve deficiency, supports the inference that the novations were yet another facet in a broad scheme to defraud investors. ¶¶132, 133. Similarly, the Complaint alleges, based on the statements of witnesses, that the true purpose of the Company's contemporaneous reorganization was to conceal the true state of the North American reserves, and to hide the novation scheme and reserve increases being implemented to address that deficiency. ¶¶125-127.

In response, Defendants argue that the novation scheme was disclosed in a filing with the Connecticut Department of Insurance. However, this argument is based on documents and facts extraneous to the Complaint, which cannot be considered by the Court. *See* Lead Plaintiffs' Motion to Strike at 8-10. Moreover, the report Defendants submit is not readily available to the public, as evidenced by the fact that not a single analyst ever commented on the Company's novation scheme. Finally, the report fails to place the Company's novation of its North American contracts in the context provided by the witnesses and documents cited in the Complaint: Defendants novated their worst contracts as part of a larger scheme that included secret reserve increases for the express purpose of concealing a massive reserve deficiency that was never disclosed to the public. Without these critical facts, which Defendants obviously did

not provide to the Connecticut Department of Insurance, the report on which Defendants rely is simply more evidence of their efforts to conceal the true state of the Company's reserves.[30]

5. The Sheer Size Of The Reserve Deficiency Supports The Inference That Defendants Acted With Scienter

"[T]he scope of the fraud alleged may appropriately be considered in determining whether scienter has been adequately pled." *Global Crossing*, 322 F. Supp. 2d at 347. *See also Rothman v. Gregor*, 220 F.3d 81, 92 (2d Cir. 2000) (magnitude of the write-offs "renders less credible" defendants' argument that they acted without scienter); *Burstyn v. Worldwide Xceed Group, Inc.*, No. 01 Civ. 1125(GEL), 2002 WL 31191741, at *5-6 (S.D.N.Y. Sept. 30, 2002) (size of accounting adjustments supported strong inference of scienter).

The Complaint alleges that Converium's reserves were deficient by hundreds of millions of dollars throughout the Class Period, and that the deficiency grew to nearly $800 million during 2003. The magnitude of the reserve deficiency, taken together with Lead Plaintiffs' other allegations, supports the inference that Defendants acted with scienter. "The more serious the error, the less believable are defendants' protests that they were completely unaware of [the Company's] true financial status and the stronger is the inference that defendants must have known about the discrepancy." *Rehm v. Eagle Finance Corp.*, 954 F. Supp. at 1256 (finding scienter was adequately pled where defendants had to record a massive year-end increase in credit loss reserves slashing its reported earnings soon after assuring investors that its reserves were adequate) (citing *In re Leslie Fay Companies, Inc. Securities Litig.*, 835 F. Supp. 167, 175 (S.D.N.Y. 1993) ("the magnitude of reporting errors may lend weight to allegations of

[30] Similarly, the passing reference made to "the novation of certain contracts from North America to Switzerland" in Converium's 2003 Form 20-F did not disclose the timing, amount or purpose of the novations, or explain that the Company was novating its worst contracts to get them off North America's books. Nor did the 20-F disclose the Company was secretly increasing Converium North America's reserves as part of this fraudulent scheme.

recklessness where defendants were in a position to detect the errors"). The charge taken by the Company to redress its reserve deficiency – first announced as a $400 million charge on July 20, 2004 – ultimately grew to a staggering $562 million, resulting in a loss for the year of $761 million. ¶217. The change meant that Converium's reserves during the Class Period were deficient by a staggering 25%. Viewed in the context of Converium's reported financial results during the Class Period, the magnitude of the Company's fraud is undeniable:

- Had Converium increased reserves by the $350 million Tillinghast determined necessary to establish adequate reserves, the Company's true loss for 2000 would have been nearly $380 million, rather than the $29.3 million the Company reported. ¶85;

- As a result of a $350 million reserve deficiency as of December 31, 2001, the net income reported by Converium for 2001 was overstated by over 80%. ¶150; and,

- Because Converium was under-reserved by at least $437 million at the conclusion of 2002, it should have reported a loss of as much as $337 million, rather than the net income of over $100 million that the Company reported. ¶172.

6. GAAP Violations Support The Inference That Defendants Acted With Scienter

The Complaint alleges that Defendants violated Generally Accepted Accounting Principles ("GAAP") by failing to properly account for Converium's massive reserve deficiency. ¶¶220-233. While GAAP violations alone do not ordinarily constitute scienter, they nevertheless have "significant inferential weight in the scienter calculus." *In re Microstrategy*, 115 F. Supp. at 635; *Reina v. Tropical Sportswear Int'l.*,No. 8:03-CV-1958-T-23TGW 2005 WL 846170 at *6 (M.D. Fla. April 4, 2005) ("the allegations of false and misleading financial reporting and GAAP violations sufficiently allege scienter as to the CFOs."). That well-settled principle is particularly true where, as here, the accounting violation was large, involved a critical aspect of the Company's business and involved a basic, non-technical accounting principle. *See In re Telxon*, 133 F. Supp. 2d at 1031.

The accounting provisions that directly relate to accounting for loss reserves and unpaid claims by reinsurance companies, such as Converium, are well-established and set forth in detail in the Complaint. ¶¶222-233. Pursuant to SFAS 60, "Accounting and Reporting by Insurance Enterprises," once an insurance (or reinsurance) policy is issued, the issuing company must account for the potential loss covered by that policy as a contingency. ¶226. SFAS 5, "Accounting for Contingencies," mandates that a charge must be taken for all contingencies where "it is probable that an asset had been impaired or a liability incurred" and "[t]he amount of the loss can be reasonably estimated." ¶224 (emphasis added). SAB 87, "Contingency Disclosures on P&C Insurance Reserves for Unpaid Claims," establishes that the provisions of SFAS 5 apply to the establishment of loss reserves by reinsurance companies.

