

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

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In re:	:	
	:	
LEHMAN BROTHERS SECURITIES	:	09 MD 2017 (LAK)
AND ERISA LITIGATION	:	
	:	
This document applies to:	:	
	:	
<i>In re Lehman Brothers Mortgage-Backed Securities</i>	:	
<i>Litigation, No. 08-CV-6762 (LAK)</i>	:	
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**THE INDIVIDUAL DEFENDANTS' MEMORANDUM OF LAW IN
OPPOSITION TO THE PUBLIC EMPLOYEES' RETIREMENT SYSTEM
OF MISSISSIPPI'S MOTION TO INTERVENE**

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PRELIMINARY STATEMENT

On March 18, 2010, the Public Employees' Retirement System of Mississippi ("PERS") moved to intervene in this action to assert Securities Act claims on behalf of a putative class of purchasers of mortgage-backed securities ("Intervenor Class") in three offerings that occurred in 2005 and 2006 ("New Offerings"). PERS's motion comes over three years after the securities at issue were first offered to the public, nearly 18 months after the first putative class action suit in this action was filed, and over a year after the existing plaintiffs ("Plaintiffs") filed a Consolidated Securities Class Action Complaint ("CAC"), the surviving allegations of which PERS now seeks to adopt. Because of PERS's years of inaction, the claims it seeks to assert on behalf of itself and the Intervenor Class are barred by the applicable three-year statute of repose and the one-year statute of limitations. The motion to intervene should be denied.

Any argument that the statutes of repose and limitations were tolled by the filing of the putative class action would be without merit. The Second Circuit, in *Korwek v. Hunt*, 827 F.2d 874 (2d Cir. 1987), held that the tolling rule announced in *American Pipe and Construction v. Utah*, 414 U.S. 538, 94 S.Ct. 756 (1974), does not allow a party to resuscitate otherwise time-barred class claims that have been dismissed. The *Korwek* court stated that extending the *American Pipe* decision to those circumstances would sanction an abuse of the class action process and would be inconsistent with the principles of efficiency and fairness underlying the *American Pipe* decision. As observed by Judge Nickerson in *In re Crazy Eddie Sec. Litig.*, 747 F. Supp. 850, 856 (E.D.N.Y. 1990), the Second Circuit's concerns in *Korwek* are more acute when the time-barred claims that a new plaintiff seeks to reassert on behalf of a class were previously dismissed for lack of standing. Tolling the statutes of repose and limitations for putative class action claims brought by plaintiffs who lack standing until other plaintiffs with standing can be identified would invite a practice of "sue first and find plaintiffs later." In the

words of the *Crazy Eddie* court, “[t]here appears to be no good reason to encourage bringing of a suit merely to extend the period in which to find a class representative.” *Id.*

Moreover, because Plaintiffs’ lack of standing was a jurisdictional defect under Article III of the Constitution, this Court never had subject matter jurisdiction over the now-dismissed claims arising out of the offerings in which no named plaintiff purchased securities, including the securities allegedly purchased by PERS. Thus, the filing of those claims by Plaintiffs without standing did not toll the statutes of repose or limitations with respect to the New Offerings. Simply stated, “[i]f the original plaintiffs lacked standing to bring their claims in the first place, the filing of a class action complaint does not toll the statute of limitations for other members of the purported class.” *In re Colonial Ltd. Partnership Litig.*, 854 F. Supp. 64, 82 (D. Conn. 1994) (Cabranes, J.).

Because the New Offerings are not included in this action, PERS has no interest in the subject of the action and therefore does not satisfy the requirements for mandatory intervention pursuant to Fed. R. Civ. P. 24(a). And because PERS’s class claims are time-barred, PERS cannot satisfy the requirements for permissive intervention under Fed. R. Civ. P. 24(b). The motion to intervene should be denied.

PROCEDURAL BACKGROUND

This litigation began in June 2008, when Alaska Electrical Pension Fund commenced an action in New York Supreme Court alleging violations of the Securities Act in connection with various offerings of mortgage-backed securities. In July 2008, New Jersey Carpenters Health Fund filed its own suit in New York Supreme Court. The Individual Defendants subsequently removed the two actions, and they were consolidated by the Court.

On February 23, 2009, Plaintiffs filed the CAC purportedly on behalf of a class of all persons or entities who purchased or acquired mortgage-backed securities issued in 94 offerings between September 2005 and July 2007. Plaintiffs, however, had not purchased any securities in 85 of the 94 offerings and, therefore, had not suffered any injury in connection with those offerings. CAC at ¶¶ 22 - 24.

