UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

IN RE: AMERICAN EXPRESS CO. SECURITIES LITIGATION

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02 Civ. 5533 (WHP)

MEMORANDUM AND ORDER

WILLIAM H. PAULEY III, District Judge:

Plaintiffs bring this securities class action lawsuit against American Express Company ("Amex" or the "Company") and Amex officers: Harvey Golub, Kenneth I. Chenault, Richard Karl Goeltz, Gary L. Crittenden, Daniel T. Henry, David R. Hubers and James M. Cracchiolo (the "Individual Defendants"). Plaintiffs purchased Amex common stock between July 26, 1999 and July 17, 2001 (the "Class Period"). The Second Consolidated Amended Class Action Complaint (the "Second Amended Complaint" or "SAC") alleges violations of § 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § 78j(b), and SEC Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5, and § 20(a) of the Exchange Act, 15 U.S.C. § 78t(a) (2000). Defendants move to dismiss the Second Amended Complaint. For the following reasons, Defendants' motion is granted.

BACKGROUND

I. Procedural History

Plaintiffs filed this action on July 17, 2002. The First Amended Complaint, dated December 10, 2002, alleged four claims: that the Company "(1) misrepresented Amex's high-yield investments as conservative when, in fact, they were high-risk; (2) concealed the extent of Amex's high-yield exposure; (3) failed to disclose the lack of risk management controls; and (4) failed to disclose the fact that Amex's accounting was not in accordance with

[Generally Accepted Accounting Principles ("GAAP"]." Slayton v. American Express, 460 F.3d 215, 221 (2d Cir. 2006). This Court dismissed the first claim finding that Plaintiffs failed to allege any misrepresentations and dismissed the second claim concluding that some of the alleged misstatements were protected projections, some were inactionable claims of mismanagement, and the remainder simply lacked a sufficient allegation of scienter. In re American Express Co. Sec. Litig., No. 02 Civ. 5533 (WHP), 2004 WL 632750, at *9-14 (S.D.N.Y. Mar. 31, 2004). This Court also dismissed the claims relating to risk management controls and accounting as time-barred. American Express, 2004 WL 632750, at *9-14.

The Court of Appeals vacated, finding that the claims relating to risk management controls and accounting were not time-barred because they related back to the first and second claims, respectively. Slayton, 460 F.3d at 228-29. The Second Circuit granted Plaintiffs leave to amend their complaint and suggested that amendments of the revived claims might cause this Court to reconsider its dismissal of the claims on the merits. Slayton, 460 F.3d at 230. To the extent Plaintiffs have re-pled claims that were dismissed on the merits, this Court reconsiders them.

II. Factual Background

For the purposes of this motion, the Court accepts the following facts as true. Golub was Amex's Chairman, chief executive officer and a director until his resignation at the end of 2000. (SAC ¶ 55(a).) Chenault, who had been Amex's President, chief operating officer and a director, replaced Golub as chief executive officer in January 2001. (SAC ¶ 55(b).) Goetz was chief financial officer of Amex until his resignation in June 2000. (SAC ¶ 55(c).) Crittenden replaced Goetz as Amex's chief financial in June 2000. (SAC ¶ 55(d).) Henry was

Amex's Controller during the Class Period. (SAC ¶ 55(e).) Hubers was President of Amex's subsidiary, American Express Financial Advisors ("AEFA"), and Cracchiolo was the chief executive officer and Chairman of AEFA. (SAC ¶¶ 55(f)-(g).)

Beginning in 1997, AEFA's life insurance division began to under-price its products in order to meet Golub's aggressive earnings targets. (SAC ¶¶ 71-72.) In order to maintain its profitability, AEFA invested in high-risk, high-yield debt securities such as below-investment grade bonds and collateralized debt obligations (the "High Yield Debt"). (SAC ¶¶ 8, 10-11.) While its peer companies limited High Yield Debt to 7 percent of their portfolios, AEFA's portfolio contained 10 to 12 percent High Yield Debt. (SAC ¶ 77.) The High Yield Debt investments and their associated risks were disclosed to the public in Amex's public filings. See American Express, 2004 WL 632750, at *10.