The Complaint details three internal loss reserve studies and two loss reserve studies performed by independent consultants, each of which confirmed that the Company was under-reserved by hundreds of millions of dollars. These studies concluded, at a minimum, that it was at least "probable" that the Company's assets had been impaired, and these studies provided reasonable conclusions as to the amount of that loss. For example, Tillinghast identified a reserve deficiency of $350 million as of year-end 2000, Deloitte identified a deficiency of $437 million as of year-end 2002, and Converium's Global Reserving Actuary identified a deficiency of nearly $300 million as of the third quarter of 2003. ¶¶82, 114, 133. GAAP required that the Company take a charge to account for these probable losses. It did not do so.

By concealing the Company's massive reserve deficiency, Defendants violated a host of general GAAP provisions, expressed in FASB Statement of Concepts Nos. 1, 2, and 58-59, designed to ensure complete and accurate financial reporting. ¶232. For example, Defendants violated the principle that "that financial reporting should provide information about the

economic resources of an enterprise, the claims to those resources, and the effects of transactions, events, and circumstances that change resources and claims to those resources." *Id.* Defendants also violated the principles of completeness, which requires that "nothing is left out of the information that may be necessary to insure that it validly represents underlying events and conditions," and the principle of conservatism. *Id.* By ignoring the reports of actuaries who consistently identified a mounting reserve deficiency, and by concealing the conclusions of Tillinghast and Deloitte, which independently identified reserve deficiencies of hundreds of millions of dollars, Defendants flagrantly disregarded these controlling accounting principles.

Taken together with Lead Plaintiffs' other allegations, these violations of basic GAAP support an inference that Defendants acted with scienter.

B. Scienter is Sufficiently Pled Through Defendants' Motive and Opportunity

In addition to clear allegations of reckless or conscious misbehavior, the Complaint also establishes that Defendants had the motive and opportunity to commit fraud. Motive represents "concrete benefits that could be realized" by engaging in the fraud. *Novak*, 216 F.3d at 307. Opportunity entails a showing of "the means and likely prospect of achieving concrete benefits by the means alleged." *Id.* Allegations that the Defendants "benefited in a concrete and personal way from [the] purported fraud" may provide the requisite "strong inference" of scienter in the Second Circuit. *Id.* at 311. Defendants do not dispute that they had the opportunity to manipulate the Company's loss reserves. The Complaint demonstrates that ZFS, Converium and the Officer Defendants each had the motive to do so.

By 2001, ZFS' reinsurance business constituted a mounting liability. The reserve deficiency in North America grew so large that it subsumed any profits that could be generated from the rest of its reinsurance operations. ZFS needed to extricate itself from its unprofitable

reinsurance business, and Defendants' best opportunity to do so was through an IPO. ¶80. *In re American Bank Note Holographics, Inc.*, 93 F. Supp. 2d 424, 444-45 (S.D.N.Y. 2000) (finding sufficient motive for scienter where the parent company stood to profit from the subsidiary's successful IPO and the concrete benefit to the corporation was to extricate itself from its financial crisis).

Each of the Defendants was motivated to ensure that the IPO would be a success, in order to avoid the alternatives: selling the reinsurance business in a private transaction (in which the purchasers would conduct extensive due diligence and discover the massive reserve deficiency), or simply close down the U.S. reinsurance operations (and forego hundreds of millions of dollars in proceeds that a sale or public offering would bring). ZFS was clearly motivated to maximize its profits from the sale of its reinsurance business while avoiding extensive due diligence by a private purchaser. For Defendants Lohmann and Kauer, the IPO offered the promise of an independent company to run. Defendant Smith faced the risk that, if the IPO failed, the U.S. operations he ran would be wound down.

Yet in order to conduct a successful IPO, these Defendants needed to assure the market that the Company was adequately reserved. When Tillinghast concluded that the Company was under-reserved by $350 million, the future of the IPO was in jeopardy. Confidential Witness No. 1 confirmed that Defendants knew and openly discussed that they could not increase reserves by anywhere close to $350 million and still complete Converium's IPO. ¶84. Defendants Lohmann and Kauer determined that the IPO could go forward only if Tillinghast revised its conclusion to find that the deficiency did not exceed $125 million. ¶86. After the New York actuaries, working at the direction of Defendant Smith, "pulled a fast one," Tillinghast revised its conclusion and the IPO proceeded as planned. ¶87.

The allegations here are strikingly similar to those in *In re American Bank*, which held that the plaintiff sufficiently alleged that a parent corporation had a motive to inflate the appearance of profitability of its subsidiary where the parent company stood to profit from the subsidiary's successful IPO. 93 F. Supp. 2d at 444-45. There, the complaint alleged that the parent corporation, which was highly leveraged and suffering from debt problems, intended to use some of the proceeds from the IPO to alleviate these financial problems. *Id.* at 431. The parent was thus motivated to make statements or omit facts about its financial health in order to sell its stock at a higher IPO price. The concrete benefit to the corporation was to extricate it from its financial crisis and receive more money in the offering.

