**UNITED STATES DISTRICT COURT**
**SOUTHERN DISTRICT OF NEW YORK**

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| IN RE BANK OF AMERICA CORP. SECURITIES, DERIVATIVE, AND EMPLOYMENT RETIREMENT INCOME SECURITY ACT (ERISA) LITIGATION | Master File No. 09 MDL 2058 (DC)<br>ECF CASE |
| THIS DOCUMENT RELATES TO<br>All Securities Actions | |

**REPLY MEMORANDUM OF LAW IN SUPPORT OF THE BANK DEFENDANTS' MOTION TO CERTIFY A QUESTION OF LAW TO THE DELAWARE SUPREME COURT**

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The Bank Defendants respectfully submit this reply memorandum in support of their motion to certify a question of law to the Delaware Supreme Court and in response to the opposition briefs submitted by Lead Plaintiffs ("LP Opp.") and Stichting Pensioenfonds ABP ("ABP Opp.").

## PRELIMINARY STATEMENT

Both opposition briefs misconstrue the nature of the question to be certified and misstate the law under which that question must be decided. The Bank Defendants have consistently asserted that the relevant question is whether plaintiffs — Bank shareholders who did not buy, sell or exchange their Bank shares in the merger with Merrill — have standing to maintain a direct claim for damages under Section 14(a) of the Exchange Act for the post-merger decline in the Bank's share price based on their assertion that they were deprived of their right to cast an informed vote on the merger.[1]

Plaintiffs argue that the question of whether they may assert such a direct claim is governed by federal law. But the Supreme Court and Second Circuit hold that gaps in federal remedial schemes that implicate the law of corporations — which include issues of "shareholder standing," *i.e.*, "the ability of a shareholder to seek redress for certain injuries on his or her own behalf rather than on behalf of the corporation" (*Strougo* v. *Bassini*, 282 F.3d 162, 167 & n.4 (2d Cir. 2002)) — must be decided under ***state*** law absent clear Congressional intent to the contrary. Thus, that controlling authority requires the application of Delaware state law here, as Section 14(a) is silent as to whether such a direct claim for damages may be maintained, and there is nothing in the Exchange Act to suggest that Congress intended to displace state law on this issue with a nationwide legal standard. *See* Point I.A, *infra.*

Plaintiffs' attempt to distinguish this controlling authority on the grounds that it relates solely to the Investment Company Act of 1940 ("ICA") is frivolous. The Supreme Court itself stated in *Kamen* v. *Kemper Financial Services, Inc.*, 500 U.S. 90, 98, 108 (1991) that state law should be used to fill gaps in "federal remedial schemes," including "the federal securities laws" — not just the ICA

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[1] Lead Plaintiffs assert that the Bank Defendants have "conceded the issue they originally sought to certify." LP Opp. 21. There has been no such concession. The Bank Defendants' consistent position has been that: (1) under the reasoning of the Delaware Supreme Court in *In re J.P. Morgan Chase & Co. Shareholder Litigation*, 906 A.2d 766 (Del. 2006), Plaintiffs cannot assert a direct claim for damages for the post-merger decline in the market price of their shares when the allegedly misstated or omitted facts were disclosed; and (2) to the extent that this Court decides that there is uncertainty as to the application of *J.P. Morgan* to plaintiffs' allegations, this issue of Delaware law should be certified to the Delaware Supreme Court.

— and federal courts have routinely looked to state law to fill such gaps in cases arising under the Exchange Act. *See* Point I.B, *infra*.

Plaintiffs cite cases in which shareholders were permitted to assert Section 14(a) claims directly without any inquiry into state law. LP Opp. 13-17; ABP Opp. 5 & n.3. But these cases are distinguishable because only a few involved Section 14(a) claims of the type at issue here — *i.e.*, claims for post-merger stock price decline damages purportedly based on a deprivation of an informed right to vote on a stock-for-stock merger in which plaintiffs did not buy, sell or exchange shares — and the defendants in those few cases apparently failed to raise the issue of whether state law controlled the question of direct standing, so the courts had no occasion to decide the issue. Thus, none of the Section 14(a) cases cited by plaintiffs actually address the issue presented by this motion. *See* Point I.C, *infra*.

Plaintiffs' analysis of Delaware law is similarly flawed. In an effort to circumvent the squarely on-point holding of the Delaware Supreme Court in *In re J.P. Morgan Chase & Co. Shareholder Litigation*, 906 A.2d 766 (Del. 2006), plaintiffs cite a myriad of authorities that address whether a direct claim for a deprivation of the right to cast an informed vote could theoretically exist. Those cases do not address the circumstance where (as here) non-transacting, acquiring company shareholders in a stock-for-stock merger seek damages based on a post-closing stock-price drop that occurred following alleged disclosures of facts allegedly showing that the target company was not worth the merger price they approved. *See* Point II, *infra*.

In short, if the Court believes that there is any uncertainty as to whether *J.P. Morgan* controls the proposed question and requires dismissal here, certifying this question to the Delaware Supreme Court would provide a proper and efficient means of resolving such uncertainty. *See* Point III, *infra*.

## ARGUMENT

### I. STATE LAW GOVERNS WHETHER PLAINTIFFS HAVE THE RIGHT TO ASSERT DIRECT CLAIMS FOR DAMAGES UNDER SECTION 14(a).

Plaintiffs do not (and cannot) dispute that the rights of shareholders vis-à-vis the companies in which they own their shares are governed by state law. *CTS Corp.* v. *Dynamics Corp. of Am.*, 481 U.S. 69, 91 (1987). Nor do plaintiffs attempt to explain how or why the issue of whether a company or its individual shareholders may advance a particular claim — essentially a question of who within

the corporation owns and controls the claim — is not precisely the type of corporate law issue, which, in our federal system, is governed by state law.