On January 22, 2001, Amex disclosed losses in AEFA's High Yield Debt portfolio of $49 million for fourth-quarter 2000 and $123 million for fiscal-year 2000. (SAC ¶ 84.) In late February 2001, AEFA's chief financial officer, Stuart Sedlacek, told Crittenden in an e-mail that AEFA's High Yield Debt portfolio was "deteriorating rapidly," and Crittenden relayed the information to Chenault. (SAC ¶ 210.) Sometime during February 2001, Chenault ordered a "very hard look" at AEFA's High Yield Debt. (SAC ¶ 209.) Subsequently, on April 2, 2001, Amex announced losses of $185 million in AEFA's High Yield Debt portfolio for the first quarter of 2001. (SAC ¶ 84.)

In early May 2001, Crittenden received a fax from Sedlacek advising him that Amex "was facing additional losses on its high-yield debt instruments beyond those already booked." (SAC ¶ 231.) A day later, Chenault was advised that the "deterioration of the high-yield debt portfolio was so bad that even the investment grade CDOs held by American Express

were likely damaged, due to the fact that defaults in underlying bonds had increased so sharply." (SAC ¶ 231.) As a result Amex assigned its treasurer, a senior risk management vice president, and a team of in-house analysts to assess the High Yield Debt portfolio. (SAC ¶ 232.)

On July 18, 2001, Amex announced that its earnings for second-quarter 2001 would likely decline 76% from the previous year in part because of an $826 million pre-tax charge to recognize "additional write-downs in the high-yield debt portfolio at [AEFA] and losses associated with rebalancing the portfolio towards lower-risk securities." (SAC ¶ 236.) On the same day, Amex announced that it would scale back AEFA's High Yield Debt investments to 7% of its portfolio. (SAC ¶ 240.) Chenault stated that Amex's "analysis of the portfolio at the end of the first quarter [of 2001] did not fully comprehend the risks that underline these structured investments during a period of persistently high default rates." (SAC ¶ 257.) In its 2001 Annual Report, Amex announced that it had created a risk management committee to "supplement the risk management capabilities resident within its business segments by routinely reviewing key market, credit and other risk concentrations across the company and recommending corrective action where appropriate." (SAC ¶ 251.)

The Second Amended Complaint alleges three categories of fraud during the Class Period relating to the High Yield Debt investments: (1) false and misleading statements that Amex had adopted risk management policies; (2) the failure to properly account for AEFA's investment losses resulting from the High Yield Debt investments in accord with GAAP; and (3) mischaracterizations of the developments relating to AEFA's High Yield Debt in 2001.

A. Risk Management Policies

According to two former AEFA pricing analysts, who were employed during the Class Period, AEFA's analysts were often "entirely unfamiliar with the bonds underlying their

investments and instead merely relied on brokers' representations as to the [High Yield Debt] securities' value." (SAC ¶¶ 93, 99.) In addition, one pricing analyst stated that if a current price could not be obtained for a security, the price would be left unadjusted from its previous price. (SAC ¶ 103.) Plaintiffs allege that as a result of these "deficient procedures used for evaluating AEFA's high-yield debt holdings" it was "impossible to monitor and gauge the risk accurately on its high-yield debt investments, and no such real risk monitoring or analysis was taking place." (SAC ¶ 130.) In addition, Plaintiffs allege that the investigations in February and May 2001, Chenault's July 18, 2001 statement, and the establishment of a new risk management committee demonstrate the "absence of any significant or consistent risk control or monitoring policies or procedures." (SAC ¶¶ 257-58.)