In addition to removing the reinsurance reserve deficiency from its own books, the IPO enabled ZFS to sell billions of dollars worth of Converium securities to the public. ¶91-94. Indeed, ZFS cashed out of Converium in the IPO, selling its entire stake in Converium – for proceeds of nearly $2 billion. Defendants Lohmann and Kauer became the CEO and CFO, respectively, of an independent global reinsurance company, and Defendant Smith continued to run Converium North America. These concrete benefits that Defendants realized at the expense of Lead Plaintiffs and the Class provided ample motivation to conceal the reserve deficiency and misrepresent the Company's financial condition.

Converium and the Officer Defendants attempt to confuse the clear allegations of the Complaint by suggesting that their motivation to maintain the Company's financial health is insufficient to support an inference of scienter. Converium Mem. at 43-45. In support of this argument, Defendants misplace reliance on *San Leandro Emergency Medica. Group Profit Sharing Plan v. Philip Morris Cos.*, 75 F.3d 801 (2d Cir. 1996), which is factually distinguishable from the case at bar. Converium Mem. at 44. In *San Leandro*, the court

determined that motive was not adequately pled "[i]n the context of [that] case" where some of the defendants sold stock and others did not. 75 F.3d at 814. The motive allegations here rest upon Defendants' efforts to conceal a massive reserve deficiency so that they could conduct a fraudulent $2 billion IPO, not Defendants' efforts to yield a couple extra dollars from the sale of stock. Accordingly, since the motive here is not one that is shared by other companies (such as a high bond or credit rating), *San Leandro* is inapplicable.

Converium and the Officer Defendants also misplace reliance on *Melder v. Morris*, 27 F.3d 1097 (5th Cir. 1994) for the proposition that a desire to have a successful IPO is insufficient to establish motive. Converium Mem. at 44. In *Melder*, the court found the allegations of motive to be insufficient because the claim of motive for the defendant officers and directors was for incentive compensation, and there were no allegations that these defendants personally profited. *Id.* at 1102. Unlike *Melder*, ZFS here obtained a nearly $2 billion windfall from the IPO, which occurred only because Tillinghast's true conclusions were concealed. ¶84, 86-87.

VIII. THE COMPLAINT ADEQUATELY STATES CONTROL PERSON CLAIMS UNDER SECTION 15 OF THE SECURITIES ACT AND SECTION 20(a) OF THE EXCHANGE ACT

Lead Plaintiffs assert control person claims under Section 15 of the Securities Act, 15 U.S.C. § 77o Section 20(a) of the Securities Exchange Act, 15 U.S.C. § 78t(a), against ZFS, the Officer Defendants and defendants Colombo, Mehl, Förterer, Schnyder, Hendrix and Parker. ¶¶276-286, 308-328. Section 15 of the Securities Act provides:

> Every person who, by or through stock ownership, agency, or otherwise, or who, pursuant to or in connection with an agreement or understanding with one or more other persons by or through stock ownership, agency, or otherwise, controls any person liable under sections 77k or 77l of this title, 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 had no knowledge of or reasonable ground to believe in the existence of the facts by reason of which the liability of the controlled person is alleged to exist.

15 U.S.C. § 77o.

Section 20(a) provides:

> 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 act or acts constituting the violation or cause of action.

15 U.S.C. § 78t(a).

As an initial matter, the question of control person liability "is necessarily fact intensive and cannot be resolved" at the motion to dismiss stage. *In re Executive Telecard, Ltd. Sec. Litig.*, 913 F. Supp. 280, 286 (S.D.N.Y. 1996); *In re Oxford Health Plans, Inc. Sec. Litig.*, 187 F.R.D. 133, 143 (S.D.N.Y. 1999) ("fact intensive" question for a jury); *Terrydale Liquidating Trust v. Barness*, 611 F. Supp. 1006, 1023 (S.D.N.Y. 1984) (determination of whether there is control "must be made at trial"); *SEC v. Franklin Atlas Corp.*, 154 F. Supp. 395, 400 (S.D.N.Y. 1957) ("The question of control is a factual question").[31] Therefore, the issue of control person liability "is not ordinarily subject to resolution on a motion to dismiss" and "dismissal is appropriate only when a plaintiff does not plead any facts from which it can reasonably be inferred the defendant was a control person." *MicroStrategy*, 115 F. Supp. 2d at 661. Notwithstanding the foregoing, Defendants' challenge Lead Plaintiffs' Section 20(a) claims. For the reasons set forth below, Lead Plaintiffs have properly pled such claims.

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[31] *See also, No. 84 Employer-Teamster Joint Council Pension Trust Fund v. America W. Holding Corp.*, 320 F.3d 920, 945 (9th Cir. 2003), *cert. denied*, 540 U.S. 966 (2003) ("intensely factual question"; reversing order granting motion to dismiss); *In re Hayes Lemmerz Intern., Inc.*, 271 F. Supp. 2d 1007, 1022-23 (E.D. Mich. 2003) ("whether one is a control person is a factual question") (denying motion to dismiss).