**A. Controlling Supreme Court and Second Circuit authorities require the application of state law to determine if plaintiffs' Section 14(a) claims may be maintained directly.**

As the Bank Defendants have previously shown, controlling Supreme Court and Second Circuit authorities — including *J.I. Case Co.* v. *Borak*, 377 U.S. 426 (1964), *Burks* v. *Lasker*, 441 U.S. 471 (1979), *Kamen* v. *Kemper Financial Services, Inc.*, 500 U.S. 90 (1991) and *Strougo* v. *Bassini*, 282 F.3d 162 (2d Cir. 2002) — hold that state law supplies the rule of decision for whether the Section 14(a) claims pled here can be maintained as direct claims.[2]

Plaintiffs do not (and cannot) deny that Congress did not speak to this issue in enacting Section 14(a). Yet they argue that *Borak* calls for the application of federal common law (divorced from the state corporate law under which the corporation at issue was chartered) to determine whether their Section 14(a) claims may be asserted directly because the "legal rules affecting the viability of federal claims are a matter of federal law." LP Opp. 7; *see also* ABP Opp. 7, 10 (arguing that federal law must determine whether a shareholder may sue directly because "federal law is the source both of the shareholders' right" to disclosure and the "corporation's corresponding obligation" to provide it). Plaintiffs simply misread the Supreme Court precedent.

In *Borak*, the Supreme Court recognized the existence of an implied right of action under Section 14(a) of the Exchange Act. 377 U.S. at 431-32. The Court further stated that a Section 14(a) right of action "exists as to both derivative and direct causes." 377 U.S. at 431. But the *Borak* Court noted that derivative actions, if any, would often be more appropriate to address alleged proxy disclosure actions because "[t]he injury which a stockholder suffers from corporate action pursuant to a deceptive proxy solicitation ordinarily flows from the damage done the corporation, rather than from the damage inflicted directly upon the stockholder." 377 U.S. at 432. As the Court explained,

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[2] *See* Bank Defendants' Memorandum in Support of the Motion to Dismiss (Nov. 24, 2009) ("Def. Sec. Br.") at 70-71; Bank Defendants' Reply Memorandum in Support of the Motion to Dismiss (Jan. 26, 2010) ("Def. Sec. Reply") at 3-7; *see also* Letter from Bank Defendants to the Court (Feb. 9, 2010) ("Def. 2/9/10 Ltr.") at 1; Letter from Bank Defendants to the Court (Mar. 8, 2010) ("Def. 3/8/10 Ltr.") at 1; Bank Defendants' Supplemental Response to Plaintiffs' Letters (Mar. 8, 2010) ("Def. Supp. Br.") at 15-17.

in such cases, "[t]he damage suffered results not from the deceit practiced on him alone but rather from the deceit practiced on the stockholders as a group." *Id.*

Although the cause of action recognized in *Borak* is federal in nature, the Supreme Court's subsequent decisions in *Burks* and *Kamen* make clear that courts are not free under *Borak* to "fashion a complete body of federal law" thereunder. *Burks*, 441 U.S. at 477. To the contrary, these Supreme Court precedents make clear that state corporation law is incorporated into the federal common law "where a gap in the federal securities laws must be bridged by a rule that bears on the allocation of governing powers within the corporation." *Kamen*, 500 U.S. at 108.

Thus, in *Burks*, the issue presented was whether the disinterested directors of an investment company had the power to terminate a derivative suit brought against other directors under the ICA and the Investment Advisers Act of 1940 ("IAA"). 441 U.S. at 473. Citing *Borak*, the Court acknowledged that the legal consequences of the violation of a federal statute ordinarily raise a federal question. *Id*. at 476. But the Court then stated:

> The fact that "the scope of [the shareholders'] federal right is, of course a federal question" does not, however, make state law irrelevant. It is true that ***in certain areas we have held that federal statutes authorize the federal courts to fashion a complete body of federal law. Corporation law, however, is not such an area***. . . . This case involves the question whether directors are authorized to determine that certain claims not be pursued on the corporation's behalf. As we have said in the past, the first place one must look to determine the powers of corporate directors is the relevant State's corporation law. "Corporations are creatures of state law," and it is state law which is the font of corporate directors' powers. By contrast, federal law in this area is largely regulatory and prohibitory in nature — it often limits the exercise of directorial power, but only rarely creates it. ***In short, in this field congressional legislation is generally enacted against the background of existing state law; Congress has never indicated that the entire corpus of state corporation law is to be replaced simply because a plaintiff's cause of action is based upon a federal statute.***

*Id*. at 477-78 (emphasis added) (citations omitted). The Court then added that the ICA and IAA did not require that federal law displace the state laws governing the power of directors to terminate a derivative claim brought under those statutes unless the application of state law "would be inconsistent with the federal policy underlying the cause of action." *Id.* at 479. After noting that "[a] state statute cannot be considered inconsistent with federal law merely because the statute causes the plaintiff to lose the litigation," *id*., the Court found nothing in the language or legislative history of the two statutes to support the conclusion that Congress intended to prohibit directors of investment companies from exercising their state law power to terminate derivative suits. *See id*. at 480-86.