Therefore, Plaintiffs claim that the following statements during the Class Period were false and misleading. First, Amex's Annual Reports for 1999 and 2000 stated that "[m]anagement establishes and oversees implementation of Board-approved policies covering the company's funding, investments and use of derivative financial instruments and monitors aggregate risk exposures on an ongoing basis." (SAC ¶¶ 128-29, 256.) The Company also stated that AEFA's "[i]nvestments in fixed income securities provides . . . a dependable and targeted margin between the interest rate earned on investments and the interest rate credited to clients' accounts" and that AEFA "regularly review[ed] models projecting different interest rate scenarios and their effect on the profitability." (SAC ¶¶ 128-29, 256.) Goeltz, Golub, Chenault, and Henry all signed these reports. (SAC ¶¶ 128-29.) Second, on February 3, 2000, Hubers stated in a presentation to financial analysts that diversification of AEFA's asset base "allowed AEFA to weather market dislocations by helping to mitigate the impact of AEFA's earnings from market volatility." (SAC ¶¶ 187, 256.) Finally, on February 7, 2001, during a presentation

to financial analysts, Chenault stated that Amex had "accepted that [returns from high-yield debt] came with higher risk" and that its "risk management staff [was] among the best in the business." (SAC ¶¶ 214-15, 256; Affidavit of Christopher P. Malloy dated Oct. 15, 2007 Ex. V: American Express Feb. 7, 2001 Financial Community Presentation at 7.)

B. High Yield Debt Accounting

Plaintiffs allege several violations of GAAP related to AEFA's High Yield Debt portfolio. First, Plaintiffs claim that Defendants violated the GAAP principle requiring impairments in the value of an investment to be accounted for even when the investment is normally carried at cost. (SAC ¶ 157.) AEFA ignored "adverse news, trends or events, which included significant defaults, increasing and persistently high default rates, and bankruptcy filings that negatively impacted the high-yield debt market," and continued to amortize its High Yield Debt securities at cost rather than fair market value despite the "increasing divergence before and during the Class Period between cost and fair market value." (SAC ¶¶ 151,156.) When Amex valued the High Yield Debt investments at fair market value, the valuation methods, as described above, were inadequate. (SAC ¶ 159.) In addition, Amex did not separately account for the High Yield Debt, but rather lumped together all corporate debt securities in its financial statements. (SAC ¶ 159.) This had the effect of disguising the magnitude of AEFA's High Yield Debt losses. (SAC ¶ 190.) Second, Plaintiffs claim that Defendants violated a GAAP requirement that the cost basis must be written down to fair value and the amount of the write-down included in earnings whenever a decline in fair value below amortized cost is "other than temporary". (SAC ¶ 165.) Third, Plaintiffs claim Defendants violated GAAP by failing to detail the probabilities of loss for the High Yield Debt. (SAC ¶ 169.) Fourth, Plaintiffs claim Defendants violated GAAP by misleading shareholders about the

adequacy of Amex's valuation methods and compliance with GAAP. (SAC ¶ 173.) Finally, Plaintiffs claim that by failing to properly value the High Yield Debt, Defendants reported materially false and misleading quarterly income growth during 1999 and 2000. (SAC ¶ 196.)

C. Developments in 2001

Plaintiffs claim that Amex attempted to minimize "the amount of damage to AEFA's portfolio with a series of misleading 'damage control' statements designed to reassure the market." (SAC ¶ 262.) First, on February 7, 2001, during a presentation to the financial analyst community, Chenault acknowledged that Amex had some issues with its High Yield Debt in 2000, but stated that the Company had "significantly scaled back [its] activity" in "structured investments, such as collateralized debt obligations" and characterized AEFA's "fundamental business model" as "sound." (SAC ¶¶ 207, 211, 262.) According to a former AEFA financial advisor, AEFA had not "significantly scaled back" its investments in CDOs and the "portfolio was still highly unbalanced and overvalued at that time due to junk bonds and risky CDOs." (SAC ¶ 219.) Second, on April 2, 2001, in a press release announcing its first-quarter 2001 results, including the $185 million in losses from High Yield Debt investments, Amex stated that "[t]otal investment losses on [AEFA's high-yield instruments] for the remainder of 2001 are expected to be substantially lower than in the first quarter." (SAC ¶ 219.) Cracchiolo and Crittenden made similar statements during conference calls on the same day. (SAC ¶¶ 223, 225.) Third, on an April 2, 2001 conference call, Cracchiolio attributed the write-downs to "asbestos problems and fallen angels that were in better graded areas that came about rather quickly." (SAC ¶ 224.) Plaintiffs claim that this statement falsely suggested that the problems with the High Yield Debt were new and unexpected. (SAC ¶ 224.) Fourth, on May 15, 2001, Amex's filing for the first quarter of 2001 stated "[t]otal losses on [AEFA's High Yield