A. Lead Plaintiffs Are Not Required to Plead Culpable Participation

To state a control person claim, a plaintiff must allege: (a) an underlying primary violation of the securities laws by the controlled person; and (b) control over the controlled person.[32] *IPO Litigation*, 241 F. Supp. 2d at 392-397. Defendants, however, argue that there is a third element, specifically, culpable participation by the controlling person. Converium Mem. at 55. Defendants are wrong. This Court has held that, at the pleading stage, it "is persuaded that an Exchange Act claim against a putative control person need not allege culpable participation." *ATSI Comm., Inc. v. The Shaar Fund, Ltd.*, No. 02 Civ. 8726 (LAK), 2003 WL 21650135, at *1 (S.D.N.Y. July 14, 2003) (Kaplan, J.); *see also Parmalat*, 376 F. Supp. 2d at 515 (plaintiff not required to plead culpable participation); *In re Interpublic Sec. Litig.*, No. 02 Civ. 6527 (DLC), 2003 WL 21250682, at *15 (S.D.N.Y. May 29, 2003); *WorldCom*, 294 F. Supp. 2d at 415; *IPO Litigation*, 241 F. Supp. 2d at 396; *In re Quintel Entm't Inc. Sec. Litig.*, 72 F. Supp.2d 283, 297-98 (S.D.N.Y. 1999); *Food & Allied Serv. Trades v. Millfeld Trading Co.*, 841 F. Supp. 1386, 1390 (S.D.N.Y. 1994); *Neubauer v. Eva-Health USA, Inc.*, 158 F.R.D. 281, 284 (S.D.N.Y. 1994) (Kaplan, J.); *Borden, Inc. v. Spoor Behrins Campbell & Young*, 735 F. Supp. 587, 588-89 (S.D.N.Y. 1990); *Terra Res. I v. Burgin*, 664 F. Supp. 82, 88 (S.D.N.Y. 1987).

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[32] The SEC defines "control" as "possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise." 17 C.F.R. § 240.12b-2; *see also* 17 C.F.R. § 230.405; *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1473 (2d Cir. 1996) (adopting this standard for Section 20(a) claims). Section 20(a) requires "only some indirect means of discipline or influence short of actual direction to hold a 'controlling person' liable." *Myzel v. Fields*, 386 F.2d 718, 738 (8th Cir. 1967). In this Circuit, "control requires only the ability to direct the actions of the controlled person, and not the active exercise thereof." *Dietrich v. Bauer*, 126 F. Supp. 2d 759, 764 (S.D.N.Y. 2001) (internal quotations omitted).

Defendants cite *Boguslavsky v. Kaplan*, 159 F.3d 715, 720 (2d Cir. 1998), a pre-PSLRA opinion, in support of the proposition that culpable participation is an element of a Section 20(a) claim. Converium Mem. at 55. However, Defendants' citation is misplaced for two reasons. First, the *Boguslavsky* decision was rendered in the context of summary judgment. Second, because the *Boguslavsky* court had before it a complete evidential record in which to decide the motion for summary judgment, the court was required under *SEC v. First Jersey Securities, Inc.*, 101 F.3d 1450, 1472 (2d Cir.1996), *cert. denied*, 522 U.S. 812 (1997) ("*First Jersey*") to rule on the sufficiency of the *evidence* which the plaintiff must prove at trial. Thus, while both *Boguslavsky* and *First Jersey* held that culpable participation is an element of a Section 20(a) claim which must be proven at trial, those cases did not decide how a Section 20(a) claim must be pled.[33] Indeed, Judge Baer noted in *In re Vivendi Universal S.A.*, 381 F. Supp. 2d. 158, 188 (S.D.N.Y. 2003) that "*First Jersey* was concerned with the sufficiency of evidence as to control at the conclusion of trial and its holding is inapposite ... on a motion to dismiss."

In *WorldCom*, 294 F. Supp. 2d at 415, Judge Cote held that "a plaintiff must plead only the existence of a primary violation by a controlled person and the direct or indirect control of the primary violator by the defendant in order to state a claim" under Section 20(a). The Court stated:

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[33] In *First Jersey*, the Second Circuit upheld Section 20(a) claims based on allegations of control coupled with an underlying violation, without any allegations of culpable participation. *First Jersey*, 101 F.3d at 1473 (finding evidence of primary violation and control, and then turning to issue of whether defendant had satisfied his affirmative defense, without discussing whether plaintiff had established culpable participation). The Second Circuit reached a similar result in *Suez Equity Investors, L.P. v. Toronto-Dominion Bank*, 250 F.3d 87, 101 (2d Cir. 2001) (allegation that "DeRoziere was an officer of the Bank and that he had primary responsibility for the dealings of that Bank and the other corporate defendants with SAM Group ... [w]hile somewhat broad, [were] sufficient to plead controlling-person liability for the Bank derived from DeRoziere, the purported primary violator").

> The concept of culpable participation describes that degree of control which is sufficient to render a person liable under Section 20(a). At the pleading stage, the extent to which the control must be alleged will be governed by Rule 8's pleading standard. At trial, the degree of control will require the plaintiff to present *prima facie* evidence of sufficient control to support liability. Although previous opinions of this Court have imposed a greater burden on plaintiffs at the pleading stage, this Court now finds that plaintiffs need not meet the PSLRA's heightened pleading standard in alleging a violation of Section 20(a), or separately allege culpable participation.

Id.

Likewise, in *IPO Litigation*, 241 F. Supp. 2d at 393-96, Judge Scheindlin analyzed Section 20(a) at length and concluded that culpable participation does not need to be pled, and most certainly does not need to be pled with particularity. The Court noted that there is no basis for equating "culpable participation" with scienter, as culpable conduct "can be blameworthy though it was done unintentionally or unknowingly," and "the scienter-free definition of 'culpable' is particularly appropriate." *Id.* at 394 n.182. Judge Scheindlin further observed that the plaintiffs "need not affirmatively plead negligence" and that:

> In both *First Jersey* and *Suez Equity*, allegations of control coupled with an underlying violation sufficed to plead a Section 20(a) claim. Neither case – both post-PSLRA – even hinted that scienter must be pled in a Section 20(a) claim ... and *Suez Equity* explicitly recognized that plaintiff's allegations, while adequate to state a claim under Section 20(a), were "somewhat broad," *i.e.*, not particular. Thus, although the meaning of "culpable participation" is unclear, there is strong reason to believe that it is not the same as scienter.