Then, in *Kamen*, the issue considered by the Court was whether to "fashion a federal common law rule" requiring a plaintiff in a derivative action founded on the ICA to "make a demand on the board of directors even when such a demand would be excused as futile under state law." 500 U.S. at 92. Plaintiff brought a suit to enforce the provision of the ICA that, like Section 14(a) of the Exchange Act, prohibits the use of materially misleading proxy statements.[3] Once again, the Court acknowledged that "[b]ecause the ICA is a federal statute, any common law rule necessary to effectuate a private cause of action under that statute is necessarily federal in character." *Id.* at 97. But as it had in *Burks*, the Court observed that simply because federal law was the source of the remedy, "[i]t does not follow . . . that the content of such a [common law] rule must be wholly the product of a federal court's own devising." *Id.* at 98. Indeed, elaborating on its analysis in *Burks*, the Court declared that state, not federal, law presumptively governs the rules "necessary to effectuate a private cause of action" under a federal remedial scheme where Congress has not otherwise specified what those rules should be:

> [A] court should endeavor to fill the interstices of federal remedial schemes with uniform federal rules only when the scheme in question evidences a distinct need for nationwide legal standards, or when express provisions in analogous statutory schemes embody congressional policy choices readily applicable to the matter at hand. Otherwise, we have indicated that federal courts should "incorporate [state law] as the federal rule of decision," unless "application of [the particular] state law [in question] would frustrate specific objectives of the federal programs." ***The presumption that state law should be incorporated into federal common law is particularly strong in areas in which private parties have entered legal relationships with the expectation that their rights and obligations would be governed by state-law standards. . . . Corporation law is one such area.***

*Id.* at 98 (citations omitted) (emphasis added).

The *Kamen* Court concluded that the "demand requirement comes within the purview of *Burks*' presumption of state-law incorporation" because it "affects the allocation of governing power within the corporation" inasmuch as it "determine[s] ***who*** has the power to control corporate litigation." 500 U.S. at 100-01 (emphasis added). Finding nothing in the text or legislative history to suggest that Congress intended to supplant the power directors of investment companies would otherwise have under state law to control corporate litigation, the Court held that none of the

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[3] *Id.* at 93 n.1, citing 15 U.S.C. § 80a-20(a). As the Supreme Court noted, SEC regulations required — and still require — proxy statements issued by a registered investment company to comply with the proxy statement rules promulgated under the Exchange Act. *See* 500 U.S. at 93 n.1, citing 17 C.F.R. § 270.20a-1(a) (1991); *see also* 17 C.F.R. § 270.20a-1(a) (2010).

enumerated exceptions to the application of state law applied. *See id.* at 107-08. Reaffirming the basic teaching of *Burks*, the Supreme Court held: "[W]here a ***gap in the federal securities laws*** must be bridged by a rule that bears on the allocation of governing powers within the corporation, federal courts should incorporate ***state*** law into federal common law unless the particular state law question is inconsistent with the policies underlying the federal statute." *Id.* at 108 (emphasis added in part).

Following *Kamen*, the Second Circuit, in *Strougo*, was called upon to decide whether claims that managers of an investment fund violated the ICA by conducting an allegedly coercive and dilutive rights offering gave rise to direct claims on the part of the fund's shareholders or, as defendants contended, such claims could only be brought derivatively. *Id.* at 165. The Second Circuit first considered whether federal or state law should be "the source of the rules we apply to decide the issue of shareholder standing." *Id.* at 167 & n.4. Though acknowledging that the claims at issue were federal in origin, the Second Circuit read *Kamen* to hold that state law controlled the issue because the ICA was "silent on issues of shareholder standing" and lacked "sufficient indicia of Congressional intent for courts to fashion nationwide legal standards to overcome the presumption that state-law rules on questions of corporate law will be applied." *Id.* at 167-69. Here, as in *Strougo*:

- There is unquestionably a "gap in the federal securities law[] that must be bridged by a rule that bears on the allocation of governing powers within the corporation" as the federal statute at issue — Section 14(a) of the Exchange Act — is "silent on issues of shareholder standing" and thus does not speak to whether shareholders of the acquiring company in a stock-for-stock merger may sue directly for damages. 282 F.3d at 168.
- The availability *vel non* of a direct claim on this set of facts is unquestionably one of the "'interstices of [the] federal remedial scheme[]'" imposed by the proxy laws. *Id.*, quoting *Kamen*, 500 U.S. at 98. Thus, the Court must "fill a gap . . . with rules borrowed from state law." 282 F.3d at 169.
- Plaintiffs have not cited to any "distinct need for nationwide legal standards" or any "express provisions in analogous [federal] statutory schemes [that] embody congressional policy choices

readily applicable to the matter at hand," or explained how "application of the particular state law in question would frustrate specific objectives" of the Exchange Act. *Id.* at 168-69.

ABP strains to distinguish *Strougo* and *Kamen* by asserting that there are no such "gaps" here. In support, ABP relies entirely upon the Seventh Circuit's 1963 decision in *Borak*, which held that federal courts have the power under the Exchange Act "to grant all of the relief which may be commensurate with the effective enforcement of the statute." ABP Opp. 7, quoting *Borak* v. *J.I. Case Co*., 317 F.2d 838, 848-49 (7th Cir. 1963), *aff'd sub nom. J.I. Case Co.* v. *Borak*, 377 U.S. 426 (1964). Whatever cogency the Seventh Circuit's analysis may have had 47 years ago, the Supreme Court's subsequent decisions in *Burks* and *Kamen* (and numerous lower court decisions since) make clear that whether there is a "gap in the federal securities law[]" is determined not by reference to the power of the federal court to grant particular relief — there was, after all, no question that the federal courts had the power under the ICA and IAA to grant the relief requested in *Burks* and *Kamen*[4] — but whether the federal securities statute at issue allocates the power to control the federal claim at issue between the shareholders and others in the corporation.[5]

That "federal law is the source both of the shareholders' right" to disclosure and "the corporation's corresponding obligation" to provide it under Section 14(a) (*see* ABP Opp. 7) does not mean that state law may be ignored. After all, in *Kamen*, federal law — Section 20(a) of the ICA — was likewise the source both of the plaintiff-shareholder's right to disclosure and the defendant investment company's obligation to provide it, yet the Supreme Court nevertheless concluded that state, not federal, law applied to fill the gaps in this proxy regulation in the absence of any demonstrable inconsistency with the policies underlying that statute.