Debt] investments for the remainder of 2001 are expected to be substantially lower than in the first quarter." (SAC ¶ 230.)

DISCUSSION

I. Legal Standard

On a motion to dismiss, the Court must accept the material facts alleged in the complaint as true and construe all reasonable inferences in the plaintiff's favor. Grandon v. Merrill Lynch & Co., 147 F.3d 184, 188 (2d Cir. 1998). Nonetheless, "factual allegations must be enough to raise a right of relief above the speculative level, on the assumption that all of the allegations in the complaint are true." Bell Atl. Corp. v. Twombly, ___ U.S. ___, 127 S. Ct. 1955, 1965 (2007) (requiring plaintiff to plead "enough fact[s] to raise a reasonable expectation that discovery will reveal evidence of [his claim]"); see also ATSI Commc'ns, Inc. v. Shaar Fund, Ltd., 493 F.3d 87, 98 (2d Cir. 2007) ("We have declined to read Twombly's flexible 'plausibility standard' as relating only to antitrust cases.").

A court's "consideration [on a motion to dismiss] is limited to facts stated on the face of the complaint, in documents appended to the complaint or incorporated in the complaint by reference, and to matters of which judicial notice may be taken." Allen v. WestPoint-Pepperell, Inc., 945 F.2d 40, 44 (2d Cir. 1991).

II. Section 10(b)

To state a claim for a violation of Section 10(b) of the Exchange Act and Rule 10b-5, a plaintiff must allege, inter alia, that a defendant made misstatements or omissions of material fact with scienter. Lentell v. Merrill Lynch & Co., Inc., 396 F.3d 161, 172 (2d Cir.

2005). "Scienter, as used in connection with the securities fraud statutes, means intent to deceive, manipulate, or defraud or at least knowing misconduct." SEC v. First Jersey Sec., Inc, 101 F.3d 1450, 1467 (2d Cir. 1996).

A plaintiff must "state with particularity facts giving rise to a strong inference that the defendant" acted with scienter. 15 U.S.C. § 78u-4(b)(2). "[I]n determining whether the pleaded facts give rise to a 'strong' inference of scienter, the court must take into account plausible opposing inferences." Tellabs, Inc. v. Makor Issues & Rights, Ltd., __ U.S. __, 127 S. Ct. 2499, 2510 (2007). For an inference of scienter to be strong, "a reasonable person [must] deem [it] cogent and at least as compelling as any opposing inference one could draw from the facts alleged." Tellabs, 127 S. Ct. at 2510. "The inquiry . . . is whether all of the facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegation, scrutinized in isolation, meets that standard." Tellabs, 127 S.Ct at 2509 (emphasis in original).

A plaintiff may establish scienter by showing that defendants: "(1) benefited in a concrete and personal way from the purported fraud; (2) engaged in deliberately illegal behavior; (3) knew facts or had access to information suggesting that their public statements were not accurate; or (4) failed to check information they had a duty to monitor." Teamsters Local 445 Freight Div. Pension Fund v. Dynex Capital Inc., __ F.3d __, 2008 WL 2521676, at *3 (2d Cir. Jun. 26, 2008) (quoting Novak v. Kasaks, 216 F. 3d 300, 311 (2d Cir. 2000)). "[A]n allegation that defendants were motivated by a desire to maintain or increase executive compensation is insufficient because such a desire can be imputed to all corporate officers." Kalnit v. Eichler, 264 F.3d 131, 140 (2d Cir. 2001). "It is well established that boilerplate allegations that defendants knew or should have known of fraudulent conduct based solely on their board

membership or executive positions are insufficient to plead scienter." In re Sotheby's Holdings, Inc., No. 00 Civ. 1041 (DLC), 2000 WL 1234601, at *7 (S.D.N.Y. Aug. 31, 2000); see also In re Winstar Commc'ns, No. 01 Civ. 3014 (GBD), 2006 WL 473885, at *7 (S.D.N.Y. Feb. 27, 2006).