On April 27, 2009, the Individual Defendants¹ moved to dismiss the CAC with prejudice pursuant to Fed. R.Civ. P. 12(b)(6). In particular, they argued that Plaintiffs lacked standing with respect to offerings in which they did not purchase securities. This Court's Memorandum Opinion (as amended) granted in part the motion to dismiss. *See In re Lehman Brothers Mortgage-Backed Securities Litigation*, No-08-CV-6762 (S.D.N.Y. Feb 23, 2010), Slip Op. ("Mem. Op.") at 17–18. On the issue of standing, the Court held:

As no named plaintiff has alleged that he or she purchased Certificates in any of the other eighty-five offerings, none can have been injured with respect to those offerings. None, therefore, has standing to bring claims with respect to these offerings.

Id.

On March 18, 2010, PERS filed a motion to intervene in this action as a named plaintiff on behalf of itself and the Intervenor Class of all those who purchased securities in three New Offerings dismissed from the action by the Court.

ARGUMENT

I. PERS DOES NOT MEET THE REQUIREMENTS FOR MANDATORY INTERVENTION UNDER RULE 24(a)

Rule 24(a) of the Federal Rules of Civil Procedure provides that a party may intervene as of right in an action where that party "(1) files a timely motion; (2) asserts an

¹ The Individual Defendants are Lana Franks Harber, Edward Grieb, Richard McKinney, Kristine Smith, James J. Sullivan, Samir Tabet and Mark L. Zusy.

interest relating to the property or transaction that is the subject of the action; (3) is so situated that without intervention the disposition of the action may, as a practical matter, impair or impede its ability to protect its interest; and (4) has an interest not adequately represented by other parties.” *U.S. v. Pitney Bowes, Inc.*, 25 F.3d 66, 70 (2d Cir. 1994). PERS does not satisfy these criteria. The New Offerings pursuant to which PERS allegedly purchased securities are not the “subject” of the action because Plaintiffs never had standing to bring claims arising out of those Offerings and, as a result, the Court dismissed them from this action. Because the New Offerings are not the subject of this action, PERS has no “interest” in the case to be represented, and the disposition of this action will not impair or impede PERS’s ability to protect its interests (or the interests of the members of the proposed Intervenor Class). In short, PERS is not necessary for the disposition of the action. *See MasterCard Intern. Inc. v. Visa Intern. Service Ass’n, Inc.*, 471 F.3d 377, 389-90 (2d Cir. 2006) (only “necessary” parties under Rule 19(a) may intervene as of right); Fed. R. Civ. P. 24, Advisory Committee’s Note (“Intervention of right is here seen to be a kind of counterpart to Rule 19(a)(2)(i) The [1966] amendment provides that an applicant is entitled to intervene in an action when his position is comparable to that of a person under Rule 19(a)(2)(i).”)

II. PERS IS NOT ENTITLED TO PERMISSIVE INTERVENTION UNDER RULE 24(b) BECAUSE ITS CLAIMS ARE BARRED BY THE STATUTES OF REPOSE AND LIMITATIONS

Permissive intervention is available at the discretion of the Court when the motion is timely and the proposed intervenor “has a claim or defense that shares with the main action a common question of law or fact.” Fed. R. Civ. P. 24(b)(1)(B). Here, the class claims PERS proposes to asset are barred by both the statute of repose and the statute of limitations; there is no “claim” with questions of law or fact common to those of the main action because there is no

valid claim at all. “[I]ntervention will not be permitted to breathe life into a nonexistent lawsuit.” *McClune v. Shamah*, 593 F.2d 482, 486 (3d Cir. 1979) (quoting *Fuller v. Volk*, 351 F.2d 323, 328 (3d Cir. 1965) (internal quotes omitted).

A. Unless Tolled, the Statutes of Repose and Limitations Bar the Claims of PERS and the Intervenor Class

Section 13 of the Securities Act sets forth statutes of repose and limitations applicable to Section 11 claims:

No action shall be maintained to enforce any liability created under section 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*

15 U.S.C. § 77m (emphasis added). PERS asserts that it purchased securities in three New Offerings: Lehman XS Trust, Series 2005-8; Lehman XS Trust, Series 2006-16N; and First Franklin Mortgage Loan Trust, Series 2006-FFB. These securities were first offered to the public on November 1, 2005, October 16, 2006, and November 30, 2006, respectively. PERS filed its motion to intervene on March 18, 2010 – well over three years from the date the securities were offered to the public.

In addition, PERS filed its motion more than one year after Plaintiffs filed the CAC and more than 18 months after the actions consolidated by this Court were commenced. It cannot be disputed that, at a minimum, PERS in the exercise of reasonable diligence should have known about the purported misstatements and omissions alleged in the CAC because the wealth of information in the public domain cited in the CAC was equally available to PERS as to the Plaintiffs. *See, e.g.*, CAC at ¶¶ 109, 133, 141, 162, 174-75, 181, 231.