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[4] The Supreme Court assumed the existence of an implied, derivative right of action under both the ICA and IAA. *Burks*, 441 U.S. at 475; *Kamen*, 500 U.S. at 97 n.4.

[5] Other courts have likewise read *Kamen* and *Burks* to require courts to look to the law of the state of incorporation in determining whether a federal claim is direct in nature. *See, e.g.*, *Halebian* v. *Berv*, 590 F.3d 195, 204 (2d Cir. 2009); *Lapidus* v. *Hecht*, 232 F.3d 679, 682 (9th Cir. 2000); *Boland* v. *Engle*, 113 F.3d 706, 715 (7th Cir. 1997); *In re AllianceBernstein Mut. Fund Excessive Fee Litig*., 2005 WL 2677753, at *3 (S.D.N.Y. Oct. 19, 2005), *reconsideration granted in part on other grounds*, 2006 WL 74439 (S.D.N.Y. Jan. 11, 2006); *In re Merrill Lynch & Co., Inc. Research Reports Sec. Litig*., 272 F. Supp. 2d 243, 259 (S.D.N.Y. 2003); *In re Dreyfus Aggressive Growth Mut. Fund Litig*., 2000 WL 10211, at *4 (S.D.N.Y. Jan. 6, 2000).

Thus, the controlling Supreme Court authorities, the Second Circuit decision in *Strougo*, and multiple lower court decisions require that Delaware law be applied to determine if plaintiffs can pursue their Section 14(a) claims directly.[6]

**B. The controlling authorities are fully applicable to Exchange Act claims.**

Plaintiffs attempt to distinguish *Kamen*, *Burks* and several Court of Appeals decisions holding that state law determines whether a claim is direct or derivative in nature on the grounds that these cases all arose under the ICA rather than the Exchange Act. *See* LP Opp. 9-10; ABP Opp. 8-10. Plaintiffs are simply wrong.

There is nothing in the reasoning of these cases to suggest that their logic does not apply to Exchange Act claims. Rather, as detailed above, these cases turn on the general principles that "'[c]orporations are creatures of state law,'" and "Congress has never indicated that the entire corpus of state corporation law is to be replaced simply because a plaintiff's cause of action is based upon a federal statute." *Burks*, 441 U.S. at 478, quoting *Cort* v. *Ash*, 422 U.S. 66, 84 (1975). *See also Kamen*, 500 U.S. at 98-99. These broad principles are equally applicable to claims asserted under the Exchange Act. Indeed, in *Kamen*, the Supreme Court itself stated that state law should presumptively be applied "where a gap in the ***federal securities laws*** must be bridged by a rule that bears upon the allocation of governing powers within the corporation." 500 U.S. at 108 (emphasis added). The Court did not limit its holding to the ICA. Not surprisingly, the federal courts, following *Kamen* and *Burks*, have repeatedly held that state corporate law governs the demand requirements applicable to Exchange Act claims, even though both of those cases arose under the ICA.[7]

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[6] Lead Plaintiffs warn that if state law is applied to determine their standing to sue, the "enforcement of the Exchange Act would vary from state to state and company to company, depending on where the company chose to incorporate itself." LP Opp. 6. While the law of direct versus derivative standing is not uniform throughout the 50 states, the possibility of such variation is not a reason to supplant state law unless the remedial scheme at issue "evidences a distinct need for nationwide legal standards." *Kamen*, 500 U.S. at 98. *See also Burks*, 441 U.S. at 480 n.6 ("This is not a situation where federal policy requires uniformity . . ."). And since the state law to be applied will be determined by reference to the company's state of incorporation, here, unlike *Ceres Partners v. GEL Assocs*., 918 F.2d 349 (2d Cir. 1990), applying state law will not "promote forum shopping by plaintiffs." LP Opp. 6.

[7] *See, e.g.*, *RCM Sec. Fund* v. *Stanton*, 928 F.2d 1318, 1324, 1326 (2d Cir. 1991); *Plymouth County Retirement Ass'n* v. *Schroeder*, 576 F. Supp. 2d 360, 369 (E.D.N.Y. 2008); *In re Countrywide Fin. Corp. Deriv. Litig.,* 554 F. Supp. 2d 1044, 1079 (C.D. Cal. 2008).

Plaintiffs nevertheless attempt to make something of the fact that the ICA provides for concurrent jurisdiction in state and federal courts, whereas the Exchange Act provides for exclusive jurisdiction in federal courts. *See* ABP Opp. 8; LP Opp. 9. Plaintiffs implicitly suggest that the Supreme Court in *Burks* and *Kamen* turned to state law to fill the gaps contained in the ICA only because both state and federal courts have the power to exercise jurisdiction over claims arising under that statute. But neither of these cases even hinted that the Court's decision to apply state law turned on the jurisdictional provisions of the ICA. Indeed, neither case mentioned that the ICA confers concurrent jurisdiction or cited the ICA provision that does so. And logically, the primacy of state law on corporate law matters does not turn on whether the claim in which the issue of corporate law arises is asserted in state or federal court.