"In addition to actual intent . . . recklessness is a sufficiently culpable mental state in the securities fraud context." Dynex, 2008 WL 2521676, at *3. Recklessness requires a showing of "reckless disregard for the truth, that is, conduct which is highly unreasonable and which represents extreme departure from standards of ordinary care." SEC v. McNulty, 137 F.3d 732, 741 (2d Cir.1998). "[A]n allegation that a defendant merely 'ought to have known' is not sufficient to allege recklessness." Hart v. Internet Wire, Inc., 145 F. Supp. 2d 360, 368 (S.D.N.Y. 2001) (quoting Troyer v. Karcagi, 476 F.Supp. 1142, 1152 (S.D.N.Y. 1979)); see also In re Bayou Hedge Fund Litig., 534 F. Supp. 2d 405, 415 (S.D.N.Y. 2007). Even an "egregious failure to gather information will not establish 10b-5 liability as long as the defendants did not deliberately shut their eyes to the facts." Hart, 145 F. Supp. 2d at 368-69 (internal quotation marks and citations omitted).

A. General Scienter Allegations

The Second Amended Complaint alleges that Defendants were motivated to commit fraud by a desire to meet aggressive income targets and that Hubers and Golub were specifically motivated by their incentive compensation. (SAC ¶¶ 281, 286-87.) Plaintiffs also allege that Defendants knew or should have known of the fraud because of their executive and managerial positions with Amex. (SAC ¶¶ 283, 284.) Although the Court must consider all of the facts collectively, under well established law in this circuit, these allegations are not entitled to any weight. See Kalnit, 264 F.3d at 140; Sotheby's Holdings, 2000 WL 1234601, at *7.

Plaintiff also alleges that if Defendants did not know, they were reckless in not being aware that "persistent, record high, and ascending default rates among high-yield debt instruments" were impacting AEFA's High Yield Debt throughout the Class Period and that the "haphazard, deficient and/or non-existent valuation reporting methods" mislead investors regarding "the true condition of American Express's reported earnings and earnings growth." (SAC ¶¶ 33, 141, 183, 288.) Again, because these allegations do no more than state in conclusory fashion what Defendants should have known, they are not entitled to any weight. See, e.g., Hart, 145 F. Supp. 2d at 368-69; Bayou, 534 F. Supp. 2d at 415.

B. Confidential Informants

The Second Amended Complaint also relies on the following scienter allegations attributed to confidential sources: (1) a former AEFA vice president, who left the company in 1998, stated that an AEFA portfolio manager warned Hubers of the risks involved in investing in high-yield securities, (SAC ¶ 74); (2) a former AEFA pricing analyst, who was employed during the Class Period stated that "[w]e knew that the junk market was getting bad," (SAC ¶ 108); (3) a former portfolio manager, who was employed throughout the Class Period, stated that he didn't know "why anyone in New York at corporate would have been surprised by any charges that came out of a high-yield portfolio" during the Class Period, (SAC ¶ 108); (4) a former chief information officer for the AEFA equity advisory board, who was employed throughout the Class Period, indicated that "he had understood that senior management had been warned that the Company was 'hanging itself' with its huge stakes in junk bonds, and that another senior employee had even gone so far as to put memos together to provide warnings of the problems with junk bonds," (SAC ¶ 108); (5) a former director of electronic payments strategy in the insurance department of AEFA and in Amex's credit card business, employed during the Class