Id. at 395.

Finally, contrary to Defendants' arguments (*See* ZFS Mem. at 11), control person claims must be pled "only in accordance with Rule 8(a). Neither the PSLRA (because scienter is not an essential element), nor Rule 9(b) (because fraud is not an essential element), apply to a claim for control person liability." *Id. at 396; accord Vivendi*, 2004 WL 876050, at *1; *Fezzani v. Bear Stearns & Co.*, No. 99 Civ. 0793 (RCC), 2004 WL 744594, at *23 (S.D.N.Y. Apr. 6, 2004) ("[t]he Rule 9(b) heightened pleading standard does not apply to averments of control person

liability."); *WorldCom*, 294 F. Supp. 2d at 414-15; *Duncan v. Pencer*, No. 94 Civ. 0321 (LAP), 1996 WL 19043, at *18 (S.D.N.Y. Jan. 18, 1996). Therefore, a "short, plain statement that gives the defendant fair notice of the claim that the defendant was a control person and the ground on which it rests its assertion ... is all that is required." *WorldCom*, 294 F. Supp. 2d at 415-16; *accord In re Philip Servs. Corp. Sec. Litig.*, No. 98 Civ. 0835 (MBM), 2004 WL 1152501, at *19 (S.D.N.Y. May 24, 2004). "[N]aked allegations of control ... will typically suffice to put a defendant on notice of the claims against her." *IPO Litigation*, 241 F. Supp. 2d at 352; *accord Vivendi*, 2003 WL 22489764, at *2 (distinguishing what must be pled from what must ultimately be proven at trial); *see also Teachers' Retirement System of Louisiana v. A.C.L.N. Limited*, No. 01 CIV 11814 (MP), 2003 WL 21657255 at *12 (S.D.N.Y. July 14, 2003) ("At the motion to dismiss stage, a plaintiff need only plead facts supporting a reasonable inference of control").

B. The Officer Defendants Were Control Persons

Lead Plaintiffs have satisfied both elements necessary to establish control person liability. First, they have established an underlying violation of the securities law. *See* Section *supra*. In addition, Lead Plaintiffs have alleged control over the controlled entity. In this regard, the Complaint alleges that by virtue of their status as officers and members of the Executive Committee of Converium during the Class Period, the Officer Defendants are "controlling persons" of Converium within the meaning of Section 15 of the Securities Act and Section 20(a) of the Exchange Act because they had the power and influence to cause the Company to engage in the unlawful conduct at issue. ¶¶284, 311.

Because of their positions of control, the Officer Defendants were able to, and did, directly or indirectly, control the conduct of Converium's business, the establishment of its loss reserves, the novation of its contracts, the information contained in its filings with the SEC, and

public statements about its business. *Id.* Each of the Officer Defendants were provided with or had access to copies of the Company's reports, press releases, public filings and other statements alleged by Lead Plaintiffs to be misleading prior to and/or shortly after these statements were issued and they had the ability to prevent the issuance of the statements or cause the statements to be corrected. *Id.* The Complaint specifically alleges that the Officer Defendants received, among other information, direct reports of the Loss Reserve Study, the Global Reserving Actuary's reserve study, Tillinghast's identification of a $350 million deficiency and the status of the novation scheme. ¶¶76, 82, 107, 132, 133.

Moreover, the Complaint provides specific examples of the control exerted by the Officer Defendants over the Company's loss reserves. For example, the Complaint alleges that Defendants Lohmann and Kauer determined that the reserve deficiency identified by Tillinghast must not exceed $125 million, and directed Defendant Smith to have Converium North America's actuaries convince Tillinghast to revise its initial conclusion. ¶86. Confidential Witness No. 4 explained that senior Company management in Switzerland – Defendants Lohmann and Kauer – made all reserve decisions for North America. ¶99 This is corroborated by Confidential Witness No. 1 who, as a Converium North America actuary, said of Defendants Lohmann and Kauer, "we didn't book anything without their ok." ¶98. Clearly, these allegations are sufficient to state control.

C. Defendant Colombo, Mehl, Forterer, Schnyder, Hendrix and Parker Were Control Persons

With respect to Defendants Colombo, Mehl, Forterer, Schnyder, Hendrix and Parker, each signed the Registration Statement for the IPO and thereby controlled its contents and dissemination, including the dissemination of the Prospectus. ¶313. The Complaint further alleges that by virtue of their status as Directors of Converium at the time of the IPO, these

defendants were controlling persons of Converium within the meaning of Sections 15 of the Securities Act and 20(a) of the Exchange Act because they had the power and influence to cause the Company to engage in the unlawful conduct at issue. *Id.*

Thus, as pled in the Complaint, Defendants Colombo, Mehl, Forterer, Schnyder, Hendrix and Parker each controlled Converium, which violated Section 11 and 12(a)(2) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder by their acts and omissions. ¶¶286, 315. By virtue of their position of control, these Defendants are liable pursuant to Section 15 of the Securities Act and Section 20(a) of the Exchange Act. *Id.*

D. Defendant ZFS Was A Control Person At The Time Of The IPO

ZFS owned 100% of Converium until December 11, 2001, when it sold its Converium shares on the IPO. ¶91. The Complaint plainly alleges that ZFS participated in the management and operation of Converium generally, and participated in the preparation and dissemination of the Registration Statement and Prospectus. ¶¶279, 326. Indeed, ZFS concedes that Lead Plaintiffs allege these facts, but dismisses them as "conclusory." ZFS Mem. at 55. Rule 8, which governs claims of control person liability, requires nothing more. *WorldCom,* 294 F. Supp. 2d at 415. Indeed, courts have held that allegations that a parent controlled the operations of its wholly owned subsidiary are sufficient to state a claim for control person liability. *See Global Crossing,* WL 1875445, (Aug. 5, 2005) (collecting cases).