ABP also argues that ICA claims warrant different treatment because that statute "merely impose[s] restrictions on what directors were otherwise entitled to do under state law," whereas the Exchange Act "impose[s] entirely new duties and obligations in connection with proxy solicitations." ABP Opp. 9. That is simply not true. As the above discussion of *Kamen* demonstrates, Section 20(a) of the ICA imposes on investment companies the same general prohibition against the use of materially misleading proxy statements imposed by Section 14(a) and, as the Court noted in *Kamen*, the SEC's regulations under the ICA require investment companies to "comply with the proxy statement rules promulgated under the [Exchange Act]." 500 U.S. at 93 n.1. Insofar as proxy statement disclosure is concerned, there is no meaningful distinction between the two statutes.

### C. Cases cited by plaintiffs are inapposite because they do not address claims by shareholders who did not buy, sell or exchange their own shares in the transaction on which they voted.

Plaintiffs argue that the federal courts have repeatedly recognized a right of shareholders to bring direct Section 14(a) claims "as a matter of federal law" and "without regard to state law." LP Opp. 13-16; *see also* ABP Opp. at 5 & n.3 (arguing that numerous federal courts have permitted direct Section 14(a) claims to proceed "without ***any*** reference to state law") (emphasis in original). The fallacy in this argument is that only a few of the cases plaintiffs cite involved Section 14(a) claims of the type at issue here — claims for damages brought by acquiring company shareholders, allegedly deprived of the right to cast an informed vote on a merger, for the post-merger decline in

the market price of their shares. *See In re JP Morgan Chase & Co. Sec. Litig.*, 2007 WL 4531794, at *8 (N.D. Ill. Dec. 18, 2007); *In re McKesson HBOC, Inc. Sec. Litig.*, 126 F. Supp. 2d 1248, 1266-68 (N.D. Cal. 2000); *Edge Partners, L.P.* v. *Dockser*, 944 F. Supp. 438, 440 (D. Md. 1996). And in those cases, defendants apparently failed to raise the issue of whether state law controlled the question; thus, the courts had no occasion to decide the issue. As such, there is no reason to think that even those courts would have diverged from the principles articulated by *Burks* and *Kamen* had that issue been presented.[8]

Accordingly, none of the cases cited by plaintiffs deviates from the proposition, flowing directly from *Burks*, *Kamen* and *Strougo*, that state law governs whether, in the circumstances of this case, plaintiffs may assert a direct claim for damages under Section 14(a).[9]

## II. UNDER DELAWARE LAW, PLAINTIFFS CANNOT MAINTAIN THE SECTION 14(a) CLAIMS THEY ASSERT AS DIRECT CLAIMS.

Under Delaware law, to assert a direct claim, a "stockholder must demonstrate that the duty breached was owed to the stockholder and ***that he or she can prevail without showing an injury to***

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[8] Many of the cases cited by Plaintiffs did not involve a merger transaction at all. *See Koppel* v. *4987 Corp.*, 167 F.3d 125 (2d Cir. 1999); *Amalgamated Clothing & Textile Workers Union* v. *Wal-Mart Stores, Inc.*, 54 F.3d 69 (2d Cir. 1995); *Weisberg* v. *Coastal States Gas Corp.*, 609 F.2d 650 (2d Cir. 1979); *Police & Fire Ret. Sys. of Detroit* v. *SafeNet, Inc.*, 645 F. Supp. 2d 210 (S.D.N.Y. 2009); *In re AOL Time Warner, Inc. Sec. & ERISA Litig.*, 381 F. Supp. 2d 192 (S.D.N.Y. 2004); *United Paperworkers Int'l Union* v. *Int'l Paper Co.*, 801 F. Supp. 1134 (S.D.N.Y. 1992); *Katz* v. *Pels*, 774 F. Supp. 121 (S.D.N.Y. 1991); *accord Stahl* v. *Gibraltar Fin. Corp.*, 967 F.2d 335 (9th Cir. 1992); *W. Dist. Council of Lumber Prod. & Indus. Workers* v. *La. Pac. Corp.*, 892 F.2d 1412 (9th Cir. 1989); *Smillie* v. *Park Chem. Co.*, 710 F.2d 271 (6th Cir. 1983); *Gladwin* v. *Medfield Corp.*, 540 F.2d 1266 (5th Cir. 1976).

And, of the cases that did involve a merger, most involved claims by acquired company shareholders who bought, sold or exchanged their shares in the transaction and who thus clearly had direct claims. *See Wilson* v. *Great Am. Indus., Inc.*, 979 F.2d 924 (2d Cir. 1992); *Mendell* v. *Greenberg*, 927 F.2d 667 (2d Cir. 1991); *Osofsky* v. *Zipf*, 645 F.2d 107 (2d Cir. 1981); *Shore* v. *Parklane Hosiery Co.*, 565 F.2d 815 (2d Cir. 1977); *Schlick* v. *Penn-Dixie Cement Corp.*, 507 F.2d 374 (2d Cir. 1974); *Gerstle* v. *Gamble-Skogmo, Inc.*, 478 F.2d 1281 (2d Cir. 1973); *accord Herskowitz* v. *Nutri/System, Inc.*, 857 F.2d 179 (3d Cir. 1988); *Lockspeiser* v. *W. Md. Co.*, 768 F.2d 558 (4th Cir. 1985); *Pavlidis* v. *New England Patriots Football Club, Inc.*, 737 F.2d 1227 (1st Cir. 1984); *Northway, Inc.* v. *TSC Indus., Inc.*, 512 F.2d 324 (7th Cir. 1975).