Accordingly, unless tolled, the three-year statute of repose and one-year statute of limitations under Section 13 pose an absolute bar to PERS’s claims.

B. The *American Pipe* Tolling Rule Is Inapplicable to PERS's Claims Because Plaintiffs Lacked Standing to Assert Claims Arising Out of the Securities PERS Purchased

Although the motion to intervene ignores the applicable statute of repose and statute of limitations, PERS will presumably seek to argue that the statutes were tolled until the New Offerings were dismissed from this action pursuant to *American Pipe and Construction v. Utah*, 414 U.S. 538, 94 S.Ct. 756 (1974), and its progeny. Such an argument would be misplaced.²

In *American Pipe*, the Supreme Court held that members of a putative class were not barred by the statute of limitations from moving to intervene to assert claims *on their own behalf* after the court denied class certification (the proposed intervenors did not seek to assert claims on behalf of a class). *Id.* at 553, 766. The Court reasoned that “the efficiency and economy which is a principal purpose of the [class action] procedure” would not be served if class members were “induced to file protective motions to intervene or to join in the event that a class was later found to be unsuitable.” *Id.* at 553, 766. The Court, however, balanced the principles of “efficiency and economy” with the “policies ensuring essential fairness to defendants” and deemed that the latter were satisfied when “a plaintiff *who is found to be representative of a class* commences a suit.” *Id.* at 554-55, 767 (emphasis added). The Court

² There is “some dispute” whether the *American Pipe* rule can ever apply to the three-year statute of repose in the Securities Act. *Fezzani v. Bear, Stearns & Co., Inc.*, 384 F. Supp. 2d 618, 632 (S.D.N.Y. 2004). The Supreme Court held in 1991 that “[b]ecause the purpose of the 3-year limitation is clearly to serve as a cutoff . . . tolling principles do not apply to that period.” *Lampf v. Gilbertson*, 501 U.S. 350, 363, 111 S.Ct. 2773, 2782 (1991). Some courts have held that *Lampf* holding does not apply to tolling under *American Pipe*, see, e.g., *Joseph v. Wiles*, 223 F.3d 1155, 1166-67 (10th Cir. 2000); *Official Comm. of Asbestos Claimants of G-I Holding, Inc. v. Heyman*, 277 B.R. 20, 31-32 (S.D.N.Y. 2002). However, neither the Supreme Court nor the Second Circuit has ruled on the issue. In any event due to Plaintiffs’ lack of standing to assert claims with respect to the New Offering, the statute of repose has not been tolled by the commencement of this class action.

specifically limited its ruling to circumstances in which class certification was denied on the basis of lack of numerosity:

at least where class action status has been denied solely because of failure to demonstrate that the class is so numerous that joinder of all members is impracticable, commencement of the original class suit tolled the running of the statute for all purported members of the class who make timely motions to intervene after the court has found the suit inappropriate for class action status.

American Pipe, 415 U.S. at 553, 94 S.Ct. at 766 (emphasis added). The Court also specifically noted that it was not addressing the circumstance of a named plaintiff that lacked standing to sue on behalf of a proposed intervenor. *Id.* (noting that “(m)aintenance of the class action was denied not for failure of the complaint to state a claims on behalf of other members of the class . . . not for lack of standing of the representative, or for reasons of bad faith or frivolity”) (emphasis added).

Nine years later, in *Crown, Cork & Seal v. Parker*, the Supreme Court extended its ruling in *American Pipe*. *Crown, Cork & Seal v. Parker*, 462 U.S. 345, 354, 103 S.Ct. 2392, 2397-98 (1983). As in *American Pipe*, the moving members of the rejected class sought to assert claims on behalf of themselves only, not on behalf of a purported class. *Id.* The court held that members of the initial putative class could either move to intervene *or* commence their own individual actions following denial of class certification. In a concurring opinion joined by two other Justices, Justice Powell noted that “the tolling rule of *American Pipe* is a generous one, inviting abuse,” and warned against “lawyers in a case of this kind [framing] their pleadings as a class action, intentionally, to attract and save members of the purported class who have slept on their rights.” *Id.* (Powell J., concurring) (citations omitted).