IX. THE COMPLAINT ALLEGES A LEGALLY SUFFICIENT BASIS TO ASSERT PERSONAL JURISDICITION OVER DEFENDANTS CLARKE, COLOMBO, MEHL, FORTERER AND SCHNYDER

Pursuant to Rule 12(b)(2) of the Federal Rules of Civil Procedure, defendants Clarke, Colombo, Mehl, Forterer and Schnyder (collectively, "the Foreign Defendants") assert that the

Complaint should be dismissed as to each of them for lack of personal jurisdiction.[34] Converium Def. Mem. at 56. The Foreign Defendants claim that the Complaint fails to show that they had sufficient "minimum contacts" with the United States to justify this Court's exercise of personal jurisdiction over them. *Id.* As set forth below, Lead Plaintiffs have satisfied the requirements for exercising personal jurisdiction.

Where a defendant's activities have an "unmistakably foreseeable effect within the United States" and "could reasonably be expected to be visited upon the United States [investors]," exercise of personal jurisdiction over foreign defendants for securities fraud claims is appropriate. *SEC v. Unifund SAL*, 910 F.2d 1028, 1033 (2d Cir. 1990); *SEC v. Softpoint Inc.*, No. 95 Civ. 2951 (GEL), 2001 WL 43611, at *5 (S.D.N.Y. Jan. 18, 2001). In the case at bar, the Foreign Defendants' activities satisfy this criteria. At a minimum, Lead Plaintiffs' factual allegations, made without benefit of discovery, suffice to defeat the Foreign Defendants' motion to dismiss at this time.[35]

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[34] Defendants also state in their brief that "at the appropriate time, [they] will file a separate motion under Fed. R. Civ. P. 12(b)(1) to dismiss" for lack of subject matter jurisdiction. ZFS Mem. at 2; *see also* Underwriters Mem. at 25. The allegations of the Complaint clearly establish subject matter jurisdiction over this action, and Lead Plaintiffs will readily respond to any properly filed motion by Defendants with respect to whether such jurisdiction exists.

[35] Where, as here, a defendant brings a motion to dismiss for lack of personal jurisdiction before discovery has begun, the plaintiff may defeat the motion simply by alleging a *prima facie* case. *See PDK Labs, Inc. v. Friedlander*, 103 F.3d 1105, 1108 (2d Cir. 1997); *A.I. Trade Finance, Inc. v. Petra Bank*, 989 F.2d 76, 79 (2d Cir. 1993). To do so, Lead Plaintiffs may rely entirely on mere allegations of fact in the Complaint, and they will prevail even if the Foreign Defendants subsequently make contrary allegations which controvert their *prima facie* case. *See A.I. Trade*, 989 F.2d at 79; *Hoffritz for Cutlery, Inc. v. Amajac, Ltd.*, 763 F.2d 55, 57 (2d Cir. 1985).

If the Court determines that Lead Plaintiffs have not yet established the basis for asserting personal jurisdiction, Lead Plaintiffs request leave to conduct discovery limited to issues of jurisdiction, such as the Foreign Defendants' contacts with the U.S. At this juncture of the case, Lead Plaintiffs need satisfy only a "light burden" to be entitled to discovery as to personal jurisdiction. *Alicea v. Lasar Mfg. Co.*, No. 91 Civ. 3929 (JFK), 1992 WL 230203, at *2 (S.D.N.Y. Aug. 31 1992). "Plaintiffs are entitled to discovery regarding the issue of personal

Section 27 of the Exchange Act, 15 U.S.C. § 78aa, empowers United States courts to exercise personal jurisdiction in Rule 10b-5 cases to the full extent permitted by due process. *See Unifund SAL*, 910 F. 2d at 1033; *ATSI Comm., Inc. v. The Shaar Fund, Ltd.*, No. 02 Civ. 8726 (LAK), 2004 WL 909173, at *2 (S.D.N.Y. April 28, 2004); *Cromer Finance Ltd. v. Berger*, 137 F. Supp. 2d 452, 473 (S.D.N.Y. 2001). To determine whether the exercise of personal jurisdiction is proper, the Court must conduct a two-part due process analysis: a "minimum contacts" inquiry and a "reasonableness" inquiry. *Metropolitan Life Ins. Co. v. Robertson-Ceco Corp.*, 84 F.3d 560, 567 (2d Cir. 1996); *Cromer*, 137 F. Supp. 2d at 473. The "minimum contacts" inquiry examines a defendant's contacts with the United States. *Chew v. Dietrich*, 143 F.3d 24, 28 n. 4 (2d Cir. 1998); *Cromer*, 137 F. Supp. 2d at 473; *The GMS Group, Inc. v. Sentinel Trust Co.*, No. 97 Civ. 1342 (WK), 1997 WL 414147, at *2 (S.D.N.Y July 23, 1997). If the Court finds sufficient contacts with the United States, it then assesses the "reasonableness" – from the forum's perspective – of exercising jurisdiction. *See Fitzsimmons v. Barton*, 589 F.2d 330, 333 (7th Cir. 1979) (reversing dismissal because the trial court's fairness analysis did not focus on interests of United States in hearing action, as reflected in the securities laws); *see also SEC v. Euro Sec. Fund, Coim SA*, No. 98 Civ. 7437, 1999 WL 76801, at * 3 (S.D.N.Y. Feb. 17, 1999). As both tests are easily satisfied here, the Court should deny the Foreign Defendants' motion to dismiss.