[9] Plaintiffs' citation to *Rudolph* v. *Cummins*, 2007 WL 1189632 (S.D. Tex. Apr. 19, 2007), is also insufficient. Perceiving "a lack of clarity in whether courts should look to state or federal law in resolving the direct/derivative dichotomy," *id.* at *2 n.4, the court determined to follow applicable Delaware law (the relevant state of incorporation) in granting a motion to stay the action in favor of proceedings by a special litigation committee, stating that it did so whether the alleged Section 14(a) claim was direct or derivative. No court has cited *Rudolph* on this (or any other) point, and certainly in this Circuit, as *Strougo* and its progeny hold, there is no "lack of clarity" on this issue. Nor is there any "lack of clarity" based on other recent Court of Appeals authority, including *Calamore* v. *Juniper Networks, Inc.*, 2010 WL 411138 (9th Cir. 2010), which — consistent with the Second Circuit's precedents — looked to state law to determine whether federal disclosure claims (including Section 14(a) claims) could be maintained as direct actions.

***the corporation***." *Tooley* v. *Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1039 (Del. 2004) (emphasis added). The Section 14(a) claims advanced by plaintiffs fail to satisfy the governing Delaware standard and thus cannot be sustained as direct claims. Indeed, under the Delaware Supreme Court's recent, controlling and squarely on-point decision in *J.P. Morgan*, plaintiffs' inability to sue directly in this case is clear. 906 A.2d at 772-73. However, in light of plaintiffs' assertions that Delaware law is to the contrary, if this Court is uncertain as to this application of Delaware law, Delaware both permits and encourages questions to be certified to the Delaware Supreme Court. *See* Def. Cert. Br. 3 n.4 (citing cases).

**A. Plaintiffs misconstrue Delaware law regarding the assertion of direct claims.**

An "infringement or deprivation of a shareholder's right to cast an informed vote" cannot alone sustain a direct claim for damages. *See* Def. Sec. Br. 70-74; Def. Sec. Reply 3-7; Def. 2/9/10 Ltr. at 2. As *J.P. Morgan* makes clear, the existence of "an alleged infringement of a 'right to cast an informed vote'" is only the start of the analysis. *J.P. Morgan*, 906 A.2d at 773. Facts must also be alleged showing "harm caused to the shareholders ***individually*** for being deprived of their right to cast an informed vote." *Id. See also Feldman* v. *Cutaia*, 951 A.2d 727, 733 (Del. 2008) ("In order to state a direct claim, the plaintiff must have suffered some ***individualized*** harm not suffered by all of the stockholders at large.").[10]

Plaintiffs do not cite a single paragraph in their complaints that pleads facts showing that the harm they claim is individual harm to Bank shareholders such that those shareholders could "prevail without showing an injury to the corporation." *Tooley*, 845 A.2d at 1036. To the contrary, the allegations in their complaints show that the damages sought are not separate from losses suffered by the Bank itself and felt by all shareholders pro rata. *See* Def. Sec. Br. 73 n.52; Def. Sec. Reply 7; Def. 2/9/10 Ltr. at 2-3; Def. 3/8/10 Ltr. at 3 (discussing Lead Plaintiffs' complaint); *see also* ABP Complaint ¶¶ 42, 284(e), 284(k) (making similar allegations). As shown in *J.P. Morgan*, whether

[10] In citing a purported "unbroken string of decisions reaffirming the bedrock principle that the infringement of a shareholder's right to cast an informed vote gives rise to a direct breach of fiduciary duty claim under Delaware law" (LP Opp. 20 & n.4), Lead Plaintiffs are attacking a straw man. The Bank Defendants do not argue that no direct claim could arise from a duty to cast an informed vote, but rather that the Section 14(a) claims at issue here — claims for damages asserted by Bank shareholders who did not themselves buy, sell or exchange shares — cannot be maintained as direct claims.

there is a "logical or reasonable relationship to the harm ***caused to the shareholders individually*** for being deprived of their right to cast an informed vote" is the critical issue. 906 A.2d at 773 (emphasis added). Yet plaintiffs here have not even attempted to plead that connection.

Lead Plaintiffs misinterpret *J.P. Morgan* in suggesting that it would countenance the direct claims they purport to assert here. *See* LP Opp. at 19. As shown (*see* 2/9/10 Letter at 4), Delaware law requires consideration of both the nature of the claim ***and*** the alleged injury in deciding if a direct claim can be sustained. *J.P. Morgan* teaches that, to recover damages, it is not enough for a shareholder plaintiff to show a breach of the duty of disclosure; the shareholder must show that he or she has suffered individual harm resulting from the deprivation of the right to cast an informed vote. Plaintiffs' apparent theory here is that the Bank's stock price fell once it became public that, as a result of Merrill's fourth quarter losses and bonus payments, the Bank paid too much for Merrill. *See* Lead Plaintiffs' Amended Complaint ¶¶ 194, 333(c), 333(k). *See also* ABP Complaint ¶¶ 42, 284(e), 284(k). But, as in *J.P. Morgan*, neither Lead Plaintiffs nor ABP have alleged any facts from which the "claimed infringement of their right to be told the material facts" resulted in individual harm to the Bank's shareholders, as opposed to harm to the Bank itself. 906 A.2d at 773. Only the Bank exchanged its shares in the merger; its shareholders did not. Under *J.P. Morgan*, therefore, plaintiffs' claims are not direct and should be dismissed.[11]

Lead Plaintiffs also cite *Mills* v. *Elec. Auto-Lite Co*., 396 U.S. 375, 377 (1970) (LP Opp. 22), in an attempt to distinguish *J.P. Morgan*'s discussion with respect to the interplay between the ability to assert direct claims and the damages sought with respect to those claims. But *Mills* and other federal authorities, which speak only to the substantive elements of a Section 14(a) claim and not to shareholder standing under Delaware law, cannot trump the holding of the Delaware Supreme Court on issues of Delaware corporate law. Moreover, the requirement in *Mills* that plaintiffs plead a causal connection between the injury they claimed and the transaction on which the shareholders