Consistent with Justice Powell’s warning, the Second Circuit in *Korwek v. Hunt*, held that the statute of limitations would not be tolled under *American Pipe* to allow putative class members to assert new class claims after certification of the original class was denied. 827

F.2d at 879 (Altimari, J.). The *Korwek* court held that allowing plaintiffs to “piggyback one class action onto another and thus toll the statute of limitations indefinitely” would be “inimical to the purposes behind statutes of limitation and the class action procedure” and would upset the balance between efficiency and fairness struck by the Supreme Court in *American Pipe*. *Id.*

Following *Korwek*, two courts in this Circuit have held that the *American Pipe* rule will not toll the statute of limitations on claims that the named plaintiffs in a putative class action lacked standing to assert. *See In re Colonial Ltd. Partnership Litig.*, 854 F. Supp. 64, 82 (D. Conn. 1994) (Cabranes, J.); *In re Crazy Eddie Sec. Litig.*, 747 F. Supp. 850, 856 (E.D.N.Y. 1990) (Nickerson, J.); *see also In re Elscint, Ltd. Sec. Litig.*, 674 F. Supp. 374, 378 (D. Mass. 1987).

In re Colonial was a putative class action in which the plaintiffs asserted claims of fraud in the selling of limited partnerships. As in this case, plaintiffs’ claims with respect to partnerships in which they did not invest were dismissed for lack of standing. A number of investors in those partnerships moved to intervene. The court dismissed the intervenors’ claims on statute of limitations grounds. *In re Colonial*, 854 F. Supp. at 78-79. Relying on *Korwek*, Judge Cabranes held that the “critical inquiry for determining whether the plaintiffs’ . . . claims . . . were tolled by the filing of the [the lead plaintiff’s] complaint is whether [the lead plaintiff] had standing to assert his claims.” *Id.* Because the lead plaintiff did not have standing to assert claims with respect to certain of the partnerships, the statute of limitations was not tolled for investors in those partnerships and, accordingly, the court dismissed the intervenors’ claims. *Id.*

Judge Nickerson also relied on *Korwek* in holding that the *American Pipe* tolling rule does not apply where claims in a previous class action had been dismissed for lack of standing. *In re Crazy Eddie Sec. Litig.*, 747 F. Supp. at 856. In *Crazy Eddie*, the plaintiffs were

asserting, among other things, that the defendant made false and misleading statements and omissions in connection with three public offerings. *Id.* at 853. After the court dismissed part of the complaint for lack of standing because the plaintiffs had not purchased the specific debentures at issue, the plaintiffs sought to amend the complaint, adding a new plaintiff with the requisite standing for those portions of the complaint previously dismissed. *Id.* at 855-56. The court ruled that the previously dismissed claims were now time-barred and that the *American Pipe* tolling rule did not apply because they had been dismissed for lack of standing. The court stated that “the [*Korwek*] court’s reasoning is equally applicable to a class action brought after a previous class has been dismissed for lack of standing. In fact the concern is perhaps more acute where the dismissal of the first action is for lack of standing.” *Id.* at 856.

The District of Massachusetts reached the same result in denying a motion to intervene by proposed plaintiffs to cure the named plaintiffs’ lack of standing. *In re Elscint, Ltd. Sec. Litig.*, 674 F. Supp. 374, 378 (D. Mass 1987). It held that allowing the filing of a purported class action to toll the statute of limitations on a claim for which the named plaintiffs have no standing “encourages attempts to circumvent the statute of limitations by filing a lawsuit without an appropriate plaintiff and then searching for one who can later intervene with the benefit of the tolling rule,” which the court held was “an impermissible use of intervention, akin to improper use of intervention to manufacture jurisdiction.” *Id.*

A court in this District did permit the intervention of a plaintiff to cure a lack of standing with respect to a claim under Section 12 of the Securities Act and held that the statute of limitations was tolled by the pendency of the putative class action. *In re Flag Telecom Holdings, Ltd. Sec. Litig.*, 352 F. Supp. 2d 429, 456 (S.D.N.Y. 2005) (Conner, J.), *abrogated on other grounds*, 574 F.3d 29 (2d Cir. 2009). The *Flag Telecom* court disagreed with Judge Cabranes’s

decision in *Colonial*, and, unlike the *Colonial* and *Crazy Eddie* courts, considered *Korwek* inapplicable to the issue. *Id.* Although the court purported to rely upon the principles of “efficiency and economy of litigation” underlying *American Pipe*, it failed to consider the potential for abuse identified by Justice Powell in *Crown, Cork*, the Second Circuit in *Korwek*, and the District Courts in *Colonial*, *Crazy Eddie*, and *Elscint*. In so doing, it did not honor the “careful balancing of the interests of plaintiffs, defendants, and the court system” reached in *American Pipe*. *Korwek*, 827 F.2d at 879. The Individual Defendants respectfully submit that the decision in *Flag Telecom* is flawed and should not be followed by this Court.³

C. The Court Lacks Jurisdiction to Toll the Statutes of Repose and Limitations With Respect to Claims for Which the Named Plaintiffs Did Not Have Standing

Finally, the Court lacks the power to toll the statute of repose or statute of limitations with respect to PERS’s claims because the Court never had jurisdiction over those claims. As this Court noted in ruling on the motion to dismiss, “Article III of the Constitution requires a plaintiff to have standing before the plaintiff may maintain a lawsuit.” Mem. Op. at 6.