Period, stated that there was pressure to conceal the impairment of AEFA's CDOs, (SAC ¶ 110); (6) a former AEFA financial advisor stated that "there was a focused attempt to put a positive public relations spin on the situation," (SAC ¶ 111); (7) a former portfolio manager of the Fixed Income Department stated that "Hubers had been goosing the numbers to look like a hero [sic] also tried to make Golub look good," (SAC ¶ 111); (8) a former AEFA vice president stated that Chenault was familiar with AEFA's practice of increasing its earnings through its accounting for high-yield investments because Hubers, "who sanctioned and engineered AEFA's high-yield debt investments strategy" reported directly to Chenault, (SAC ¶ 282); and (9) a former AEFA Financial Advisor stated that "AEFA was aware that the portfolio was still highly unbalanced and overvalued" in April 2001, (SAC ¶ 219).

A complaint may rely on confidential sources as long as the facts alleged "provide an adequate basis for believing that the defendants' statements were false." Novak, 216 F.3d at 314. In addition, the confidential sources must be "described in the complaint with sufficient particularity to support the probability that a person in the position occupied by the source would possess the information alleged." Novak, 216 F.2d at 300.

While the Court of Appeals has not addressed the weight to be afforded allegations based on confidential sources in light of Tellabs, the Seventh Circuit held after Telllabs that "allegations from confidential witnesses must be discounted" because "[i]t is hard to see how information from anonymous sources could be deemed compelling or how we could take account of plausible opposing inferences. Perhaps these confidential sources have axes to grind. Perhaps they are lying. Perhaps they don't even exist." Higginbotham v. Baxter Int'l, Inc., 495 F.3d 753, 757 (7th Cir. 2007). However, several district courts in this circuit have considered allegations based on confidential sources after Tellabs without discounting them. See

e.g., City of Brockton Ret. Sys. v. Shaw Group Inc., 540 F. Supp. 2d 464, 474 (S.D.N.Y. 2008) (declining to adopt the Higginbotham standard); In re Xethanol Corp. Secs. Litig., No. 06 Civ. 10234 (HB), 2007 WL 2572088, at *3, n.3 (S.D.N.Y. Sept. 7, 2007)(descriptions of confidential sources were sufficient to allow the court "to infer that the witnesses are likely to posses the information contained in their statements").

None of the confidential sources specifically states that any Individual Defendant had information or access to information indicating that Amex was not properly valuing the High Yield Debt, that its risk control policies were inadequate, that Amex was violating GAAP, or that contradicted the Company's statements in 2001. See, e.g., Shaw Group, 540 F. Supp. 2d at 474 (allegations based on confidential sources did not establish scienter where they did not show that defendants had information regarding accounting irregularities). Allegations that Hubers and senior management were warned of the risks or that senior management should not have been surprised by the charges relating to High Yield Debt show only that the Individual Defendants may have been made aware of the risks associated with the High Yield Debt, not that Amex was not properly valuing the debt or monitoring its risk. See, e.g., Malin v. XL Capital Ltd., 499 F. Supp. 2d 117, 141 (D. Conn. 2007) (statements by confidential sources that accounting deficiencies were well known were insufficient to establish scienter). Allegations that Hubers reported to Chenault are meaningless unless Plaintiffs establish what Hubers knew or should have known. Plaintiffs' allegation that Hubers "sanctioned and engineered AEFA's high-yield debt investments strategy" does not establish that Hubers was aware of any information contradicting the Company's statements. Moreover, Plaintiffs fail to allege any specific details regarding what Hubers told Chenault.

Plaintiffs have also failed to allege any facts showing that the confidential sources—AEFA portfolio managers, an AEFA vice president who left AEFA prior to the start of the Class Period,[1] a chief information officer of the equity advisory group, an AEFA pricing analyst, one or more AEFA financial advisors, and an Amex director of Electronic Payments Strategy—had any contact with the Individual Defendants or would have knowledge of what they knew or should have known during the Class Period. See, e.g., In re Elan Corp. Secs. Litig., 543 F. Supp. 2d 187, 219 (S.D.N.Y. 2008) (allegations based on confidential sources were insufficient to establish scienter where there were no facts to establish that the confidential sources would have known what information was communicated to senior executives).