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jurisdiction if they have made a sufficient start, and shown their position not to be frivolous." *Newbro v. Freed*, No. 03 Civ. 10308 (PKC), 2004 WL 691392, at *3 (S.D.N.Y. Mar. 31, 2004); *see also Stratagem Dev. Corp. v. Heron Int'l N.V.*, 153 F.R.D. 535, 547 (S.D.N.Y. 1994) (discovery allowed where plaintiff failed to make a *prima facie* showing of jurisdiction but its position was not frivolous); *The Manhattan Life Ins. Co. v. A.J. Stratton Syndicate*, 731 F. Supp. 587, 593 (S.D.N.Y. 1990) (same).

A. The Minimum Contacts Test Is Satisfied

Minimum contacts with the United States can be established under either of two theories: general or specific jurisdiction. General jurisdiction exists where a defendant's contacts with the forum are so "continuous and systematic" that it can be sued for any claim, irrespective of the relationship of the claim to the forum-related conduct. *Helicopteros Nacionales de Colombia S.A. v. Hall*, 466 U.S. 408, 415-16 (1984). "Specific jurisdiction exists when 'a State exercises personal jurisdiction over a defendant in a suit arising out of or related to the defendant's contacts with the forum.'" *Metropolitan Life Ins. Co. v. Robertson Ceco-Corp.*, 84 F.3d 560, 567-68 (2d Cir. 1996) (citing *Helicopteros Nacionales*, 466 U.S. at 414-16 & nn.8-9).

To assert specific jurisdiction, the Court must find that "the defendant has 'purposefully directed' his activities at residents of the forum, and the litigation results from alleged injuries that 'arise out of or relate to' those activities." *Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 472 (1985). Moreover, courts examine whether it was foreseeable to the defendant that its actions would cause injury in the forum State. *Burger King*, 471 U.S. at 474 (foreseeability analysis requires that "'the defendant's conduct and connection with the forum State are such that he should reasonably anticipate being haled into court there'") (quoting *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 297 (1980)). One circumstance making such anticipation reasonable is where a defendant has acted in such a way as to have "caused consequences" in the forum state. *See Unifund SAL*, 910 F.2d at 1033 (finding personal jurisdiction where defendants' actions abroad had a clearly foreseeable and direct impact on the United States securities market).

The Foreign Defendants assert a myriad of reasons why the Court lacks jurisdiction over each of them. For example, they make much of the fact that none of them resides in the Unites

States. Converium Def. Mem. at 57. They also claim that they did not engage in any wrongful conduct in the United States and that the Complaint does not allege that they made any misrepresentations concerning the Company's reserves or were themselves involved in any reserving activities. *Id.* at 57-58. In addition, they claim that the Complaint's allegations regarding the Company's ADS program fails to provide a basis for asserting personal jurisdiction. *Id.* at 58. Not one of these arguments has any merit.

Personal jurisdiction in a Rule 10b-5 case may be asserted over a defendant with *no* physical contact with the forum if he or she "caus[ed] an effect in the state by an act done elsewhere." *Perez-Rubio v. Wyckoff*, 718 F. Supp. 217, 228 (S.D.N.Y. 1989); *see, e.g.*, *Shanahan v. Vallat*, No. 03 Civ. 3496, 2004 WL 2937805 at *8 (S.D.N.Y. Dec. 19, 2004) ("These contacts are sufficient to establish specific personal jurisdiction: [foreign] defendants acted with intent to influence a resident of the United States, and this litigation arises out of Defendants' acts."); *SEC v. Ogle*, No. 99 C 609, 1999 WL 446857, at *2 (N.D. Ill. June 15, 1999) (finding personal jurisdiction where complaint alleged the defendants' "knowing participation in planning and executing a scheme designed to defraud American investors and securities markets" and finding "irrelevant" contention that the defendants had no direct contact with the United States). Thus, even if the Foreign Defendants did not have any physical contacts with the United States, this Court would still have authority to exercise personal jurisdiction based upon their non-United States activities that affected United States investors.[36] *Teachers' Retirement System of Louisiana v. A.C.L.N. Limited*, No. 01 Civ. 11814(MP), 2003 WL

[36] The Complaint alleges that the Company's ADSs were listed and traded on the New York Stock Exchange and that a significant portion of Converium's securities were held by United States investors. ¶11. Following the Company's IPO in December 2001, 24% of Converium's shareholders resided in the United States. *Id.* By December 2002, the percentage of U.S. investors comprised 70% of the Company's shareholders. *Id.*

21058090, at *8-9 (S.D.N.Y. May 15, 2003) (foreign parent of international accounting firm subject to personal jurisdiction where the plaintiff alleged it was "engaged in a course of conduct with the knowledge that it would affect American investors in the United States."); *SEC v. Foundation Hai*, 736 F. Supp. 465, 469 (S.D.N.Y. 1990) (overseas trading activities of the foreign defendants in United States-listed securities sufficiently directed toward United States for purposes of liability under §10(b)); *see also MTC Elec. Tech. Co. v. Leung*, 889 F. Supp. 396, 400 (C.D. Cal. 1995) ("within the rubric of 'purposeful availment,' jurisdiction may be exercised over a defendant whose only contact with the forum is the 'purposeful direction' of a foreign act which has an effect in the forum") (quoting *Calder v. Jones*, 465 U.S. 783 (1984)).