³ In another case, *In re IPO Sec. Litig.*, No. 21 MC 92, 01 Civ. 9741, 01 Civ. 10899 (SAS), 2004 WL 3015304 (S.D.N.Y. Dec. 27, 2004) (Scheindlin, J.), the court applied *American Pipe* tolling to permit a putative class member to be substituted as lead plaintiff in the place of the previously appointed lead plaintiff, who had incorrectly alleged in the complaint against defendant Antigenics, Inc. – and stated in his PSLRA certification – that he had purchased securities issued by the defendant when he had not. The substitution motion was filed shortly after this error was discovered. Here, in contrast, it was clear on the face of the CAC, the initial complaints filed by Alaska Electrical Pension Fund and New Jersey Carpenters Health Fund, and Plaintiffs’ PSLRA certifications that Plaintiffs lacked standing to assert claims with respect to the New Offerings because Plaintiffs never alleged that they purchased securities from those Offerings. As a result, *In re IPO Securities Litigation*, has no applicability to PERS’s motion to be added as a named plaintiff on behalf of itself and the Intervenor Class. The court, in *dicta*, also referred to but did not apply the doctrine of equitable tolling. *Id.* at *7 n. 62. Here, where it was clear from the face of the complaints and PLSRA certifications that the offerings in which PERS purchased were not offerings in which Plaintiffs made purchases, there is no basis to equitably toll the statute of limitations. See *Johnson v. Nyack*, 86 F.3d 8, 12 (2d Cir. 1996) (holding that equitable tolling applies where plaintiff had been “prevented in some extraordinary way from exercising his rights” and the delay was not attributed lack of diligence by the plaintiff). Moreover, the statute of repose is not subject to equitable tolling. *Lampf*, 501 U.S. at 363, 111 S.Ct. at 2782.

Because standing “is a threshold constitutional requirement . . . [i]t cannot be dispensed with by styling the complaint as a class action.” *Id.* at 7-8. For the reasons the Court identified in its Memorandum Opinion, namely that it would violate the Rules Enabling Act to allow a Federal Rule of Civil Procedure to “abridge, enlarge or modify and substantive right,” *Id.* at 8, n 19, it would violate that Act if the filing of a putative class claim under Rule 23 for which the named plaintiff lacked standing were permitted to toll the statutes of repose and/or limitations for other potential class members, either as intervenors under Rule 24 or in separate actions. The Rules cannot confer power on a court with respect to a claim as to which the court lacks subject matter jurisdiction under Article III.

As the Second Circuit has noted, the statute of limitations may be tolled for other class members only by those “who have valid claims at the time the action is instituted.” *Escott v. Barchris Construction Corp.*, 340 F.2d 731, 733 n. 3 (2d Cir. 1965); *cf. Dietrich v. Bauer*, 76 F. Supp. 2d 312, 326 (S.D.N.Y. 1999) (a plaintiff may not use intervention in a class action as a procedure to “bootstrap” itself into standing it lacks under substantive law).

The Seventh Circuit, in *Walters v. Edgar*, specifically considered whether new plaintiffs could be substituted to maintain a stale class action claim after the original named plaintiffs were found to lack standing. 163 F.3d 430, 432-33 (7th Cir. 1998) (Posner, J.). The court held that new plaintiffs could not be substituted and the claim must be dismissed because jurisdiction under Article III had never attached and, therefore, the filing of the action did not toll the statute of limitations. *Id.* The Northern District of California, relying on Judge Posner’s decision in *Walters*, denied a motion by a plaintiff in a putative class to amend the complaint to add plaintiffs with standing to assert a state unfair competition claim following dismissal of that claim because the new plaintiffs’ claims were time-barred. *Palmer v. Stassinis*, 236 F.R.D. 460,

466 (N.D. Cal. 2006) The court held that “it would be beyond the constitutional power of a federal court to toll a period of limitations based on a claim that failed because the claimant had no power to bring it.” *Id.* at 466 n. 6.

CONCLUSION

For all the foregoing reasons, the Individual Defendants respectfully request that the Court deny the Motion to Intervene.

Dated: New York, NY
April 5, 2010

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