D. February and May 2001 Communications

Finally, the Second Amended Complaint does specifically allege that Cracchiolo and Crittenden received information from Sedlacek in February and May 2001 which alerted them or should have alerted them to the fact that their public statements were false and misleading. In late February 2001, Crittenden and Chenault were aware of deterioration in the High Yield Debt portfolio as a result of an email from Sedlacek. However, this does not demonstrate that either Crittenden or Chenault were aware that the Company's April 2001 statements that "[t]otal investment losses on [AEFA's high-yield instruments] for the remainder of 2001 are expected to be substantially lower than in the first quarter" or Cracchiolio's statement during an April 2, 2001 conference call attributing the write-downs to "asbestos problems and fallen angels that were in better graded areas that came about rather quickly" were false and misleading. After the February 2001 email, Chenault ordered a "very hard look" at

[1] In some instances, the Second Amended Complaint refers to a former vice president who left AEFA before the Class Period, while in other instances it refers to a former AEFA vice president, without indicating whether he or she worked at AEFA during the Class Period. (SAC ¶¶ 74, 282.) The Court assumes this is the same person.

AEFA's High Yield Debt and there are no facts alleged that suggest the result of that "very hard look" was inconsistent with the April 2001 statements. In fact, the allegation that in early May 2001 Crittenden and Chenault learned that Amex would have to book further losses from AEFA's High Yield Debt investments suggests that prior to that date there was no reason for them to believe the April 2001 statements were false and misleading.

Amex again stated on May 15, 2001 that "[t]otal investment losses on [AEFA's high-yield instruments] for the remainder of 2001 are expected to be substantially lower than in the first quarter." The information Crittenden and Chenault received in May 2001 could support an inference of scienter because it suggests that they had access to information indicating that the May 15, 2001 statement was no longer accurate. However, in light of the fact that Defendants immediately put together a team to analyze all of AEFA's High Yield Debt and then announced the results of the analysis in July 2001, the more compelling inference is that Defendants were not acting with an intent to deceive, but rather attempting to quantify the extent of the problem before disclosing it to the market. See Baxter, 495 F.3d at 758 (fact that defendant had learned information leading to the "launch of an investigation . . . is a very great distance from convincing proof of intent to deceive.")

D. Duty to Monitor

"A strong inference of recklessness may arise where plaintiffs point to 'facts demonstrating that defendants failed to review or check information that they had a duty to monitor, or ignored obvious signs of fraud.'" Pension Comm. of Univ. of Montreal Pension Plan v. Banc of America Secs., 446 F. Supp. 2d 163, 181 (S.D.N.Y. 2006) (quoting Novak, 216 F.3d at 308). Plaintiffs' allegations that Defendants initiated examinations of the High Yield Debt

portfolio both in February 2001 and May 2001 suggest that Defendants upheld their duty to monitor and precludes any inference of recklessness.

Accordingly, Plaintiffs have failed to plead scienter and Defendants' motion to dismiss the § 10(b) claim is granted.

III. Section 20(a) Claims

"In order to establish a prima facie case of liability under § 20(a), a plaintiff must show, inter alia, a primary violation by a controlled person." In re Alstom SA Sec. Litig., 454 F. Supp. 2d 187, 209 (S.D.N.Y. 2006) (quoting Boguslavsky v. Kaplan, 159 F.3d 715, 720 (2d Cir. 1998)); see also 15 U.S.C. § 78t(a). Because the Complaint fails to allege a primary violation by a controlled person, Defendants' motion to dismiss the § 20(a) claim is granted.

CONCLUSION

For the foregoing reasons, Defendants' motion to dismiss is granted and the Second Consolidated Amended Class Action Complaint is dismissed in its entirety. The Clerk of the Court is directed to terminate all pending motions and mark the case as closed.

Dated: September 26, 2008
New York, New York

SO ORDERED:

WILLIAM H. PAULEY III
U.S.D.J.

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