[11] In *St. Clair Shores Gen. Employees Ret. Sys.* v. *Eibeler*, 2008 WL 2941174 (S.D.N.Y. July 30, 2008) — a case upon which plaintiffs purport to rely — Judge Kram (citing *J.P. Morgan*) was skeptical that plaintiff had adequately pled its claim for damages based on defendants' alleged disclosure violations, even if "the right to cast an informed vote" might give rise to a direct claim. *See id.* at *23 & n.17. In any event, *St. Clair Shores* does not, as plaintiffs would have it (ABP Opp. 12-13) trump *J.P. Morgan* — nor could it as *J.P. Morgan* was issued by the Delaware Supreme Court, the ultimate arbiter of Delaware law.

voted, 396 U.S. at 388-89, cuts against plaintiffs. Plaintiffs here cannot simultaneously assert the contrary positions that, on the one hand, the harm they suffered is causally connected to the merger in which only the Bank exchanged its shares — as required by *Mills* to be cognizable under Section 14(a) — and, on the other, the harm they suffered was independent of the Bank — as required to state a direct claim under Delaware law. Either (i) the harm suffered by plaintiffs is separate from the merger, in which case they have no Section 14(a) claim, or (ii) the harm resulted from the merger and thus is not independent of the harm to the Bank, and thus they have no direct claim to assert under Delaware law. But plaintiffs cannot have it both ways.[12]

### B. The SEC settlement does not represent a concession that plaintiffs have a direct damage claim.

The ABP plaintiffs argue that the Bank's settlement of litigation with the SEC constitutes, in effect, an acknowledgement by the Bank that shareholders suffered cognizable harm and, thus, may state direct claims. *See* ABP Opp. 13. As shown previously, the Final Consent Judgment entered in the SEC actions makes clear that the Bank made no such admission, and the distribution of funds paid by the Bank pursuant to the "Fair Fund" provision of Section 308(a) of the Sarbanes-Oxley Act of 2002, 15 U.S.C. § 7246(a), does not constitute any determination that any loss suffered by a Bank shareholder was proximately caused by a violation of the securities laws. *See* Def. Supp. Br. 15-17.[13]

## III. CERTIFICATION IS AN APPROPRIATE AND EFFICIENT COURSE.

This Court is authorized to certify questions of Delaware law to the Delaware Supreme Court — the only Court that can provide definitively correct answers to such questions — and the Delaware Supreme Court may appropriately review such certified questions. If uncertainty exists as to the application of Delaware law to the issue of whether the Section 14(a) claims for damages asserted here can be maintained as direct claims, this Court should avail itself of that opportunity.

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[12] Lead Plaintiffs persist in asserting that "Defendants have not challenged . . . loss causation." LP Opp. 19 n.3. This is simply not true. *See* Def. Sec. Br. 74 n.53.

[13] The basis on which Plaintiffs seek to recover directly — alleged damages based upon a decline in the Bank's stock price — was not the basis on which the Consent Judgment was entered. That claim was never raised in the SEC Actions, and there was no adjudication that any Bank shareholder was harmed in any way.

**A. <u>There is no jurisdictional bar to certification.</u>**

Plaintiffs argue that because a Section 14(a) claim is within the exclusive jurisdiction of the federal courts under Section 27 of the Exchange Act, 15 U.S.C. § 78aa, this Court cannot delegate the certified question to the Delaware Supreme Court. *See* LP Opp. 5-7; ABP Opp. 4. This is plainly not the case. The issue proposed to be certified is not an issue of interpretation of the federal securities laws over which Section 27 creates exclusive federal jurisdiction. To the contrary, the proposed certified question is an issue of Delaware law, which, under *Kamen* and its progeny, must be applied to fill the gap in the federal remedial scheme and which the Delaware Supreme Court is best positioned to decide. Only this Court will be called upon to decide the issues of federal law presented by plaintiffs' Section 14(a) claims, and the exclusive jurisdiction that Section 27 grants to this Court over "violations" of the Exchange Act will not be abridged.

For this reason, too, Lead Plaintiffs' reliance on *Standard Power & Light Corp.* v. *Investment Associates, Inc.*, 51 A.2d 572, 579 (Del. 1947) (LP Opp. 1, 5, 6) is misplaced. The Bank Defendants do not seek the Delaware Supreme Court's interpretation of Section 14(a) or the elements of that cause of action; they seek a ruling with respect to an issue of Delaware law.[14]

**B. <u>Plaintiffs misstate the applicable legal standard for certification.</u>**

Plaintiffs' contention that this Court is not "permitted" to certify the proposed question (LP Opp. 4) is meritless. Under Delaware Supreme Court Rule 41, this Court may, in its discretion, certify a question of Delaware law so long as (1) there are "important and urgent" reasons for invoking the "immediate" aid of the Delaware Supreme Court and (2) the "facts material to the issue certified" are not in dispute. Del. Sup. Ct. R. 41; *see also* Def. Cert. Br. Point II.A. Rather than grappling with this broad grant of authority in Rule 41, Lead Plaintiffs have chosen to ignore it entirely and, instead, try to create obstacles to certification that appear nowhere in the text of Rule 41.

Lead Plaintiffs incorrectly argue that *L. Cohen & Co., Inc.* v. *Dun & Bradstreet, Inc.*, 629 F. Supp. 1419 (D. Conn. 1986), sets forth prerequisites to certification in addition to those in Rule 41.

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[14] Plaintiffs note that in *Arnold* v. *Society for Savings Bancorp, Inc.*, 678 A.2d 533, 539 (Del. 1996) (LP Opp. 2, 11, 12, 23), the Delaware Supreme Court declined to create a direct cause of action under state law for disclosure violations in a proxy statement. Plaintiffs nowhere explain why that precludes that Court from deciding, as it did in *J.P. Morgan*, whether the asserted disclosure claim is direct or derivative in nature.