In the case at bar, Lead Plaintiffs set forth numerous allegations regarding each of the Foreign Defendants' involvement sufficient to allow this Court to assert personal jurisdiction over them. For example, the Complaint notes each of these defendants' roles on Converium's Board of Directors and the respective committees that they served on as well as their tenure on the Board. ¶¶26-30, 240. Similarly, the Complaint notes that they signed the Registration Statement and Prospectus issued in conjunction with the Converium IPO. *Id.* These allegations alone demonstrate that the Foreign Defendants were among *the* key players at Converium. In light of the Company's U.S. operations, these allegations are sufficient to establish the minimum contacts necessary to assert personal jurisdiction.

Clearly, the Foreign Defendants knew or should have known that their conduct would have a direct effect in the United States, and on investors in the United States. *See Unifund SAL*, 910 F.2d at 1031 (asserting personal jurisdiction based on trading through foreign brokers of options of United States-based company); *Derensis v. Coopers & Lybrand Chartered Accountants*, 930 F. Supp. 1003, 1014 (D.N.J. 1996) (personal jurisdiction existed over Canadian

defendants who had no direct contacts with forum but allegedly approved and disseminated financial statements they knew would influence the price of securities traded on NASDAQ); *Itoba Ltd. v. LEP Group PLC*, 930 F. Supp. 36, 41 (D. Conn. 1996) (personal jurisdiction is appropriate where director of foreign corporation knew or should have known a form he approved would be filed with the SEC and relied upon on by potential investors); *Landry v. Price Waterhouse Chartered Accountants*, 715 F. Supp. 98, 102 (S.D.N.Y. 1989) (personal jurisdiction existed over a foreign defendant charged with control person liability based on his "behind the scenes" role in the subject transaction which he must have known would have an impact on stock trading within the United States). The Complaint's allegations sufficiently establish "minimum contacts" with the United States such that the exercise of personal jurisdiction is appropriate and proper.

B. The Reasonableness Test Is Satisfied

It is reasonable to compel the Foreign Defendants to litigate in the Southern District of New York. Indeed, each Foreign Defendant was a Director of Converium – and Converium's North American headquarters during the Class Period were located in New York City. In assessing whether the assertion of personal jurisdiction is reasonable, courts employ a five-factor test: (1) the burden on the foreign entity to litigate here; (2) the interests of the United States as the forum for adjudicating the case; (3) the plaintiffs' interest in obtaining convenient and effective relief; (4) the most efficient interstate resolution of the controversy; and (5) the availability of relief in another forum. *See Asahi Metal Indus. Co. v. Superior Ct.*, 480 U.S. 102, 113-14 (1987). Contrary to their assertions, these factors weigh decidedly in favor of asserting personal jurisdiction over the Foreign Defendants.

First, it is indisputable that this Court and the United States have an interest in enforcing the securities laws against obvious violators like defendants herein, who were active and willful participants in this international fraud. *See SEC*, 1999 WL 76801 at * 4 ("The United States has a substantial interest in the integrity of its securities markets"). In addition, Lead Plaintiffs have a strong interest in obtaining convenient and effective relief, for themselves and the Class, as Converium's investors have suffered millions of dollars in losses. *Id.* Moreover, the courts in this District, and the remedies provided plaintiffs in the Exchange Act, support the assertion of jurisdiction here. *See Cromer*, 137 F. Supp. 2d at 479 (federal courts in Southern District of New York have an "expertise in [securities] litigation"). Moreover, the IPO Prospectus stated that the registered agent for service of process in the United States was Converium's North American headquarters located at One Chase Plaza in New York City.

All of these reasons weigh in favor of exercising personal jurisdiction over the Foreign Defendants. Therefore, the Foreign Defendants' arguments must be rejected.

X. CONCLUSION

For all of the foregoing reasons, Defendants' motions should be denied in their entirety. In the alternative, should the Court find any infirmity in the allegations of the Complaint, Lead Plaintiffs respectfully request leave to amend and/or limited discovery to investigate any jurisdictional deficiencies.

Dated: February 17, 2006
New York, New York

Respectfully submitted,

/s/ Matthew K. Handley

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2/17/06

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February 17, 2006

BY OVERNIGHT DELIVERY
The Honorable Michael B. Mukasey
Chief Judge
Southern District of New York
Daniel Patrick Moynihan United States Courthouse
500 Pearl Street
New York, New York 10007-1312

Re: *In re Converium Holding AG Securities Litigation* No. 04-cv-07897-MBM

Dear Chief Judge Mukasey:

We represent Lead Plaintiffs in the above-referenced action.

We respectfully enclose two courtesy copies of the following documents filed electronically with the Clerk of the Court and served on all counsel of record:

- Lead Plaintiffs' Memorandum of Law In Opposition To Defendants' Motions To Dismiss The Consolidated Amended Class Action Complaint;

- Lead Plaintiffs' Motion To Strike Certain Exhibits Attached To Defendants' Motions To Dismiss; and

- Lead Plaintiffs' Memorandum Of Law In Support Of Their Motion To Strike Certain Exhibits Attached To Defendants' Motions To Dismiss

Respectfully submitted,

Matthew K. Handley

Enclosures

cc: All counsel of record