LP Opp. 4. *L. Cohen & Co.* does no such thing. Although that decision offers several factors that federal judges "***might***" consider when exercising their discretion to invoke a state's certification procedure, where a state certification procedure is available, *L. Cohen & Co.* holds that the "decision whether to invoke the certification process" is "best left . . . to 'the sound discretion' of the individual federal judge." 629 F. Supp. at 1423-24, quoting *Lehman Bros.* v. *Schein*, 416 U.S. 386, 393 (1974). Accordingly, it does not purport to modify Rule 41 or any state certification rule.

Further, every case Lead Plaintiffs and ABP cite in an effort to transform the prudential considerations raised in the *L. Cohen & Co.* decision into mandatory prerequisites to certification (*see* LP Opp. 4, 24-25; ABP Opp. 17-18), without exception, involved the application of ***state rules other than those of Delaware***, which do not permit certification as broadly as Delaware's Rule 41 does.[15] The Delaware rule — which provides examples of "important and urgent reasons" for certification for "illustrat[ive]" purposes only — represents a marked departure from the more restrictive model adopted by those states, which requires more specific prerequisites be met prior to certification, including, for example, that the issue to be certified be "determinative" of an issue on which there is "no controlling precedent" in state law. *Compare, e.g.*, Del. Sup. Ct. R. 41(b) *with* N.Y. Ct. App. R. 500.27(a). Plaintiffs' reliance on these cases is thus misplaced.

### C. <u>Certification is warranted under Delaware Supreme Court Rule 41.</u>

Plaintiffs do not dispute that the proposed certified question implicates an important area of Delaware law. Plaintiffs also do not contest that a definitive answer to the proposed certified question may facilitate the adjudication of future state and federal cases. And plaintiffs also do not dispute that Delaware permits litigants to obtain expeditious resolution of unsettled issues by empowering trial courts to seek certification.

Lead Plaintiffs contend that resolution of the proposed certification would "not narrow the issues to be decided" in this case. But Lead Plaintiffs' brief in opposition to the Bank Defendants'

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[15] *See Holmes* v. *Grubman*, 568 F.3d 329, 339 (2d Cir. 2009) (Georgia); *Fid. & Guar. Ins. Underwriters, Inc.* v. *JASAM Realty Corp.*, 540 F.3d 133, 144 (2d Cir. 2008) (New York); *In re WorldCom, Inc.* v. *MCI*, 546 F.3d 211, 218 n.2 (2d Cir. 2008) (Kansas); *O'Mara* v. *Town of Wappinger*, 485 F.3d 693 (2d Cir. 2007) (New York); *Morris* v. *Schroder Capital Mgmt. Int'l*, 445 F.3d 525, 530-31 (2d Cir. 2006) (New York); *DiBella* v. *Hopkins*, 403 F.3d 102, 111-12 (2d Cir. 2005) (New York); *Green* v. *Montgomery*, 219 F.3d 52, (2d Cir. 2000) (New York); *Strougo* v. *Bassini*, 1 F. Supp. 2d 268, 274 (S.D.N.Y. 1998) (Maryland); *Wachovia Bank N.A.* v. *Cummings*, 2010 WL 466160, at *2 (D. Conn. Feb. 8, 2010) (Connecticut).

motion to dismiss their amended complaint devotes nearly 50 pages (from page 19 to page 68) to the merits of their Section 14(a) claims and such matter need not be addressed in detail if plaintiffs lack standing to assert the claims to which they relate. Moreover, Lead Plaintiffs' argument — that because they have alleged claims under Section 10(b) as well as under Section 14(a), eliminating the Section 14(a) claims would not narrow the issues — ignores their own pleading in which they assert that one need not plead purchaser status or scienter under Section 14(a) as one would under Section 10(b).[16] It also ignores the possibility that the Court may dismiss Lead Plaintiffs' Section 10(b) claims for a failure to plead scienter without reaching any issue Lead Plaintiffs contend would be applicable to their Section 14(a) claim (such as, for example, whether there was any material misrepresentation or omission). In that case, if the Section 14(a) claim were not dismissed for lack of standing here, its continued existence would potentially force the Court to undertake a full analysis of the disclosures and their materiality, which otherwise could have been avoided. As such, resolving the Section 14(a) claims may substantially narrow Lead Plaintiffs' remaining litigation.

Certification to the Delaware Supreme Court could have an even more profound impact on the spate of complaints recently filed by ABP and other Bank shareholders, which plead claims only under Section 14(a) (and related control person claims arising out of the proxy solicitation). If these claims cannot be maintained as direct claims, these complaints will be dismissed in their entirety.

## CONCLUSION

If the Court views the applicability of Delaware law to be uncertain, the Court should certify the proposed question to the Delaware Supreme Court.

[16] Lead Plaintiffs' attempt to manufacture a concession on the part of the Bank Defendants that Lead Plaintiffs need not prove scienter with respect to their Section 14(a) claims (LP Opp. 24 n.7) is without basis. The Bank Defendants have repeatedly made clear their position that Lead Plaintiffs are required to plead scienter with respect to their Section 14(a) claims as they "sound in fraud." *See* Def. Sec. Br. 30-31; Def. Sec. Reply 18-23. They thus do not concede this point but point out that even under Lead Plaintiffs' view that only negligence is required to be pled, the claims remaining post-certification may be substantially narrowed.

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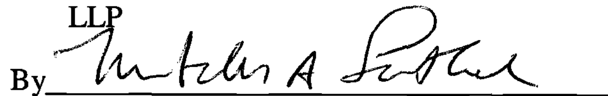

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